



CESTNICK

TAX MATTERS

Seven creative tax moves to make when markets are tanking

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My parents, like many, head south during winters. They recently returned home from Arizona. “Tim, it’s so cold here at home in the winter that I actually saw some of our politicians with their hands in their own pockets,” my father said.

Speaking of politicians reaching into pockets, I talked to my parents about the U.S. tax system. If you’re a snowbird returning home, you need to think about tax filings south of the border too. Let me share the highlights.

The test

Spending more than a certain number of days in the United States can lead to tax and information reporting requirements south of the border. The total matters a lot. Each year, you should do a simple math test at home. It’s called the Substantial Presence Test (SPT).

Here’s how: Add up the number of days you were in the U.S. in the current year, plus one-third of the days in the prior year, plus one-sixth of the days in the second prior year. If the total comes to 183 or more, and if you’ve spent at least

31 days in the U.S. in the current year, then you’ve met the SPT.

You need to count even partial days in the U.S. as one full day. Now, if you were in the U.S. between Feb. 1, 2020, and April 1, 2020, and intended to come home to Canada but couldn’t because of COVID-19 pandemic travel issues, you can exclude up to 60 days from the SPT calculation for 2020.

So, what if you’ve met the SPT? This means you’re considered to be a resident of the U.S. for tax purposes for the current year. The problem with this is that you’ll generally have to report your worldwide income for the year on a U.S. tax return. While you’ll be entitled to a foreign tax credit on your Canadian tax return for the U.S. tax you pay, this just complicates your tax filings immensely, and means that your tax dollars will be split between Canada and the U.S.

As an aside, if you keep your days in the U.S. to 120 or less each year, you’ll avoid being considered a U.S. tax resident under the SPT. But, if you’re like my parents, there’s no chance of convincing

them to come back after that short time. So, what else can be done?

The exception

If you meet the SPT, you can still avoid filing a full-blown U.S.-resident tax return and reporting all your income on that return if you're in the U.S. for less than 183 days in the current year, you maintain a "tax home" in Canada (a place where you regularly live) and you have a closer connection to Canada than to the U.S. You can demonstrate that closer connection if you have a home here that is available to you at all times, family and personal belongings here, and social, political, cultural or religious connections.

If you qualify for the exception (most snowbirds will if you're in the U.S. for less than 183 days each year), you can file U.S. tax Form 8840 (Closer Connection Exception Statement for Aliens) and avoid filing a U.S. tax return as a U.S. tax resident. For most snowbirds, the due date for Form 8840 is June 15 each year, so the deadline is June 15, 2022, for a 2021 Form 8840.

Some snowbirds might be required to file a U.S. non-resident tax return (called Form 1040NR) if they have certain types of U.S. income (such as rental income, in some cases). If you have to file Form 1040NR, then your Form 8840 should be attached to it.

I'll talk more about filing Form 1040NR next week. For now, just realize that most snowbirds won't have to file Form 1040NR, in which case you should send your Form 8840 by itself to the Internal Revenue Service (IRS) south of the border by the June 15 deadline.

The treaty

One last point. If you meet the SPT and don't qualify for the closer-connection exception, you can still refer to the Canada-U.S. tax treaty to avoid tax residency in the U.S. The treaty has tiebreaker rules that could deem you to be resident in Canada and not in the U.S., avoiding the need to file a tax return as a U.S. resident.

The tiebreaker rules look at your permanent home, centre of vital interests, your habitual abode and citizenship to determine where you should be considered a tax resident. But it's best not to rely on the treaty because you may still be treated as a resident of the U.S. for other provisions of U.S. tax law, which can mean other information reporting requirements.

There's more to say, so I'll finish off this topic next week.

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