

TaxTalk

U.S. Tax Update – Individuals - 2010

*If you or any of your colleagues would prefer to receive an electronic copy of TaxTalk in PDF format instead of a paper copy, please send an email to taxtalk@mgca.com
To review previous issues of our TaxTalk, please visit our website at www.mgca.com*

There have been a number of U.S. tax developments in recent years as well as changes to the Canada–United States Tax Convention (Treaty)¹. These changes will affect Canadian residents who may be required to file U.S. income tax returns or who may be carrying on business in the U.S. In addition to the recent changes, many of the tax reduction measures introduced in the U.S. Economic Growth and Tax Relief Reconciliation Act of 2001² (“Economic Growth Act”) and the Jobs and Growth Tax Relief Reconciliation Act of 2003³ (“Jobs and Growth Act”) will be automatically repealed at the end of 2010.

¹ On September 21, 2007, the Fifth Protocol to the Canada–United States Tax Convention was signed by both Canada and the U.S. It was ratified and entered into force on December 15, 2008.

² On June 7, 2001 the Economic Growth and Tax Relief Reconciliation Act of 2001 came into law and introduced several significant tax reduction measures for individuals. These tax measures, however, are **not** permanent – they are scheduled to expire on December 31, 2010. Due to procedural obstacles in the Senate when the Act was introduced, a “sunset provision” was included in the Economic Growth Act, which repeals the measures introduced in the legislation effective January 1, 2011. Barring action by the U.S. Congress before this time, after December 31, 2010, the tax laws will revert to the pre-2001 provisions, as if the Economic Growth Act had never existed.

³ On May 28, 2003, the Jobs and Growth Tax Relief Reconciliation Act of 2003 introduced additional tax cuts for both individuals and corporations, and accelerated the phase-in of various measures introduced in the Economic Growth Act. However, these measures are also only temporary. Some of the measures included in the Jobs and Growth Act were scheduled to be in place for as little as two years while some are scheduled to be in place for up to 10 years.

On December 6, 2010, President Obama announced a "framework" agreement with the Republican Congressional leadership on several tax cuts otherwise scheduled to be repealed at the end of 2010². If enacted, the “2010 framework agreement” extends the tax cuts introduced by former President Bush for an additional 2 years and includes the reinstatement of the estate tax for 2011 and 2012, with an exemption amount of US\$5 million and a maximum tax rate of 35%.

This TaxTalk discusses some of the changes in the U.S. laws and to the Treaty, together with various U.S. reporting requirements relevant to Canadian resident/citizens and U.S. citizens living in Canada. A detailed index of the specific topics discussed can be found on the last page of this TaxTalk.

U.S. Income Tax Filing Requirements for Canadian Residents/Citizens

Certain Canadian residents may be required to file U.S. income tax returns. The list of Canadian residents includes Canadians who: [i] spend a good deal of time in the U.S., [ii] are members of partnerships that own U.S. real property interests, [iii] carry on a business in the U.S., [iv] are employed in the U.S., or [v] are beneficiaries of U.S. trusts.

In general, individuals who meet the “substantial presence” test⁴ are considered to be “resident aliens” for U.S. tax purposes. Resident aliens are generally subject to tax in the U.S. on their **worldwide income, and must⁵ file a U.S. income tax return.**

In contrast, **non-residents of the U.S.** (non-resident aliens) are subject to U.S. tax *only* on their U.S. source income and income effectively connected with a U.S. trade or business. For some types of income, e.g. dividend income, there is U.S. withholding tax, and it is not necessary for a U.S. tax return to be filed. For other types of U.S. source income / activity, e.g. rental income, sales of U.S. real estate and business income earned in the U.S., a non-resident is required to file a U.S. tax return in respect of these types of income. In the event an individual is a resident of both Canada and the U.S. there are “tie breaker” rules⁶ in the Treaty that determine which country the individual will be considered to be a resident for tax purposes.

The following provides comments that may be of interest to Canadian residents earning income in or from the U.S.:

a. U.S. Individual Taxpayer Identification Number (ITIN)

Many Canadian resident taxpayers must obtain an ITIN for U.S. tax purposes. All individuals [i] who are required to file U.S. income tax returns or [ii] who have filed U.S. withholding tax exemption certificates are required to have either a U.S. Social Security Number (SSN) or an ITIN.

⁴ Under the substantial presence test, an individual is considered to be a U.S. resident for U.S. tax purposes for a taxation year if the individual is physically present in the U.S. at least 31 days during the year **and** 183 days during the current and 2 preceding years, computed by counting all the days in the current year and 1/3 of the days present in the U.S. in the immediately preceding year and 1/6 of the days present in the U.S. in the second preceding year.

⁵ Administratively, the IRS allows Canadian residents who meet the substantial presence test to file a ‘closer connection’ (to Canada) exemption form in lieu of filing a U.S. tax return.

⁶ In general, the Treaty tie-breaker rules consider the person’s permanent home and/or the country with which his or her personal and economic relations are closer (centre of vital interests).

U.S. citizens, green card holders and individuals working in the U.S. under work visas or permits are issued SSNs. All other individuals, including non-residents, their spouses and dependants of U.S. residents who are not eligible to obtain a SSN, are required to obtain an ITIN. An ITIN is an identification number used for tax purposes only.

Individuals requiring an ITIN number must file Form W-7, *Application for IRS Individual Taxpayer Identification Number*, and provide original documentation⁷ to substantiate their foreign status and true identity to the Internal Revenue Service (IRS). The IRS has authorized “Acceptance Agents” who may certify and send the application to the IRS to obtain the ITIN for the taxpayer. **McCarney Greenwood LLP** is an IRS Certifying Acceptance Agent and can assist individuals in obtaining ITINs.

b. Canadians Working in the U.S.

Canadians who work or provide services **in the U.S.** may be subject to U.S. tax on the portion of their salaries and business incomes that are attributable to those services provided in the U.S. As such, they will be required to file a U.S. tax return.

As an Employee

Beginning January 1, 2009, individuals who spend **more than 183 days** in the U.S. in *any 12 month period commencing or ending in a particular fiscal year* (pursuant to recent changes to the Treaty) while working for a **Canadian employer** which does **not** have a place of business in the U.S., will be subject to U.S. tax on the portion of their salary earned while they are physically present in the U.S.

Canadians working in the U.S. for either a **Canadian or a U.S. employer** are liable to file a U.S. tax return and pay U.S. tax on the salaries related to the U.S. work, regardless of the time that they actually spend in the U.S. Both Canadian and U.S. employers are required to withhold U.S. employment taxes on salary earned while working in the U.S. These taxes withheld would be eligible for foreign tax credits in Canada to the extent there is Canadian tax payable on the U.S. sourced employment income.

⁷ *Requisite original documentation includes birth certificate and photo identification, e.g. a passport, a driver’s licence etc. A passport is the only stand-alone document accepted by the IRS.*

Although any U.S. tax paid can be claimed to reduce/eliminate Canadian tax due on this income, a U.S. tax return will still need to be filed and the U.S. taxes owing will need to be paid in respect of this income.⁸ The return is required to be filed by April 15th of the following year.

As an Independent Contractor

Canadians working in the U.S. as self employed or independent contractors will now be governed by the "Business Profits" article of the Treaty, which has been modified and expanded under the Fifth Protocol¹ to the Treaty. Previously, independent contractors and business enterprises were governed by the "Independent Personal Services" article of the Treaty.

Canadian independent contractors and business enterprises will only be taxable on business profits earned in the U.S. if they carried on business in the U.S. through a permanent establishment (PE). Only those business profits attributable to the U.S. PE will be taxable in the U.S. The Fifth Protocol expands the definition of "Permanent Establishment" such that independent contractors and all other business enterprises will now be deemed to have a PE in the U.S. *if*:

- a) the services are performed in the U.S. by an individual who is present in the U.S. for a period or periods aggregating *183 days or more in any 12 month period* **and** during that period or periods, more than 50% of the gross active business revenues of the independent contractor or business enterprise consists of income derived from the services performed in the U.S., **or**
- b) the services are provided in the U.S. for an aggregate of 183 days or more in any 12 month period with respect to the same or connected project for customers who are either residents of the U.S. or who maintain a PE in the U.S. and the services are provided in respect of that PE.

⁸Under the Treaty, Canadians who (i) earned compensation not exceeding US\$10,000, (ii) were not present in the U.S. more than 183 days in any 12 month period commencing or ending in the fiscal year **and** (iii) worked for a Canadian company that did not have a fixed place of business in the U.S., are **not** subject to U.S. taxation on these earnings. There is no requirement to file a U.S. tax return in respect of this income.

The expanded definition will *not* apply to any days of presence or services rendered in the U.S. prior to January 1, 2010. Going forward, it will be increasingly difficult for Canadian independent contractors and business enterprises to avoid having a PE in the U.S. if services are provided in the U.S. for 183 days or more.

c. U.S. Rental Income

Canadian residents who own U.S. property and rent the property out on a part-time or full-time basis are subject to U.S. income tax on the rental income. Rental income received by a Canadian resident is subject to a 30% U.S. withholding tax (based on the **gross** rental revenue) to be withheld by either the property management agent in the U.S. or the U.S. tenant. In order to avoid the withholding tax, a Canadian resident can apply for an ITIN (see discussion above) to file a U.S. non-resident income tax return (Form 1040NR) to report the U.S. rental income and expenses.

By filing the return, U.S. tax would apply to the **net** rental income. Any U.S. tax paid could be claimed on the taxpayer's Canadian tax return to reduce Canadian income tax payable in respect of the net rental income.

In many cases, Canadian residents would not owe any U.S. taxes with respect to U.S. rental properties since, under U.S. tax law, depreciation **must** be deducted each year in the determination of net rental income. This differs from Canadian tax law, under which tax depreciation (capital cost allowance) is a *discretionary* deduction and may only be claimed to the extent it reduces net rental income to nil. For U.S. tax filings, rental losses may be carried forward and may reduce future rental incomes and/or future gains, if any, on the ultimate sale of the property.

Important Note: *It is crucial to keep in mind that non-resident taxpayers (i.e. Canadians) are allowed to claim rental expenses only if their U.S. income tax return is filed on a **timely basis**. The IRS may deny the expenses if a return is late filed by more than 16 months. If the expenses are denied by the IRS, U.S. tax will be payable on the **gross** rental income received in the year, which could result in significant double-tax being payable in respect of the U.S. rental income.*

d. Gambling and Racing Winnings

In general, gambling and racing winnings paid to a non-resident of the U.S. are subject to a U.S. federal withholding tax of 30%. This tax is **not** eligible as a foreign tax credit to reduce Canadian income taxes payable since these types of winnings are not taxed in Canada. Canadian residents who have had U.S. tax withheld on their winnings may, however, be able to file a U.S. non-resident income tax return to report their net gambling income (i.e. winnings less losses) and claim a refund of part or all of the tax withheld on their winnings.

e. Capital Gains on Sales of U.S. Real Estate

When U.S. real estate is sold by a non-resident of the U.S., a 10% withholding tax⁹ will be applied to the **gross** proceeds. A U.S. non-resident income tax return must be filed to report any gain (or loss) on the disposition and compute U.S. taxes payable. The tax withheld on the sale will be credited against final U.S. taxes payable on the sale. Alternatively, any withholding tax in excess of the final U.S. taxes payable will be refunded.

f. Capital Gains on Sales of U.S. Investments

Sales of shares of U.S. corporations, regardless of where they are traded, are generally **not** subject to U.S. tax if sold by a Canadian resident under the Treaty. Thus, it is not necessary to file a U.S. tax return in respect of these disposals.

g. U.S. Social Security Benefits

Under the Treaty, Canadian residents who receive U.S. Social Security benefits are **not** subject to U.S. withholding tax on these amounts, i.e. the amounts are not taxable in the U.S. These U.S. benefits are, however, subject to Canadian income tax, but only on 85% of the benefits received.

Important Note: *Individuals who began receiving U.S. Social Security benefits prior to 1996, were only required to include 50% of the benefits in income prior to 1996; that is the 85% inclusion rate began in 1996. The 2010 Canadian Federal Budget reinstated the 50% inclusion rate for those individuals who started receiving U.S. Social Security benefits prior to 1996, effective January 1, 2010.*

⁹ Under certain circumstances, application may be made to the IRS to reduce the 10% withholding tax, e.g. when it is expected that the actual tax payable on the disposition will be less than the 10% withholding tax or when the purchaser plans to reside in the property.

U.S. Income Tax Filing Requirements for U.S. Citizens Living in Canada

Under **Canadian** tax law, only Canadian *residents* are subject to Canadian tax on their worldwide income, i.e. the Canadian tax system is based on residency. Non-residents of Canada (including Canadian citizens) are only subject to Canadian income tax on certain income from Canadian sources.

U.S. tax rules for individual taxpayers differ from the Canadian rules in that they are based on *residency and citizenship*. As such, **U.S. citizens living outside the U.S. are required to file** annual U.S. federal income tax returns and report their worldwide income to the IRS as if they were still resident in the U.S. An individual is generally considered to be a U.S. citizen if they were born in the U.S., or became naturalized in the U.S.¹⁰ These returns are due by June 15th of the following year. Interest, however, is charged from April 15th of the following year if there is a balance due on the U.S. income tax return and penalties are calculated from June 15th of the following year.

The obligation to file a U.S. tax return exists, even if the U.S. income tax liability is minimal (for instance, due to the foreign earned income exclusion and/or foreign tax credits). There is no statute of limitations for non-filing of returns by non-resident U.S. citizens - in theory, tax, penalty, and interest could be assessed for any prior delinquent years. If a U.S. citizen living outside of the U.S. fails to file a U.S. income tax return each year (whether there is a tax liability or not), because the statute of limitations on tax assessments will never run out, the IRS may require tax returns for *all of the years* of residency in Canada. The IRS may decide to assess tax based on their 'best estimate' of the expatriate's income. The interest and penalties on any old tax amounts owed would grow exponentially and after as little as 4 to 5 years may exceed the amounts of the original tax due.

If U.S. tax returns are filed each tax year while living in Canada, the statute of limitations in most situations for IRS audits will expire three years after the tax return for a particular year is filed. Therefore, the IRS cannot go back (absent fraud) and try to audit or change those returns at a later time. *It is suggested that U.S. tax returns should be filed even if there is no*

¹⁰ A green card holder is also subject to U.S. tax on their world wide income.

income or no taxes are owed in order to force the statute of limitations to start.

With increased technology and increased information sharing between Canada and the U.S., the chances of a non-filer being detected by U.S. tax authorities are mounting, e.g. especially at the time U.S. citizens living abroad renew their passports. With passport renewals, an IRS information return must be filed. Failure to file the return when requested by the IRS could result in criminal penalties.

Important Note: *In cases where a U.S. citizen living outside of the U.S. fails to file a U.S. income tax return each year (whether there is any income to report or not), because the statute of limitations on tax assessments will never run out, the IRS may require tax returns for all of the years of residency in Canada. We understand, however, that the current administrative policy of the IRS is to generally require returns from a non-filer for only **six years**, and the late-filing penalties could be waived if the individual voluntarily contacts the IRS with reasonable cause for their failure to file prior year returns.*

The following provides comments that may be of interest to **U.S. non-resident citizens** in respect of their requisite U.S. tax returns:

a. Foreign Earned Income Exclusion

In filing their U.S. returns, **non-resident U.S. citizens** may qualify to elect to exclude all or part of their "foreign earned income" from total income for U.S. tax purposes. The annual maximum exclusion amount is inflation adjusted and for 2010 is US\$91,500 (US\$91,400 in 2009). Foreign earned income includes wages, salaries and business income received for service provided in a foreign country. Interest and dividend income, pension or annuity payments and social security benefits are not exempt as they do **not** qualify as earned income.

Married taxpayers filing jointly may potentially exclude for 2010 up to US\$183,000 of foreign **earned** income. However, one spouse may not utilize the unused portion of the exclusion of the other spouse and, electing the exclusion may preclude eligibility for the U.S. Child Credit.

The election to exclude foreign earned income remains in effect for all subsequent years, unless it is revoked. A taxpayer who revokes an election however, cannot reelect to exclude foreign earned income, without the IRS's consent, again for five years after the year the election is revoked.

Important Note: *Even if the foreign earned income exclusion causes there to be no U.S. tax liability, a U.S. tax return must still be filed. Failure to file could lead to significant U.S. tax, penalties etc.*

b. Foreign Tax Credit

To avoid double taxation, U.S. citizens living in Canada are allowed to claim a foreign tax credit on their U.S. return for Canadian taxes paid on Canadian-source income to reduce/offset any U.S. tax that must also be paid on this income. The credit cannot exceed the Canadian taxes paid on the income. Any excess Canadian tax paid in any taxation year can be carried back one year and forward ten years for U.S. tax purposes to offset excess U.S. tax on the Canadian source income in the carryover years. In addition, U.S. citizens living in Canada are allowed to claim a foreign tax credit on their Canadian returns for U.S. taxes paid on U.S.-source income to reduce/offset any Canadian tax that must also be paid on this income.

c. Alternative Minimum Tax

The U.S. alternative minimum tax (AMT) attempts to ensure that U.S. citizens/green card holders with high gross income cannot avoid all U.S. tax liabilities by using exclusions, deductions and credits, similar, in concept, to the Canadian AMT. AMT can be fully reduced by foreign (e.g. Canadian) taxes paid.¹¹

d. Capital Gains and Capital Losses

The Canadian and U.S. tax rules with regard to capital gains and losses differ. As a result, additional tax may be incurred in respect of capital gains realized by U.S. citizens resident in Canada. The discussion below provides a brief overview of the Canadian and U.S. rules.

¹¹Prior to 2004 the reduction was restricted to 90% of the AMT liability, and thus, taxpayers in this situation ended up incurring U.S. tax equal to 10% of U.S. AMT. There was no remedy to avoid the remaining AMT at that time and Canada did **not** allow a foreign tax credit for this AMT paid.

In general, only one-half of capital gains are subject to Canadian income tax, regardless of how long the property is held. U.S. capital gains tax rules are more complex. If a property is held for a **short term**, i.e. 12 months or less, any gain, for U.S. tax purposes, is taxed as ordinary income at the individual's graduated marginal U.S. tax rate.

Long-term capital gains apply to assets held for *more than one year*. The maximum tax rate for 2010 is 15%. For taxpayers in the 10% or 15% income tax brackets the tax rate is 0%. Under the sunset provisions introduced in 2001, the maximum long-term capital gains tax rate was scheduled to go back up¹² to 20% from 15% for 2011. For individuals who are in the 15% tax bracket, the long-term capital gains rate was scheduled to increase to 10%. If enacted, the 2010 framework agreement reached on December 6, 2010 will postpone these tax rate increases for an additional 2 years.

Under Canadian tax law, a taxpayer may exclude any gain that arises on the sale of the taxpayer's "**principal residence**", without limitation. Under U.S. tax law, a taxpayer can exclude up to US\$250,000 (US\$500,000 for married couples filing joint U.S. returns) of any gain from the sale of their main home that is owned and used by the taxpayer as a principal residence for at least two of the five years prior to the sale. Gains in excess of the US\$250,000 (US\$500,000) are subject to tax in the U.S. at the capital gain rates indicated above.

Also, pursuant to Canadian tax law, capital losses that exceed capital gains in a particular year can either be carried back and applied to offset capital gains earned in the previous three years or carried forward indefinitely to reduce future capital gains. Under U.S. tax law, however, to the extent capital losses exceed capital gains in a year, up to an additional US\$3,000 of capital losses may be claimed against other income in the year. Any unused capital losses may be carried forward and applied against future capital gains or against US\$3,000 of other income in any future year (i.e. there is no provision to carry the loss back).

As the above discussion indicates, the Canadian and U.S. tax systems are not integrated with respect to capital gains; which can cause gains to be recognized in different tax years. As such, it is important for a

¹² For tax years beginning after 2010, the rules and rates in effect for capital gains before May 6, 2003 were scheduled to apply.

taxpayer realizing capital gains to obtain professional advice to minimize potential double-tax.

e. Dividend income

For U.S. tax purposes, "qualified dividends" received in 2010 are taxed at rates from 0% to 15%, the same as long-term capital gains, and "non-qualified dividends" are taxed as ordinary income at the highest marginal rate. Qualified dividends are generally dividends paid by public companies (U.S. and qualifying Canadian corporations). As with the long-term capital gains rates, in 2011, the taxation of all dividends was to revert back to the pre-May 6, 2003 rules; as a result, all dividend income (other than capital gain distributions from mutual funds) was to be taxed as ordinary income at the highest marginal tax rate, which was scheduled to increase to be as high as 39.6% in 2011. If enacted, the 2010 framework agreement reached on December 6, 2010 will postpone these tax rate increases for an additional 2 years.

f. Canadian Retirement Plans (RRSP, RRIF, RPP or DPSP)¹³

Although income earned within a retirement plan, such as an RRSP, RRIF, RPP or a DPSP, is *not* subject to Canadian tax until funds are actually withdrawn from these plans, there are no corresponding deferral provisions for this income under U.S. tax law. Thus, there can be a mismatching in the timing of income recognition in the two countries which could cause a double-tax situation.

The Treaty provides some protection against double-tax. Specifically, an election can be made to defer, for U.S. tax purposes, the recognition of income accrued in the retirement plan in the year until the funds are distributed from the plan. This is a one-time election for Canadian RRSPs or RRIFs, held by a U.S. citizen or U.S. resident.

This election is irrevocable. The election is included as part of Form 8891 *U.S. Information Return for Beneficiaries of Certain Canadian Registered Retirement Plans*. A separate Form 8891 must be filed each year, in a timely manner, with the

¹³ RRSP - Registered Retirement Savings Plan; RRIF - Registered Retirement Income Fund; RPP - Registered Pension Plan; DPSP - Deferred Profit Sharing Plan.

individual's U.S. tax return.¹⁴ Non-compliance could lead to penalties being assessed.

The election defers U.S. federal tax on the accumulations within the plan until there is a distribution from the plan. As such, the timing of Canadian and U.S. tax on any distribution will occur in the same year, thus providing for the ability to offset U.S. income tax with a "foreign tax credit" relating to the Canadian income tax paid in the year of withdrawal.

Important Note: *A distribution from the plan is defined by U.S. tax law, and not Canadian tax law. For example, a withdrawal under the Home Buyers' Plan from an RRSP is not taxed in Canada, but it is a taxable distribution for U.S. tax purposes. Although U.S. income tax will be payable on the distribution, there is no U.S. penalty applicable for early distributions, as can apply on withdrawals from U.S. retirement plans.*

When distributions are made from a retirement plan, all of the income and *capital* is taxed in Canada at ordinary tax rates. Meanwhile, the U.S. taxes the accumulation of income only. Thus, it is important that there is adequate tracking of contributions, capital trades, dividends and other income credited to the plan for annual currency translations. If these items are not tracked by year and historical exchange rates, the tax cost basis (and/or tax-paid capital) of the plan may be incorrect.

For U.S. citizens and residents, the disadvantage of *not making the election* on Form 8891 with respect to RRSPs/RRIFs is that they are required to include the income earned or realized annually within the plan in their U.S. tax return, and pay U.S. income tax thereon. The income does retain its character for U.S. tax purposes, so dividends, capital gains and losses are reported separately.

If Form 8891 is not filed, then there are other reporting requirements in the U.S., for **both the plan holder and the plan administrator**. Failure to file a report in a timely filed return (including extensions) carries a penalty, separate from the penalty assessable for a late filed return. The penalties for failing to file these reports as required can be significant - they can

¹⁴ Information required to be reported on Form 8891 includes the name and address of the plan administrator, the plan number and the closing balance of the plan on December 31 of each taxation year.

equal more than 50% of the *value* of the plan for each year of a filing deficiency.

All in all, it is prudent to file Form 8891 and elect to defer U.S. taxation on income earned in the Canadian deferred plan until distributions are made, so as to match-up the timing of the income recognition in both countries.

g. Canadian RESP and TFSA

The "tax-free" status of Registered Education Savings Plans (RESP) and Tax-Free Savings Accounts (TFSA) is only for Canadian tax purposes. The income earned in an RESP or TFSA will be treated as ordinary investment income¹⁵ for U.S. tax purposes for U.S. citizens and U.S. residents. Unlike income earned in registered retirement plans, which can be deferred for U.S. tax purposes, income earned in an RESP or a TFSA will be subject to U.S. tax in the year earned, regardless of whether any funds are withdrawn from the RESP or TFSA.

h. Automatic Extensions to File Individual Income Tax Returns

U.S. citizens living outside the U.S. have an automatic extension to file their U.S. federal income tax return until June 15th of the following year. Filing an extension will extend the time to file by four months until October 15th. The extension of time is only an extension of the time to file the return, not an extension of time to pay any outstanding taxes. Interest will be charged if there is a balance due from April 15th and penalties will be calculated from June 15th. It is recommended that taxpayers, who owe income tax but do not file until June 15th or later, pay their estimated tax balance due by April 15th. Estimated payments (U.S. tax instalments) for the following year should be made on a timely basis in order to avoid estimated tax penalties.

i. U.S. Tax Penalties and Interest

There are several U.S. tax penalties, such as "failure to file", "failure to pay", "accuracy related penalties", "failure to provide foreign information", etc. Also, the IRS charges interest on overdue taxes, including penalties.

¹⁵ U.S. tax law considers Canadian tax deferral plans to be grantor trusts. This allows the investment income to maintain its character as interest, dividends and capital gains for U.S. tax purposes.

The “failure-to-file” penalty is calculated based on the time from the deadline of the tax return (including extensions) to the date the tax return is actually filed. The “failure to file” penalty is 5% of the tax due for each month the tax return is late, up to a total maximum penalty of 25% of the tax.

The “failure-to-pay” penalty is calculated based on the amount of tax owed. The penalty is 0.5% for each month the tax is not paid in full to a maximum limit of 25% of the tax. The penalty is calculated from the original payment deadline (the original April 15th filing deadline) until the balance due is paid in full.

Federal tax underpayment interest is calculated based on how much tax is owed. Interest rates change every three months. Currently, the IRS interest rate for underpayment of tax is 4% per year. The interest is calculated for each day the balance due is not paid in full.

Additional Reporting Requirements for U.S. Citizens

a. Required Reporting by U.S. Persons of Foreign Financial Accounts

U.S. persons (being U.S. citizens, green card holders, U.S. residents and persons carrying on business in the U.S.) having a financial interest in, signature or other authority over financial accounts located in foreign countries at any time in the year with an *aggregate value greater than US\$10,000* are required to disclose these foreign financial accounts to the U.S. Department of the Treasury (U.S. Treasury). Form TD F 90-22.1 *Report of Foreign Bank and Financial Accounts* (FBAR) is required to be filed annually, on or before June 30 of the year following the applicable taxation year. Failure to file Form TD F 90-22.1 could result in a penalty of US\$10,000.

The term “financial account” can include not only bank and securities accounts but also RRSPs, RRIFs, EPSPs, DPSPs, RPPs, RESPs and TFSAs. There are other accounts that are frequently not thought about that are required to be reported. These include corporate accounts that you have signing authority on, a child’s “in-trust” account where you are named on the account as the guardian or trustee, and other accounts that you have signing or control authority over, even though you are not the owner of the assets in the account. An ‘account’ also includes life

insurance that has an investment component (a Universal Life Policy), GICs, private loans, and other instruments.

If a U.S. citizen is a beneficiary or trustee of a Canadian trust, Form TD F 90-22.1 (discussed above) must be filed with the U.S. Treasury. In addition, a special form disclosing a beneficial interest in a Canadian trust must be filed with the IRS. Failure to file any of these forms as required by law will be subject to penalties up to US\$10,000 or more. Once the IRS or the U.S. Treasury discovers the failure to file these forms, penalties might be assessed at any time in the future, i.e., there is no statute-barred period. The Treaty contains a provision which allows the Canada Revenue Agency (CRA) to share tax and financial information with the IRS and some of this information is shared on a regular basis. If these forms are not filed when required, it will be very difficult to avoid non-filing penalties at a later date.

The IRS and the Financial Crimes Enforcement Network (FinCEN) of the U.S. Treasury both issued additional guidance on the FBAR reporting in early 2010.¹⁶

b. U.S. Citizens in Canada with Ownership or Interest in a Canadian Entity

U.S. citizens in Canada who have 10% or more ownership interest in a Canadian or any non-U.S. corporation are required to file Form 5471 with the IRS reporting the ownership interest and selected corporate information. If the Canadian corporation is earning profits, it will be considered a “Controlled Foreign Corporation (CFC)” and it is possible that the U.S. citizen may also owe U.S. tax on the CFC’s earnings. In addition, Form 5472 must be filed by a U.S. corporation which owns at least 25% of a

¹⁶ The IRS issued Notice 2010-23 and Announcement 2010-16 with respect to FBAR reporting. The IRS has temporarily suspended the FBAR filing requirement for persons who are not U.S. citizens, U.S. residents, or domestic entities for 2009 and prior calendar years. In addition, the IRS has announced FBAR and Form 1040 filing relief for (i) certain persons having no financial interest but only signature authority over a foreign financial account by granting them a temporary extension to June 30, 2011 to report for 2009 and prior calendar years and (ii) persons having a financial interest in or signature authority over foreign commingled funds other than mutual funds, such as foreign hedge funds or private equity funds, who do not have to file the FBAR for 2009 and prior calendar years.

Canadian corporation, or by a Canadian corporation which is carrying on a trade or business in the U.S. to report the ownership and cross border transactions with the corporation.

c. Required Reporting by U.S. Persons of Certain Canadian Trusts

U.S. citizens living in Canada who have an interest in or who have had transactions with a Canadian trust may be required to file U.S. Forms 3520 and/or 3520-A¹⁷ to report their interest in a Canadian trust, and transfers to or withdrawals from a Canadian trust. For U.S. purposes, Canadian trusts that are required to be reported on these forms include a Registered Pension Plan (RPP), a Deferred Profit Sharing Plan (DPSP), an Employee Profit Sharing Plan (EPSP), etc. Significant penalties (up to 35% of the value of the property) generally applies if Form 3520/3520-A is not timely filed or if the information is incomplete or incorrect.

d. Foreign Account Tax Compliance Act (FATCA)

A new U.S. financial reporting rule will affect U.S. citizens living in Canada. The FATCA, enacted in March 2010 to generally come into effect for 2013, increases information reporting by U.S. taxpayers holding financial assets outside the U.S. and imposes stiff penalties for failure to comply. Under the FATCA, all foreign financial institutions (FFIs), including Canadian banks and financial institutions, are required to comply with the FATCA or be subject to the 30% withholding tax on interest and dividends paid to them by U.S. sources.

Compliance will result in providing financial information to the U.S. Treasury, including financial information of all U.S. citizens living in Canada, regardless of whether the individual has filed U.S. tax and information returns. *This rule will make it much easier for the IRS to identify U.S. citizens living in Canada who have not filed tax returns.*

The legislative intent of FATCA is to ensure that the U.S. government has a means to determine the ownership of U.S. assets held in foreign accounts by U.S. citizens. The name, address and taxpayer identification number (TIN) is required for every

account holder who is a specified U.S. person; and, in the case of any account holder who is a U.S. owned foreign entity, the name, address, and TIN of each substantial U.S. owner of such entity. The account number is also required to be provided, together with the account balance or value, and the gross receipts and gross withdrawals or payments from the account.

Starting with the 2011 income tax return, under the Hiring Incentives to Restore Employment (HIRE) Act, U.S. persons will be required to disclose detailed information about specified *foreign financial assets* whose aggregate value exceeds US\$50,000. A minimum US\$10,000 penalty could result from non-disclosure, and the statute of limitation period does not begin until the required disclosure is filed. This new reporting is separate from, and in addition to, the Form TD F 90-22.1 Report of Foreign Bank and Financial Accounts (FBAR) discussed above, which is required to be filed if the aggregate value of the foreign financial accounts exceeds US\$10,000. The definition of specified foreign financial assets is much broader than the definition of foreign financial accounts and includes foreign investments not held in or at a foreign financial institution.

Other Issues for U.S. Citizens

a. Canadian Tax on Roth IRAs

For U.S. income tax purposes contributions to a Roth Individual Retirement Account (Roth IRA) are not deductible from income and withdrawals are generally not taxable. However, for Canadian tax purposes, income earned in a Roth IRA is taxable each year.

Pursuant to recent changes in the Fifth Protocol, a Roth IRA will be considered a "pension" for purposes of the Treaty *provided no contributions are made by a U.S. citizen living in Canada to the Roth IRA after December 31, 2008*. As a 'pension', the Treaty makes it possible to elect to defer the taxation in Canada of income earned within a U.S. pension plan until such time as withdrawals are made from the pension plan. Accordingly, this election to defer the taxation of income can now be made with respect to a Roth IRA.

¹⁷ Form 3520 Annual Return to Report Transactions with Trust Foreign Trusts and Receipt of Certain Foreign Gifts and Form 3520-A Annual Information Return of Foreign with a U.S. Owner.

The election to defer Canadian tax on income accrued in a Roth IRA after December 31, 2008 must be made by April 30, 2011. It is one-time irrevocable election and must be made for each Roth IRA. The election would be valid for all taxation years.

b. Roth IRA Conversions in 2010

Under U.S. tax law, a traditional Individual Retirement Account (IRA) can be converted to a Roth IRA at any time provided the individual's Adjusted Gross Income (AGI) for the year does not exceed US\$100,000. Beginning in the 2010 tax year this maximum AGI limit is now waived.

A traditional IRA is similar to a Canadian RPP/RRSP where contributions are generally tax deductible and withdrawals are taxable. There are early withdrawal penalties if withdrawals are made before age 59½ (with some exceptions). The mandatory withdrawals start no later than age 70½ with the minimum payments set by age at the time of withdrawal. As discussed above, for U.S. tax purposes, contributions to a Roth IRA are *not* deductible from income, withdrawals are generally not taxable, and the investment income earned in the plan also accrues tax free. In this respect, a Roth IRA is similar to a Canadian TFSA.

A traditional IRA (tax deferred) can be converted to a Roth IRA (tax paid) but the conversion is a taxable event (but without any early withdrawal penalties if converted before age 59½). For 2010 conversions, the income inclusion (and taxes payable) is split equally between 2011 and 2012. The key restriction with respect to a Roth IRA is that any withdrawals in the first 5 years are taxable or if there are withdrawals prior to age 59½. There is no requirement to begin minimum payments at age 70½. The full Roth IRA (including all income earned) is subject to estate tax and the beneficiaries would then have to start taking the minimum mandatory withdrawals per year, based on their life expectancy.

For Canadian tax purposes, under the Treaty, withdrawals from traditional IRAs are taxable (similar to withdrawals from a Canadian RPP or RRSP). Withdrawals from Roth IRAs are not subject to Canadian tax provided they are not taxable for U.S. tax purposes (it is possible to have a portion of a Roth IRA taxable, in certain circumstances). CRA has stated that when a traditional IRA is converted to a Roth IRA, the Canadian tax will follow the U.S. tax treatment – i.e. the income is taxable in Canada in the

same year it is taxable in the U.S. (i.e. for 2010 conversion the income will be taxable in 2011 and 2012, when it becomes taxable under U.S. tax law). Canada will allow a foreign tax credit each year for the U.S. taxes paid.

When a traditional IRA is converted to a Roth IRA after December 31, 2008, the conversion will be treated as a contribution to the plan and the election to defer the Canadian tax on the income earned in the plan as discussed above cannot be made. All income earned or accrued in the Roth IRA after the conversion will be subject to Canadian tax.

c. Renouncing U.S. Citizenship or Surrendering a Green Card

In the last year, the U.S. has seen a noticeable increase in the number of non-resident U.S. citizens beginning the process to renounce their citizenship. Many feel that the U.S. government is making it ever more difficult for Americans living abroad, both in taxing them and increasing reporting requirements. In 2004, the U.S. Congress first introduced expatriate rules with respect to (i) U.S. citizens who wish to renounce their U.S. citizenship and (ii) U.S. Green Card holders who want to, or are required to, surrender their card. Under the 2004 rules, individuals may have had U.S. tax reporting obligations for up to ten years following expatriation from the U.S. if they met certain criteria.

For individuals who “expatriate” from the U.S. after June 16, 2008, the rules changed. After this date, expatriates may be subject to the “mark-to-market regime” under which the expatriate is “deemed” to have sold all of their property for fair market value on the day before they expatriate. The expatriate is subject to U.S. tax on any deemed but unrealized gain above US\$600,000. This US\$600,000 exclusion amount is annually adjusted by a cost of living adjustment factor for calendar years after 2008. For those who “expatriate” in 2010 the exclusion amount is US\$627,000. The mark-to-market regime applies to any U.S. citizen who relinquishes citizenship, any green card holder who wants to surrender their card, and any long-term resident who terminates U.S. residency, if such individual is a “covered expatriate.”

A covered expatriate is an expatriate that:

- (i) has a net worth of US\$2,000,000 on the date of expatriation,

- (ii) has an average annual net income tax for the five years prior to expatriation that exceeds a specific amount which is adjusted for inflation (US\$145,000 for the years 2009 and 2010), *or*
- (iii) fails to certify under penalties of perjury that they have satisfied all of the requirements in the Internal Revenue Code for the five years preceding the date of expatriation.

A detailed discussion of the various tax issues involved in expatriation is beyond the scope of this TaxTalk.

U.S. Estate and Gift Taxes in 2010 and 2011/12

2010 was a chaotic year for U.S. estate tax. Under the (2001) Economic Growth Act, the estate tax was repealed for 2010. For 2011, the estate tax rules were to revert to what they were in 2001, with an exemption of US\$1 million as compared to the 2009 exemption of US\$3.5 million. It was anticipated that changes would be made such that the 2010 and 2011 rules and rates would be similar to what they were in 2009; but alas, political bickering blocked any changes.

If enacted, the 2010 framework agreement with the Republican Congressional leadership announced by President Obama on December 6, 2010 will reinstate estate tax for 2011 and 2012 but with an exemption amount of US\$5 million and a maximum tax rate of 35%.

a. Overview of U.S. Estate Tax

Individuals who are Canadian residents and citizens who own property located in the U.S. can be subject to U.S. estate tax, even if they are not U.S. citizens. The estate tax applies to the gross value of the asset. U.S. property subject to U.S. estate tax includes tangible personal property and real estate located in the U.S., stock of U.S. corporations (even if held in a Canadian brokerage or RRSP/RRIF/TFSA account), U.S. property transferred in trust, U.S. intangible property (copyrights, trademarks etc), gifts within three years of death, U.S. pensions and annuities, debt obligations of U.S. persons and life insurance plans of U.S. persons issued by U.S. insurers.

U.S. "situs" property subject to U.S. estate tax does not include funds held in U.S. bank accounts by non-

U.S. citizens/residents (but not cash in safety deposit boxes), life insurance of non-U.S. citizens/residents and U.S. stock held by a non-U.S. corporation.

The estate tax is based on the **value of the assets at the time of death** less certain allowable credits. For 2009, a Canadian was entitled to an **estate tax credit**¹⁸ equal to the estate tax payable on a worldwide estate valued at US\$3.5million¹⁹. This is the same credit that U.S. citizens and U.S. residents were allowed. However, the estate tax credit for many Canadians is reduced – the credit must be prorated by the value of the Canadian decedent's U.S. estate (i.e. U.S. situated assets) over the value of the decedent's worldwide estate. The worldwide gross estate is determined under U.S. law and may include items such as insurance that are not normally included in a decedent's estate for Canadian tax purposes.

b. Estate tax in 2010 and 2011/12

As mentioned above, there is no U.S. federal estate tax on the estates of individuals who die in 2010; although it should be noted that as a result there are less favourable capital gains tax rules for estates.²⁰ On January 1, 2011, the federal estate tax was scheduled to automatically revert back to the rates in effect in 2001 with a top tax rate of 55% and an exemption of only US\$1 million. **However, under the 2010 framework agreement reached December 6, 2010, if enacted, for 2011 and 2012, the top tax rate will be 35% and exemption will be US\$5 million.**

¹⁸ *The credit offsets estate tax that would otherwise be due, and therefore provides the same relief for all taxpayers, regardless of the size of their estate.*

¹⁹ *The basic 2009 estate tax credit of US\$13,000 (equivalent to estate tax on the first US\$60,000 of U.S. property) is increased for Canadians under the Treaty to US\$1,515,800 (equivalent to estate tax on US\$3,500,000).*

²⁰ *Under U.S. estate tax rules, the cost basis of assets transferred to beneficiaries is generally "stepped-up" to the fair market value of the assets at the date of death. When the assets are sold, the gains that had accrued prior to death are not taxable to the beneficiaries. For 2010, however, there is no estate tax and, therefore, there is no step-up in the cost base for the beneficiaries. Accrued gains at the date of death in excess of US\$1.3 million will be subject to U.S. income tax to the beneficiaries when sold.*

c. U.S. Estate Tax - Examples

To illustrate the calculation of U.S. estate tax for a Canadian estate, please consider the following example and the computation of pro forma U.S. estate tax in different years based on the then and current rules:

At the time of Mr. Taxpayer's death

- gross value of Mr. Taxpayer's worldwide estate was US\$15,000,000, including a condo in Florida valued at US\$1,000,000 and U.S. shares valued at US\$200,000, for a total U.S. Gross estate worth US\$1,200,000.
- Mr. Taxpayer is a Canadian resident/citizen who has lived in Canada his entire life.

U.S. Estate Tax in 2009 - If he died in 2009, the exemption amount would have been US\$280,000 (*being* $US\$3,500,000 * 1,200,000/15,000,000$). The estate subject to tax would have been US\$920,000 and estate tax payable would have been approximately US\$315,000.

U.S. Estate Tax in 2010 - if he died in 2010, there would be no U.S. estate tax.

U.S. Estate Tax in 2011 or 2012 - If he dies in 2011 or 2012, the exemption amount would be US\$400,000 (*being* $US\$5,000,000 * 1,200,000/15,000,000$), since under the 2010 framework agreement, *if enacted*, the exemption amount increases to US\$5,000,000 from the US\$3,500,000 exemption amount in 2009. The estate subject to tax would be US\$800,000 and estate tax payable would be approximately US\$261,000, which is US\$54,000 lower than the amount computed for 2009.

If the 2010 framework agreement is not enacted, and if the estate tax rules do revert to what they were in 2001 (an exemption of US\$1 million and a top rate of 55%), then Mr. Taxpayer would incur significant estate tax on his death - approximately US\$395,000, which is US\$80,000 higher, than the amount computed for 2009.

In general, under the 2010 framework agreement, *if enacted*, **Canadians will not be subject to U.S. estate tax in 2011 and 2012 unless the value of their worldwide gross estate exceeds US\$5 million.** However, if a U.S. property estate exceeds US\$5 million **and** if U.S. property represents a relatively small proportion of the total estate, the credit prorating mechanism can reduce the estate tax

credit significantly, and cause a large U.S. estate tax liability, as illustrated in the example above.

U.S. estate tax can be *deferred* if property is left to the surviving spouse who is a U.S. citizen or to a qualified U.S. domestic trust (QDOT). A detailed discussion of planning in this area is beyond the scope of this TaxTalk.

Canada does not have estate tax. Instead, Canada's tax system requires recognition of accrued gains and losses on the death of a taxpayer, with the exception for any transfer of assets on death to a spouse (or spousal trust) at their tax cost. If gains are recognized by the deceased taxpayer in their final Canadian tax return, then Canadian income tax may be incurred in respect of these gains. As such, for many taxpayers, the Canadian and U.S. tax systems are not coordinated on death, and double-tax could arise.

There is potential **relief from the double-tax.** Canadian tax law allows U.S. estate tax to be deducted from a deceased person's Canadian tax otherwise payable in certain circumstances. In some cases, some relief from double-tax will be available, but in other cases it may not. As an example, a Canadian taxpayer may pay estate tax related to the *value* of the U.S. asset, but perhaps not have any Canadian tax related to the deemed disposal of the asset, either because there was no gain, or because the asset was transferred tax-deferred on death to the spouse (or spouse trust). In this case, there would be no credit in Canada allowed for U.S. estate tax paid in respect of the asset.

The U.S. estate tax rates schedule is provided as **Appendix 2** at the end of this TaxTalk.

d. Gift Tax

The U.S. transfer tax system is designed to tax gifts made during a person's lifetime so that such gifts will generally not escape the estate tax. The U.S. gift tax applies to all gifts made by U.S. citizens or domiciliaries, regardless of where they reside, where the recipients of their gifts reside, or where the gifted property is located. Taxpayers are currently allowed a lifetime gift tax exemption of US\$1 million before tax is paid on gifts. The US\$1 million exemption reduces a taxpayer's estate tax exemption on a dollar-for-dollar basis. The U.S. gift tax regime generally does not impact non-residents as long as they are not gifting tangible property located in the U.S.

All “gifts” of property, including money, are generally taxable gifts except for gifts made to spouses, charities or political parties and payments made for medical expenses or tuition. There is an annual exemption amount for gifts made to each individual. The exemption amount for 2010 is US\$13,000. Accordingly, in 2010, each individual (including a spouse) can make gifts up to US\$13,000 to any number of individuals during the year and these gifts would not be taxable gifts. The annual gift tax exemption amount does not reduce a taxpayer's US\$1 million lifetime gift tax exemption amount.

The gift tax rate is based on the cumulative amounts of taxable gifts made during one's life time. The maximum gift tax rate for taxable gifts is reduced from 45% to 35% for gifts made in 2010. Lower gift tax rates and no Generation Skipping Tax (GST) in 2010 have made lifetime gifts to grandchildren and distributions from non-GST exempt trusts attractive planning opportunities. As with the U.S. estate tax, under the sunset provisions of the 2001 Economic Growth Act, the top gift tax rate reverts back to 55% with a US\$1 million exemption, beginning in 2011.

Although not specifically addressed in the 2010 framework agreement reached on December 6, 2010, it is assumed the gift tax top tax rate will remain at 35% for 2011 and 2012 given the agreement, if enacted, extending the tax cuts introduced by former President Bush for an additional 2 years.

There have been several significant changes over the last few years to the U.S. tax landscape. The scrutiny and disclosure requirements are much more enhanced and the IRS is increasingly more aggressive in applying these new rules. New legislation continues to expand the IRS's capability to access information on U.S. citizens wherever they may be. These changes are far reaching and extend well beyond the U.S. borders. Significant penalties have been introduced to promote compliance by both U.S. persons and foreign financial institutions. Implementation of the FATCA rules (discussed above) will make it much easier for the IRS to identify U.S. citizens living in Canada who have not filed tax returns.

Appendix 1 - U.S. Individual Income Tax Rates

2009 U.S. Individual Income Tax Rates & Brackets

Rate	Single		Married filing jointly, Qualifying widow(er)	
	From	To	From	To
10%	US\$0	US\$8,350	US\$0	US\$16,700
15%	8,350	33,950	16,700	67,900
25%	33,950	82,250	67,900	137,050
28%	82,250	171,550	137,050	208,850
33%	171,550	372,950	208,850	372,950
35%	372,950	no limit	372,950	no limit

2010 U.S. Individual Income Tax Rates & Brackets

Rate	Single		Married filing jointly, Qualifying widow(er)	
	From	To	From	To
10%	US\$0	US\$8,375	US\$0	US\$16,750
15%	8,375	34,000	16,750	68,000
25%	34,000	82,400	68,000	137,300
28%	82,400	171,850	137,300	209,250
33%	171,850	373,650	209,250	373,650
35%	373,650	no limit	373,650	no limit

Appendix 2 - U.S. Estate Tax Rates in 2009 and Projected 2011/12

Estate Tax Rate Schedule for Taxable Estate Value exceeding the exemption amounts of US\$3,500,000 for 2009 and projected US\$5,000,000 for 2011/12				
NO ESTATE TAX IN 2010				
Taxable Estate Amount subject to tax		2009 Estate Tax on amount in column 1	2009 Tax rate on excess over amounts in column 1	2011/12 Tax rate on excess over amounts in column 1
Estate Value Exceeding	But not Exceeding			
US\$0	US\$10,000	US\$0	18%	18%
10,000	20,000	1,800	20%	20%
20,000	40,000	3,800	22%	22%
40,000	60,000	8,200	24%	24%
60,000	80,000	13,000	26%	26%
80,000	100,000	18,200	28%	28%
100,000	150,000	23,800	30%	30%
150,000	250,000	38,800	32%	32%
250,000	500,000	70,800	34%	34%
500,000	750,000	155,800	37%	37%
750,000	1,000,000	248,300	39%	39%
1,000,000	1,250,000	345,800	41%	41%
1,250,000	1,500,000	448,300	43%	43%
1,500,000	2,000,000	555,800	45%	45%
2,000,000	2,500,000	780,800	45%	49%
2,500,000	3,000,000	1,025,800	45%	53%
3,000,000		1,290,800	45%	55%

Note:

There is a surtax of 5% which would apply to estates whose value exceeds US\$10,000,000 up to a value of US\$17,184,000 which effectively phases out the benefits of the graduated tax rates.

Index

U.S. Income Tax Filing Requirements for Canadian Residents/Citizens	1
a. U.S. Individual Taxpayer Identification Number (ITIN).....	2
b. Canadians Working in the U.S.	2
c. U.S. Rental Income.....	3
d. Gambling and Racing Winnings.....	4
e. Capital Gains on Sales of U.S. Real Estate.....	4
f. Capital Gains on Sales of U.S. Investments	4
g. U.S. Social Security Benefits.....	4
U.S. Income Tax Filing Requirements for U.S. Citizens Living in Canada	4
a. Foreign Earned Income Exclusion.....	5
b. Foreign Tax Credit	5
c. Alternative Minimum Tax	5
d. Capital Gains and Capital Losses	5
e. Dividend income	6
f. Canadian Retirement Plans (RRSP, RRIF, RPP or DPSP).....	6
g. Canadian RESP and TFSA	7
h. Automatic Extensions to File Individual Income Tax Returns.....	7
i. U.S. Tax Penalties and Interest.....	7
Additional Reporting Requirements for U.S. Citizens	8
a. Required Reporting by U.S. Persons of Foreign Financial Accounts.....	8
b. U.S. Citizens in Canada with Ownership or Interest in a Canadian Entity.....	8
c. Required Reporting by U.S. Persons of Certain Canadian Trusts	9
d. Foreign Account Tax Compliance Act (FATCA)	9
Other Issues for U.S. Citizens.....	9
a. Canadian Tax on Roth IRAs.....	9
b. Roth IRA Conversions in 2010.....	10
c. Renouncing U.S. Citizenship or Surrendering a Green Card	10
U.S. Estate and Gift Taxes in 2010 and 2011/12.....	11
a. Overview of U.S. Estate Tax	11
b. Estate tax in 2010 and 2011/12.....	11
c. U.S. Estate Tax - Examples	12
d. Gift Tax	12
Appendix 1 - U.S. Individual Income Tax Rates.....	14
Appendix 2 - U.S. Estate Tax Rates in 2009 and Projected 2011/12.....	15

A memorandum of this nature cannot be all encompassing and is not intended to replace professional advice. Its purpose is to highlight tax-planning possibilities and identify areas of possible concern. Anyone wishing to discuss the contents or to make any comments or suggestions about this TaxTalk is invited to contact one of our offices.

Offices 10 Bay Street, Suite 600
 (Bay Street and Queen's Quay)
 Toronto, Ontario M5J 2R8
 Phone: 416-362-0515
 Fax: 416-362-0539

8501 Mississauga Road, Suite 100
 (Steeles Avenue and Mississauga Road)
 Brampton, Ontario L6Y 5G8
 Phone: 905-451-4788
 Fax: 905-451-3299

TaxTalk is prepared by our Tax Group (taxtalk@mgca.com)

Please visit our website at www.mgca.com.

McCarney Greenwood LLP is an independent member of Morison International.

MCCARNEY GREENWOOD LLP

DECEMBER 2010