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TAX MATTERS

Snowbirds face a potpourri of tax issues

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I've got a friend who's trying to make it big as a movie producer. His latest idea is a thriller about a couple who are snowbirds. They look innocent but are really deadly fugitives on the run, wreaking havoc in their vacation home neighbourhood. "What's going to be title of the movie?" I asked. He replied: "Snowbirds: They're back. And they're a year older."

Last week I wrote about snowbirds who may have returned home and could face U.S. tax issues. If I were to write a script, I'd call the movie "Snowbirds: They're back. And they owe taxes." It would be scarier than any thriller my friend might produce. Today, I want to finish the conversation about snowbirds and U.S. tax issues to think about.

Owning property

Do you own a vacation property in the United States? If so, do you rent it out? If not, it's a personal-use property, which will simplify your tax filings because there won't be any rental income for the U.S. to tax. Further, you'll avoid having to report the property on Form T1135, which is filed with your Canadian tax return annually.

But if you do rent the property, your gross rental income is generally subject to a 30-per-cent flat withholding tax. To avoid this, you can elect to treat your U.S. rental income as "effectively connected with a U.S. trade or business" and instead report your rental income on a U.S. tax return (Form 1040-NR if you're not a U.S. tax resident). If you do make this election, you can deduct expenses against your rental income and you'll only pay tax (at graduated rates) on any net rental income – which is typically reduced to zero after deductions, including depreciation (which is a mandatory deduction in the U.S.). The deadline for filing U.S. Form 1040-NR is typically June 15 each year.

Selling property

Whether your U.S. property is for personal use, generates rental income or is used for both, you'll generally be subject to a 15-per-cent withholding tax (with some exceptions) on the gross sale price if you sell your property. You'll also need to report the sale on a U.S. tax return (again, Form 1040-NR if you're a Canadian, but not U.S., tax resident). If the 15-per-cent withholding tax is higher than your actual tax liability on any capital gain in the U.S., you can expect a refund when the Internal Revenue Service processes your U.S. tax return.

If you expect your U.S. tax bill to be less than the 15-per-cent withholding tax, you can apply to the IRS for a withholding certificate to reduce or eliminate the withholding tax. You can make this application by filing U.S. Form 8288-B with the IRS before the closing date on the sale of your property. You'll also have to report the sale of your U.S. property in Canada, and if you did pay tax in the U.S., you can claim a foreign tax credit on your Canadian tax return for these taxes.

State taxes

I should mention that some states, like Florida, don't have a personal income tax. But others, such as Arizona or California, do. Some of the rules that might allow you to escape filing tax returns federally in the U.S. may not apply in the state where you spend time. So, make sure you speak to a tax pro about this.

U.S. estate tax

In addition to income tax, owning U.S. real estate can give rise to U.S. estate taxes when you pass away. The good news? If your worldwide estate is worth less than US$12.06-million in 2022, then the U.S. estate tax exemption will allow you to avoid this tax. But if your worldwide estate is more than this, you need to carefully consider how you structure ownership of your U.S. property (owning the property in a special trust, for example, can allow you to avoid the U.S estate tax). The U.S. estate tax rates range from 18 per cent to 40 per cent of your property's value.

U.S. immigration

In most cases, Canadian citizens don't require visas to enter the United States, either from Canada or from other countries. There are, however, some exceptions. Those intending to immigrate to the U.S., for example, would need to qualify for a visa before entering the country.

Canadians can generally stay in the U.S. for up to six months at the time of entry. Requests to extend a stay can be made to the U.S. Citizenship and Immigration Services. Counting your days in the U.S. for income tax purposes (which I talked about last week) is different than keeping track for immigration purposes. That is, the rules around what days can be excluded, etc., can be different in each case.

Finally, I've simplified the rules here, so speak to a tax pro to talk about how you might be affected.

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