



## Reference Guide

---

SPENDING TIME IN THE US



Canadians who spend considerable amounts of time in the US should be aware of the US and Canadian income tax issues that can arise in these circumstances. This reference guide outlines these tax issues.

Please note:

- This reference guide is intended for Canadian individuals and couples who are not US citizens, Green Card holders, or certain former US citizens and long-term Green Card holders who expatriated after 2000 and before June 17, 2008 under an older version of the US expatriation rules. US citizens, Green Card holders and such US expatriate persons are subject to very different rules and should consult with qualified cross-border legal and accounting advisors regarding their situation.
- This reference guide deals only with applicable US federal income taxes in a general manner. It does not deal with state and local income taxes, which may also be applicable in certain circumstances.
- For more specific advice relating to your situation, you should consult with qualified cross-border tax professionals.

The following topics are covered in this reference guide:

- US federal income tax issues:
  - Deemed US resident?
  - Closer connection
  - The Canada-US tax treaty
  - Working in the US
- Canadian income tax issues
- Other matters to consider

## **US federal income tax issues**

### **DEEMED US RESIDENT?**

If you spend a significant amount of time in the US each year, you may be considered to be a US resident for US federal income tax purposes. This would mean that you may have to file US tax returns and would be subject to US taxes on your worldwide income. By comparison, if you are not considered to be a US resident, you would generally only be subject to US income tax on your US-source income.

Under the US income tax rules, you will be considered to be a US resident for any calendar year if one of the following applies to you:

- if you hold or obtain a Green Card during the year, or
- if you meet the substantial presence test – that is, if you were physically present in the US on at least 31 days in the current year and on at least 183 days in total during the three-year period consisting of the current year and the previous two years, counting as follows:
  - the total number of days spent in the US in the current year, plus
  - $\frac{1}{3}$  of the number of days spent in the US in the preceding year, plus
  - $\frac{1}{6}$  of the number of days spent in the US in the second preceding year.

As a result of this formula, it is possible that you may be considered to be a resident of the US in a particular year even if you were present in the US for less than 183 days in that year.

By way of example, if you spent 126 days in the US (slightly more than four months) in each of the current year (year 3) and the previous two years (year 2 and year 1 respectively), you would be considered resident in the United States in year 3 (126 days in year 3 +  $\frac{1}{3}$  of 126 days in year 2 +  $\frac{1}{6}$  of 126 days in year 1 = 189 days).

It is therefore important for individuals who travel to the US to track their time in the US and run the substantial presence test on an annual basis.

## CLOSER CONNECTION

If you meet the substantial presence test described above, but spent less than 183 days in the US in the current year, you may be able to avoid being treated as a US resident (and instead be treated as a non-resident alien) if you demonstrate to the US Internal Revenue Service (the IRS) that you have a closer connection to Canada than to the US – that is, that you maintained more significant ties with Canada than with the US. This is determined by a careful review of numerous facts and circumstances, such as the following:

- the country of residence you designate on forms and documents
- the types of official forms and documents you file in the US
- the location of:
  - your family
  - your permanent home

- your personal belongings, such as vehicles, furniture, clothing and jewellery
- your business activities
- where you hold a driver's licence
- where you are registered to vote.

Your permanent home can be a house, apartment or furnished room, and can be owned or rented. However, the home must be available to you at all times, continuously, and not only for short stays.

To claim a closer connection, you must file IRS form 8840 in the US by June 15 of the following year. This form must be filed for any year that you would otherwise be deemed to be resident in the US for US tax purposes. If the form is not filed, you may jeopardize your claim and trigger US income tax liability.

If you are found to have a closer connection to Canada, you would be considered to be a non-resident alien for US income tax purposes, and would be subject to US tax only on your US-source income, as described below.

Note that you cannot claim a closer connection if either of the following applies:

- you personally applied, or took other steps during the year, to change your status to that of a permanent US resident
- you had an application pending for adjustment of your status during the current year.

## THE CANADA-US TAX TREATY

Even where you meet the above substantial presence test and spent 183 days or more in the US in the current year, you may be able to use the Canada-US Income Tax Convention (the Treaty) to maintain your Canadian residency status. However, this protection is not as broad as being treated as a non-resident using the closer connection rule described above, since you would have to file a US non-resident income tax return (IRS form 1040NR) within certain time limits to disclose your use of the Treaty.

There is an order to the factors that are used to determine an individual's residency under the Treaty. Each factor supersedes the subsequent factors – that is, once one of the determining factors is met in assessing residency, the subsequent factors become irrelevant. The factors are determined in the following order:

1. Location of your permanent home (whether owned or leased)

If, however, you have a home available to you in both countries, or in neither country, the next factor comes into play.

2. Where you have closer personal and economic ties

Items considered here include the location of your investment accounts, where your credit cards were issued, where your family and friends are located, what mailing address you use, where you have your medical coverage, where your driver's license was issued, the location of your club memberships and religious affiliations, etc.

3. Your habitual abode

This test can be thought of as where you tend to be found or where you spend most of your time.

4. Your citizenship

5. Competent authorities

This factor represents a last resort, where none of the above tests determine where you are considered resident (either because either countries come out equally or neither country seems to apply). In this situation, the Canadian and US governments are asked to jointly determine an individual's residency.

Even when the Treaty results in an individual being considered a resident of Canada, this is solely for the purpose of determining the individual's US income tax liability. The individual is still considered a US resident under other aspects of US law, which would have broad implications, including:

- US information reporting involving the individual's ownership of, transactions with, transfers to, and distributions from, certain non-US-resident corporations, partnerships or trusts
- US information reporting for gifts or bequests over a specified threshold that the individual has received during the year from non-US persons or estates
- US information reporting of non-US bank accounts and other financial accounts with a total value over \$10,000 that the individual owns or holds authority over, and
- determining if the Controlled Foreign Corporation (CFC) or Passive Foreign Investment Company (PFIC) rules apply to certain non-US-resident corporations in which the individual is a shareholder. This may also have implications for other shareholders of the corporation who are US persons.

As the penalties for non-compliance with these reporting requirements can be severe, cross-border tax professionals should be consulted to ensure timely and complete reporting.

## WORKING IN THE US

If you are an employee resident in Canada (and not a US citizen or Green Card holder) and you are sent to work temporarily in the US, your employment income for the time you were physically working in the US is US-source income. Accordingly, you may be subject to US federal income tax and, depending on the state involved, state income tax as well.

There is, however, some relief from US federal tax (though not US state tax) available under the Treaty if one of the following conditions applies:

- your income from that employment in the US is less than US\$10,000
- you were present in the US for less than 183 days in any 12-month period commencing and ending in the fiscal year, including work and non-work days, and your remuneration was not paid by, or on behalf of, a US resident, and is not reported as a deductible expense by a permanent establishment in the US.

If you qualify for relief under the Treaty, your employer must have you complete IRS form 8233 which the employer would then certify and submit to the IRS.

If you do not qualify under the Treaty, your employer may be required to withhold US tax from your earnings and report your income and the amount withheld to the IRS.

If you are self-employed, your US-source earnings are only taxable in the US if you have a permanent establishment in the US. Where your business involves providing services in the US, you are deemed to have a US permanent establishment if:

- the services are performed in the US by an individual (which could be you or an employee) who is present in the US for 183 days or more (including work and non-work days) in any 12-month period, and during that period the business derives more than 50% of its gross active business revenue from the individual's services in the US
- the services are provided in the US during a period of 183 days or more (counting only work days) in any 12-month period, by one or more persons, with respect to the same or connected projects for customers' resident in the US, or on behalf of a permanent establishment that the customer maintains in the US.

The US can tax the income attributable to the US permanent establishment, subject to limited exemptions under the Treaty.

Regardless of whether you qualify for relief under the Treaty, you are required to file a US income tax return (IRS form 1040NR) when you earn US-source income. Depending on the state you worked in, you may also have to file a tax return in that state.

## Canadian income tax issues

If you develop closer ties to the US than to Canada and, as a result, become resident in the US under the Treaty, you may also trigger unintended Canadian tax consequences.

If you are determined under a tax treaty to be resident in a country other than Canada and not to be resident in Canada, then for Canadian income tax purposes, you will be deemed to be a non-resident. Consequently:

- You would be deemed to have disposed of certain of your property in the year you were deemed to become a non-resident for proceeds equal to fair market value, which could trigger a significant Canadian tax liability. This is known as departure tax.
- You would also be subject to Canadian withholding taxes on your Canadian-source income.

Please see our reference guide on Ceasing Canadian Residence for a more detailed discussion of the departure tax.

## Other matters to consider

In addition to potential income tax issues, there are other matters that you may wish to consider in connection with spending time in the US. Some of these are outlined below.

## US VISA/IMMIGRATION LAW CONSIDERATIONS

Apart from US and Canadian income tax considerations, you should also consider US immigration law considerations if planning an extended trip to the US. Generally speaking, entry into the US by Canadians (that is, people who are Canadian residents and citizens) is by way of a verbal visa given by US border official, using their discretion. This verbal visa is generally sufficient for stays in the US not exceeding six months from the date of entry; however, the actual length of stay granted is determined by the granting official.

Staying in the US beyond your authorized period can have serious consequences, such as deportation and a limitation on your ability to return to the US. If you wish to extend a stay in the US you must apply for an extension with the nearest US Citizenship and Immigration Services office before the initially authorized period expires.

It is important to note that your time spent during “short trips” outside of the US may continue to count against your six month limit for US immigration law purposes. This is different from how things work for tax purposes, where the focus is on actual days spent in the US.

## HEALTH CARE

You should check the extent to which you have coverage through your provincial and private health plans for out-of country health care. Such coverage is generally quite limited, while the cost of health care in the US can be prohibitive. Accordingly, you should consider purchasing supplementary health coverage for the period of time that you will be out of Canada.

Here are some important factors to keep in mind when deciding on supplemental travel health coverage:

- Review the health insurance policy carefully before you buy it.
- Check in particular for the following to make sure that the policy meets your needs:
  - What coverage does it provide?
  - What are the limitations and exclusions?
  - What are the implications if you have a pre-existing health condition?
  - What is the maximum coverage provided?
  - In what currency is the coverage provided?
  - What is the deductible amount?
- Consider whether you should purchase multi-trip insurance, which may be worthwhile if you will be traveling out of Canada several times throughout the year.

## POWERS OF ATTORNEY

If you spend a considerable amount of time in the US each year, it may be advisable to ensure that you have appropriate documentation in place to appoint someone to act on your behalf in the event that you become unable to look after your financial matters or make health care decisions for yourself. This could arise as a result of illness, injury, or other cause.

You might therefore consider consulting with professional legal advisors in the US about whether your Canadian powers of attorney for property and for personal care would be adequate for use in the United States or whether you should have separate documents prepared.

## SEPARATE WILL TO DEAL WITH US PROPERTY

If you own real estate in the US, such as land, or a home, condominium, or other building, you may wish to consider having a separate will prepared specifically for use in the US to deal with your US assets.



Often referred to as a separate situs will, such a will can help to reduce difficulties that can arise in trying to probate a Canadian will in the US.

If you have a separate situs will prepared to deal with your US property, you should ensure that your Canadian and US wills are drafted appropriately so that they do not inadvertently revoke each other.

## CANADIAN AND US CUSTOMS AND BORDER RULES

Before you travel between Canada and the US, you should familiarize yourself with all Canadian and US customs and border-crossing rules and requirements that may apply to you. This might include, for example:

- Travel document requirements.
- What you are allowed to bring into the other country and what items are prohibited or restricted. Examples of prohibited or restricted items may include certain food items, plants, live animals, medications and alcoholic beverages.

## Conclusion

If you spend significant amounts of time in the US, you should closely monitor the amount of time you spend in the US each year. You should also run the substantial presence test every year, to ensure that you are not deemed to be a US resident for US tax purposes.

There are many complex issues and options to consider when dealing with the interaction of Canadian and US taxation. This is only a very brief overview of one aspect of these issues. We recommend that you obtain advice from qualified cross-border tax advisors to ensure that you optimize your Canadian and US tax situation.

If you own, or intend to acquire, residential real estate or other property in the US, other tax issues should also be carefully considered. Please refer to our reference guide on owning residential property in the US. You may also wish to refer to our reference guide on US Estate Tax.

---

March 2016

*Although this material has been compiled from sources believed to be reliable, we cannot guarantee its accuracy or completeness. All opinions expressed and data provided herein are subject to change without notice. The information is provided solely for informational and educational purposes and is not intended to provide, and should not be construed as providing individual financial, investment, tax, legal or accounting advice. Professional advisors should be consulted prior to acting on the basis of the information contained in this reference guide.*

© 2016 Assante Private Client, a division of CI Private Counsel LP. All rights reserved.