

F.A.T.C.A. and the U.S./Canada I.G.A.

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F.A.T.C.A.: Brief History

- Foreign Account Tax Compliance Act (F.A.T.C.A.) became law in March 2010 as part of the HIRE Act.
- Addresses tax abuse by U.S. persons through the use of offshore accounts.
- Objective: automatic information reporting
- How to incentivize compliance on foreign financial institutions: impose 30% penalty withholding (WH) tax on any U.S. source payments.

F.A.T.C.A.

- Imposes 30% WH tax on certain U.S. source payments unless:
 - extensive information reporting with respect to non U.S. accounts held by certain U.S. persons is provided to the I.R.S. by non-U.S. financial institutions that have entered into an agreement with the I.R.S., or
 - by governments that have entered into an I.G.A. with the U.S.
- Imposed on F.F.I.s or certain N.F.F.E.s.

F.A.T.C.A.

WH Tax

- Generally, anyone who makes withholdable payments to a non-U.S. entity is subject to withholding requirements, unless:
 - The non-U.S. entity is a P.F.F.I.
 - The non-U.S. entity is an N.F.F.E. with no U.S. substantial owners; or
 - The non-U.S. entity is excepted from withholding due to existence of an I.G.A.
- If no U.S.-source income, subject to an anti-abuse rule relating to foreign pass-thru payments, no F.A.T.C.A. WH is required, however, WH agent may need verification as to status of payee.

Canada / U.S. IGA

- I.G.A.s
 - An I.G.A. overrides the F.A.T.C.A. Code & regulations.
 - If an I.G.A. is on point, apply I.G.A.
- Canada signed an I.G.A. with the U.S. on February 5, 2014.

Canada / U.S. I.G.A.

- Model 1 Agreement
- Reciprocal
 - U.S. will report on certain accounts maintained by a U.S. financial institution held by residents of Canada and vice versa.
 - Institution to government reporting: instead of reporting to the I.R.S., institutions will report to the C.R.A. which will in turn, report to the I.R.S.
- Eliminates WH but not information reporting obligations
 - Exception: F.I. is in significant and long-term non-compliance with its obligations under the I.G.A.

Canada / U.S. IGA

Exemptions

- Certain accounts will not be reportable, including R.R.S.P.s, R.R.I.F.s, R.D.S.P.s and T.F.S.A.s.
- Smaller deposit-taking institutions such as credit unions with assets of less than \$175M will be excepted.

Canada / U.S. IGA

- Due Diligence Obligations of Each Canadian F.I.
 - Must identify its U.S. account holders under specified due diligence procedures.
 - Exceptions for low value accounts (e.g., \$50k or less in the case of a pre-existing individual account or \$250k or less in the case of a pre-existing entity account) as long as they remain low value.

What is an F.F.I.?

- Final Regulations:

- F.F.I. includes:

- ❖ Foreign banks and custodial institutions,
- ❖ Certain insurance companies, and
- ❖ Investment entities.

- Investment entities:

- Direct: an entity that primarily conducts as a business, on behalf of a customer:

- ❖ (1) Trading in money market instruments, foreign exchange, interest rate, index instruments, transferable securities; or commodity futures trading;
- ❖ (2) Individual or collective portfolio management;
- ❖ (3) Otherwise investing, administering, or managing funds, money or financial assets on behalf of other persons.

- Indirect: an entity that is professionally managed by a foreign bank, custodial institution, or another investment entity as described above and its gross income is primarily attributable to investing, reinvesting, or trading in financial assets.

What is an F.F.I.?

I.G.A.

- Canadian F.I. means:
 - Any F.I. that is resident in Canada, but excluding any branch of such FI located outside the U.S.
 - Any branch of a F.I. that is not resident in Canada, if such branch is located in Canada.
- F.I.:
 - Custodial Institution
 - Depository Institution
 - Investment Entity
 - Specified Insurance Company

What is an F.F.I.?

I.G.A.

- Investment Entity

- Any entity that conducts as a business (or is managed by an entity that conducts as a business) one or more of the following activities or operations for or on behalf of a customer:
 - (1) trading in money market instruments (cheques, bills, certificates of deposit, derivatives, etc.); foreign exchange; exchange, interest rate and index instruments; transferable securities; or commodity futures trading;
 - (2) individual and collective portfolio management; or
 - (3) otherwise investing, administering, or managing funds or money on behalf of other persons.
- Interpreted in a manner consistent with similar language set forth in the definition of “financial institution” in the Financial Action Task Force Recommendations.

What is an N.F.F.E.?

Final Regulations

- Any of those non-U.S. entities that do not qualify as an F.F.I. are N.F.F.E.s.
- Excepted N.F.F.E.s are not subject to F.A.T.C.A. withholding or reporting (other than certification as to their own F.A.T.C.A. status: W8). Includes:
 - Certain publicly traded corporations and affiliates;
 - Active N.F.F.E.s; and
 - Certain nonfinancial entities.

What is an N.F.F.E.?

Final Regulations

- “Active N.F.F.E.s” which are generally operating companies in which <50% of the N.F.F.E.s gross income is passive and <50% of assets are those that produce or are held for the production of passive income.
- Passive N.F.F.E.s are those N.F.F.E.s that are *not* “excepted N.F.F.E.s”.
- Required to report information on their substantial U.S. owners to withholding agents or to certify that they have no substantial U.S. owners to an applicable withholding agent.

What is an N.F.F.E.?

Methodology Under Canada / U.S. I.G.A.

- Definitions link to final regulations
- Determine if Passive N.F.F.E.
- Determine if Passive N.F.F.E. has one or more Controlling Persons as determined under A.M.L./K.Y.C. procedures
- Determine if Controlling Person is a U.S. Person
- If so, treat as U.S. Reportable Account

What Information Must Be Provided Under Canada / U.S. I.G.A.?

Controlling Persons

- The term “Controlling Persons” means the natural persons who exercise control over an entity. In the case of a trust, such term means the settlor, the trustees, the protector (if any), the beneficiaries or class of beneficiaries, and any other natural person exercising ultimate effective control over the trust, and in the case of a legal arrangement other than a trust, such term means persons in equivalent or similar positions.
- The term “Controlling Persons” shall be interpreted in a manner consistent with the Financial Action Task Force Recommendations.

The Result of FATCA

The Impact

Registration Timeline

Year	Date	Who?	What?
2014	January 1	Financial institutions	Official opening date to register and obtain Global Intermediary Identification Number (GIIN)
	June 2		First Registered FFI list published – updated monthly thereafter

Exception: FFIs in Model 1 IGAs jurisdiction have more time register and be listed since withholding agents are not required to confirm GIINs before January 1, 2015

Withholding Timeline

Year	Month/ Day	Who?	What?
2014	July 1	By withholding agents	30% U.S. withholding tax will apply to payments of certain U.S. source income made to FFIs, unless FFI establishes by registration that it is: <ul style="list-style-type: none">- A participating FFI (PFFI)- An FFI in a jurisdiction with a Model 1 IGA treated as in effect, or- A low risk FFI

Reporting Timeline

Year	Month/Day	Who?	What?
2015	September 30	FFIs in Model 1 IGA jurisdictions	With respect to 2014 (individuals), (1) Account holder's name; (2) Account holder's U.S. TIN; (3) Account holder's address; (4) Account number (5) Balance or value (6) For accounts held by recalcitrant/non-consenting account holders; report aggregate number and balance or value.
	September 30	FFIs in Model 1 IGA jurisdictions	- With respect to 2015, everything reported in (1) through (6) for 2014. (7) Income paid (except certain gross proceeds from the sale or redemption of property).

Reporting Timeline

Year	Month/Day	Who?	What?
2017	September 30	FFIs in Model 1 IGA jurisdictions	- With respect to 2016, everything reported in (1) through (7) for 2015 (8) Gross proceeds paid to custodial accounts
After 2017	September 30	FFIs in Model 1 IGA jurisdiction	- With respect to previous year, everything reported in (1) through (8) for 2016.

What Information Must Be Provided Under Canada / U.S. I.G.A.?

Canada to U.S.

- (1) The name, address, and U.S. TIN of each Specified U.S. Person and, in the case of a Non-U.S. is identified as having one or more Controlling Persons that is a Specified U.S. Person, the name, address, and U.S. TIN (if any) of such Entity and each such Specified U.S. Person;
- (2) the account number;
- (3) the name and identifying number of the Reporting Canadian Financial Institution;
- (4) the account balance;
- (5) in the case of any Custodial Account:
 - (A) the total gross amount of interest, the total gross amount of dividends, and the total gross amount of other income generated; and
 - (B) the total gross proceeds from the sale or redemption of property paid or credited to the account during the calendar year or other appropriate reporting period
- (6) in the case of any Depository Account, the total gross amount of interest paid or credited; (7) All other accounts, the total gross amount paid or credited to the account with respect to which the Reporting CA FI is the obligor or debtor, including the aggregate amount of any redemption payments made to the Account Holder during the applicable reporting period.

What Information Must Be Provided Under Canada / U.S. I.G.A.?

U.S. to Canada

- (1) the name, address, and Canadian TIN of any person that is a resident of Canada;
- (2) the account number;
- (3) the name and identifying number of the Reporting U.S. Financial Institution;
- (4) the gross amount of interest paid on a Depository Account;
- (5) the gross amount of U.S. source dividends paid or credited to the account; and
- (6) the gross amount of other U.S. source income paid or credited to the account.

- U.S. Citizens can no longer hide!
- Information will be available to the IRS (see Timelines)
- Recommend to file BEFORE the IRS comes knocking on your door!
- Who and what needs to be filed?

Who is Caught with U.S. Filing Requirements?

- United States citizens – who is a citizen?
- Green card (permanent resident aliens)
- Non-resident aliens who have met the substantial presence test
- Dual status (arriving) non-resident aliens who make the first year election to be treated as a resident

Who is Caught with U.S. Filing Requirements?

U.S. citizen

Not elective provisions – you are a U.S. citizen if:

- 1) you were born in the United States
- 2) you were born outside of the United States but to U.S. citizen parents (one or both)
 - Depends on date of birth
 - Depends on periods of U.S. residency of parent(s)

Who is Caught with U.S. Filing Requirements?

- Permanent resident aliens “green card” holders
- Those who meet the substantial presence test
 - Number of days in current year
 - Number of days in prior year x 1/3
 - Number of days in second prior year x 1/6
- Residents are taxable on their world wide income
- Closer connection statement
- Reliance on treaty

What needs to be filed?

- Tax Return – Form 1040
- FinCEN Form 114, “*Report of Foreign Bank and Financial Accounts*” (aka FBAR)
 - Not part of the income tax return – separate filing
 - Imposed under the U.S. Bank Secrecy Act
 - Used by the Financial Crimes Enforcement Network division (FINCEN) of the United States Treasury Department ***not the IRS***
 - This is the form that the Media hyped last year and caused panic with a lot of taxpayers

More Forms

- Form 5471, “*Information Return of U.S. Persons With Respect to Certain Foreign Corporations*”
- Form 5472, “*Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business*”

More Forms

- Form 8621, “*Return by a Shareholder of a Passive Foreign Investment Company or Qualified Electing Fund*”
 - Canadian mutual funds, corporate class investment, Canadian ETFs
 - Mark to market regime for publicly traded funds
- Form 3520, “*Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts*”
 - Transactions to/from non-U.S. trusts
 - Exclusion for RRSPs
 - TFSAs, RESPs, RDSPs
- Form 3520-A, “*Annual Information Return of Foreign Trust With a U.S. Owner*”

More Forms

- Form 926, “*Return by a U.S. Transferor of Property to a Foreign Corporation*”
- Form 8865, “*Return of U.S. Persons With Respect to Certain Foreign Partnerships*”
- Form 8938, “*Statement of Specified Foreign Financial Assets*” (the income tax equivalent to FBAR)
 - You could have been FBAR compliant but still not have reported the income to the IRS

U.S. Estate and Gift Tax Rules

- U.S. persons are subject to the U.S. Estate and Gift Tax Rules.
- Exemption amounts:
 - 2014 lifetime exclusion US\$5,340,000
 - Filing requirements if annual gift over US\$14,000 (2014) or if
 - NRA Spouse - US\$145,000 (2014)

Filing Options

Choices

- File under 2012 OVDP (8 years)
- File under streamlined filing procedure (3 years returns, 2009-2011, 6 years FBARs), 2012 on filed per normal rules
- File under general IRS policy (6 years returns, 6 years FBARs) – “Quiet Disclosures”
- Do nothing – FATCA risk
 - What’s the risk to the advisor?
 - They can’t hide anymore!

Streamlined Filing Procedures

- Effective September 1, 2012
- For “low risk” taxpayers
- Requires 3 years worth of returns
- Required 6 years with of FBARs
- Risk of no prosecution not guaranteed

OVDI

2012 Offshore Voluntary Disclosure Program

- Announced January 9, 2012, no announced ending date
- 8 years worth of returns
- Penalty - 27.5% of highest FBAR balance though possibility of reduced 5% penalty
- No relief from income tax, late filing, late payment and interest penalties
- Additional 20% under reporting penalty

Potential Civil Penalties

If taxes owed

- Late filing penalty
 - 5% per month up to a maximum of 25% - IRC §6651(a)(1)
- Late payment penalty
 - 0.5% per month up to a maximum of 25% - IRC §6651(a)(2)
- Accuracy related penalty
 - 20% (or 40%) – IRC §6662
- Fraud penalty – IRC §6651(f) or IRC §6663

Quiet Disclosures

- Still an option?
- Six-year reasonable cause approach
 - File six years returns
 - File six years FBARs
 - Include a reasonable cause letter
 - IRS trying to deter taxpayer from taking this approach

Potential Civil Penalties

Even if no taxes owed

- Form 5471, “*Information Return of U.S. Persons With Respect to Certain Foreign Corporations*”
- Form 5472, “*Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business*”
- Form 3520, “*Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts*”
- Form 3520-A, “*Information Return of Foreign Trusts With a U.S. Owner*”

Potential Civil Penalties

Even if no tax (continued)

- Form 8938, “*Statement of Specified Foreign Financial Assets*”
- Form 926, “*Return by a U.S. Transferor of Property to a Foreign Corporation*”
- Form 8865, “*Return of U.S. Persons With Respect to Certain Foreign Partnerships*”

Potential Civil Penalties

FinCEN Form 114, “*Report of Foreign Bank and Financial Accounts*” (formerly TD F 90-22.1)

- Imposed under Bank Secrecy Act (BSA) 31 U.S.C. §5321(a)(5)
- Willful violation
 - Greater of US\$100,000 or 50% of the account balance per violation
- Non-willful violation (not due to reasonable cause)
 - US\$10,000 per violation

Potential Criminal Penalties

Under the Internal Revenue Code

- Tax Evasion – IRC §7201
 - Prison term of up to 5 years
 - Criminal penalties up to \$250,000
- Filing a False Return – IRC §7206(1)
 - Prison term of up to 3 years
 - Criminal penalties up to \$250,000
- Failure to File – IRC §7203
 - Prison term of up to 1 year
 - Criminal penalties up to \$100,000

Potential Criminal Penalties

Under the Bank Secrecy Act

- Failure to File an FBAR
 - Prison term of up to 10 years
 - Criminal penalties up to \$500,000

Penalty Relief

- “First offence” relief
- Request penalty abatement for reasonable cause
- Appeal level
 - IRS has the ability to abate all penalties but can not abatement interest
 - Will not abate 100% of the failure to pay penalty

Problem Areas for Canadian Advisors

Common situations where U.S. tax may be payable

- Why do some U.S. (Canadian resident) taxpayers owe U.S. tax?
 - Canadian planning does not consider whether taxpayers are subject to U.S. rules
 - Some laws are just different!

Contribution to RRSP

- Income is deferred subject to treaty relief – Article XVIII(7)
- Form 8891, “*U.S. Information Return for Beneficiaries of Certain Canadian Registered Retirement Plans*” must be timely filed in order to defer current income
- Require Private Letter Ruling (PLR) to make retroactive election - cost
- Streamlined filing procedure providing relief

TFSA/RESP/RDSP

- Not covered under Internal Revenue Code
- Not covered under Canada-United States Tax Convention (1980)
- Income not deferred for U.S. tax purposes
- May be considered foreign trusts for U.S. tax purposes
 - Forms 3520, “*Annual Return to Report Transactions with Foreign Trust and Receipt of Certain Foreign Gifts*” and Form 3520-A, “*Annual Information Return of Foreign Trust With a U.S. Owner*” may be required to be filed

Capital Dividends

Under U.S. law, dividends follow a certain order of distribution :

- To the extent a company has earnings and profits a distribution is a taxable dividend
- Then a tax free return of capital, and
- Then a capital gain
- The effective U.S. federal tax rate of dividends may be as high as 23.8% (20% tax rate and 3.8% Medicare surtax)

Canadian Estate Freezes

Typical Canadian Estate Freeze

- Exchanging common stock for fixed value preferred stock
- In general, preferred stock not considered stock in these transactions – result taxable exchange
- Chapter 14 of the Internal Revenue Code
 - Preferred stock valued at zero
 - Transferor making a gift of entire value to new common shareholders
 - Can we give preferred stock value?

Stock Options

Potential Timing Mismatch

- U.S. Incentive Stock Options (ISOs)
 - Convert employment benefit to capital gain
 - Requires no disposition within 2 years of grant or 1 year from exercise – otherwise becomes NQO
 - Employment benefit – AMT adjustment
- U.S. Nonqualified Options (NQOs)
 - Very similar to Canadian rules
- IRC 83(b) election – ability to elect to “close” employment benefit at grant – no ability to undo if option never exercised

Capital Gains Exemption

- U.S. does not recognize the capital gains exemption
- May be issues with sourcing of gain – IRC §865(g) – at least a 10% tax must be paid (on gain computed under U.S. rules) to be considered foreign source gain

Allowable Business Investment Losses

- Remains a capital loss for U.S. tax purposes – no special treatment
- Capital losses can be used to offset up to \$3,000 of ordinary income (MFJ) or \$1,500 (MFS)
- Capital losses can not be carried back – just forward

Principal Residence Exemption

- Factual test
- Property must have been used as the principal residence for at least 2 years in the 5 year period ending on the date of sale
- \$500,000 of gain may be excluded (MFJ)
- \$250,00 otherwise (Single, MFS)

Flow-Through Shares

- U.S. does not recognize the flow through character of these shares
- With excess deductions, Canadian tax may be reduced so much that there is not enough to claim a foreign tax credit on U.S. return

Pension Income Splitting

- Canadian residents can elect to split eligible pension for Canadian tax purposes
- Assume mixed marriage – one spouse is a U.S. citizen, other spouse is a non-resident alien
 - U.S. citizen spouse transfers eligible pension to NRA spouse – reduces Canadian taxable income
 - Not a deduction for computing U.S. tax
 - May drive effective Canadian tax rate down

Lottery Winning and Gambling

- IRC §61 states “Except as otherwise provided in this subtitle, gross income means all income from ***whatever source derived...***”
- No exclusion for lottery winnings
- Gambling winnings also taxable
- Losses, however, may be deductible subject to certain limits

Use of LLCs

- Limited Liability Companies (LLCs) is a U.S. invention to solve a U.S. double tax problem
- U.S. does not have any dividend tax credit mechanism
- LLC treated as a disregarded entity or partnership – not taxed
- Unit holders
 - Taxed when income is earned
- Canada treats it as a corporation
 - Taxed on distribution

LLC Example

- Single owner LLC
- Carries on business in Florida
- Year 1 –
 - LLC earns active business income of \$1,000
 - No distribution
 - U.S. tax \$396 (maximum federal tax)
 - No Canadian tax as no distribution
 - May be able to claim ITA 20(12) deduction

LLC Example

- Year 2 –
 - No earnings
 - Retained earnings of \$604 distributed
 - No further U.S. tax
 - Considered a foreign source dividend for Canada taxed at marginal rates
 - Canadian tax = $\$604 \times 43.7\% = \264
 - No foreign tax credit as no U.S. tax paid in year
 - Total tax now \$660 – 66% of income!!
 - Didn't consider state tax

Estates and Trusts

- For Canadian purposes, an estate and trust are taxed the same
- In the U.S. a foreign estate is treated very differently than a foreign trust
- Distributable Net Income (“DNI”)
- Undistributed Net income (“UNI”)
 - No conversion of prior year income to capital
 - Subject to tax as ordinary income, loses character of income
 - Interest charge

Use of Holding Companies

- Controlled Foreign Corporation (CFC)
 - Subpart F income
 - ❖ Investment income
 - ❖ Personal services contract income
 - May not meet exemptions
 - ❖ Same country exception
 - ❖ High tax kick-out
- Passive Foreign Investment Company (PFIC)
 - Just penalty provisions
 - Canadian mutual fund trusts, corporate class

Gifts

- U.S. Citizen
 - 2014 lifetime exclusion US\$5,340,000
 - Filing requirements if annual gift over US\$14,000 (2014) or if
 - NRA Spouse - US\$145,000 (2014)
- Deemed Disposition for Canadian Purposes
 - Attribution of income

Basis Differences

- U.S. – default – FIFO
- Canada – weighted average ACB
- Other differences
- Foreign exchange differences

Under FATCA - What Do Foreign Entities Have To File and To Whom?

Form W-9

- W-9
 - WH agents may require W-9 from U.S. exempt recipients to overcome presumption of foreign status.
 - Includes:
 - ❖ Individual who is a U.S. citizen or U.S. resident alien.
 - ❖ A U.S. partnership, corporation, company or association.
 - ❖ Any estate other than a foreign estate.
 - ❖ A U.S. domestic trust.
- Not to be submitted directly to the IRS by individual or entity completing the form—to be submitted by WH agent.

Form W-8BEN

- Send to requester (WH agent/FFI), not to IRS
- Establishes that individual is not a U.S. person
- Claim that individual is the beneficial owner of the income for which Form W-8BEN is being provided or a partners in a partnership subject to withholding on distributive share of ECI; or
- Claim a reduced rate of, or exemption from WH as a resident of a foreign country with which the U.S. has an income tax treaty.
- W8-BEN-E will be used for entities when finalized (6 pages – <http://www.irs.gov/pub/irs-utl/formw8benentityexeccirculation2.pdf>)

Form W-8IMY

- For upper-tier partnerships, foreign simple or grantor trusts—intermediaries or foreign flow-thru entities.
- Not for beneficial owners.
- Not to be sent to the IRS—to be provided to the payor/WH agent.

FATCA's Impact on Corporations

- Required to certify its status to financial institutions with which it does business as a U.S. or non-U.S. person (W-8BEN-E (when finalized)/W-9).
- Must establish the status of each of the members of the corporate group to provide appropriate information.
- Should review each of the legal entities within a corporate group and testing of each entity under definitions and exclusions set out in the Regulations.

Trusts

- All foreign trusts that invest in the U.S. either directly or indirectly or through one or more private companies or collective investment vehicles will be affected.
- Must determine if a grantor or non-grantor trust.
- For a grantor trust, the **grantor** will be treated as the owner of the account.
- For a non-grantor trust, the **trust** itself will be considered the owner of the account.
- Whether it is a grantor or non-grantor trust determines whether an account has any substantial U.S. owners, and whether the account is exempt from due diligence requirements under the *de minimis* exceptions.

Is it a U.S. account?

- Non-U.S. grantor trusts with a U.S. grantor will be U.S. accounts.
- Accounts held by non-U.S. grantor trusts that have a non-U.S. grantor should be treated as owned directly by that non-U.S. grantor and, therefore, should not be U.S. accounts regardless of whether the trust makes distributions to U.S. beneficiaries.
- For non-grantor trust, use attribution rules to determine whether there is a substantial U.S. owner.

The Trustee

- The IRS will consider a trustee to be an FFI under the investment entity provision.
- An investment entity is one that engages primarily in trading, portfolio management, or investing, administering, or managing funds on behalf of its 'customers'.
- Unless a trustee earns at least 50% of its gross income from other sources, it will be treated as an investment entity.

Is The Trust an FFI or NFFE?

- Regulations imply that a grantor trust 'owned' for U.S. tax purposes by an *individual* is an account, not an FFI or NFFE.
- Non-grantor trusts and grantor trusts considered owned by entities must ascertain whether the trustee is an entity or an individual to determine whether the trust is an FFI or NFFE.
- Only an entity may qualify as an FFI.
- If an individual trustee manages the assets of a trust, the trust will be considered an NFFE.
- If its assets are managed by a trustee that is an investment entity then it is a FFI unless the trust holds assets that are primarily non-financial in nature such as real estate or art.

Family Trusts and Family Investment Entities

- Trusts of family investment entities that are “primarily” engaged in the investing in, reinvesting or trading of securities should be considered FFIs.
- Almost all family trusts would be FFIs, and only NFFEs if the trust or family entity does not ‘primarily’ engage in securities investments.

What to do: FFI Trusts

- Must report its substantial U.S. owners to WH agent/CRA.
- Substantial U.S. owner for investment entities (including trusts that qualify): a U.S. beneficiary with *any* interest whatsoever.

De Minimis for FFI

- If trust is an FFI and U.S. beneficiary received a small *discretionary* distribution, beneficiary must be reported to CRA, no *de minimis* rule.
- A U.S. person is not treated as a substantial U.S. owner if:
 - the FMV of the distributions to that person during the calendar year are \$5,000 or less and,
 - if the person is entitled to mandatory distributions, the value of that person's interest in the trust is \$50,000 or less.

NFFE Trust

- NFFE trust must provide the WH agent with specified information pertaining to any “substantial U.S. owners” or certify that it does not have any substantial U.S. owners.
- Substantial owner for trusts classified as NFFE: any specified U.S. person that holds directly or indirectly, more than 10% of the beneficial interest of the trust.
- An individual holds a beneficial interest if he or she has the right to receive, directly or indirectly, a mandatory or discretionary distribution from the trust.
- A person’s proportionate interest in a non-U.S. trust is aggregated with related persons who also hold beneficial interest in the trust.

Trusts

- Beneficial owners of income paid to a foreign simple trust are generally the beneficiaries of the trust, if the beneficiary is not itself a foreign partnership, foreign simple or grantor trust, nominee or other agent.
- The beneficial owners of a foreign grantor trust are persons treated as the owners of the trust.
- The beneficial owner of income paid to a foreign complex trust is the trust itself.

Trusts

- A **foreign trust** is *presumed* to have a U.S. beneficiary unless the U.S. person that directly or indirectly transfers property to a foreign trust submits information and demonstrates to the satisfaction of Treasury that:
 - Under the terms of the trust, no part of the income or corpus of the trust may be paid or accumulated during the tax year to or for the benefit of a U.S. person.
 - If the trust were terminated during the tax year, no part of the income or corpus of the trust could be paid to or for the benefit of a U.S. person.

De Minimis: NFFEs

- Do not have to be reported if , in the year in question, they receive less than \$5,000 in distributions and their mandatory distribution rights, if any, are worth less than \$50,000.

Estates

- Accounts held by estates are excepted from the definition of a financial account.

Partnerships

- Disregarded entities do not file any forms; instead, the owner of a disregarded entity must submit appropriate documentation.
- Nominees that hold a partnership interest on behalf of another person do not submit any withholding forms; instead, the beneficial owner of the interest must submit the form.

Partnerships

- U.S. partners may be required to sign a Form W-9 from its partners to overcome a *presumption* of foreign status and to avoid WH.
- Foreign partners to use W-8 or Form 8233 for Personal Services of a NRA individual.
- Beneficial owners of income paid to a foreign partnership are generally the partners in the partnership, provided that the partner itself is not a partnership, foreign simple or grantor trust, nominee or other agent.

Partnerships

- A partner that is a U.S. person must provide W-9.
- A partner that is a NRA must provide Form W-8BEN.
- A partner that is a foreign partnership must provide form W-8IMY.
- A partner that is a foreign corporation must provide a W-8BEN.

A change that may affect your non-U.S. clients

The Days Counting Test

The Days Counting Test

Substantial Presence Test vs. Immigration Counting Test

- Not the same!

Tax “Day Count” ≠ Immigration “Day Count”!

TAX

IMMIGRATION



182 Days in the Calendar Year

**180 Days in Rolling 12 Months –
Treaty, “Closer Connection”, and
“Substantial Presence” are irrelevant**

0 Days

120 Days

182 Days

365 Days

No action required

File Form 8840

Treaty tie-breaker exception may apply

Tax “Day Count” ≠ Immigration “Day Count”!

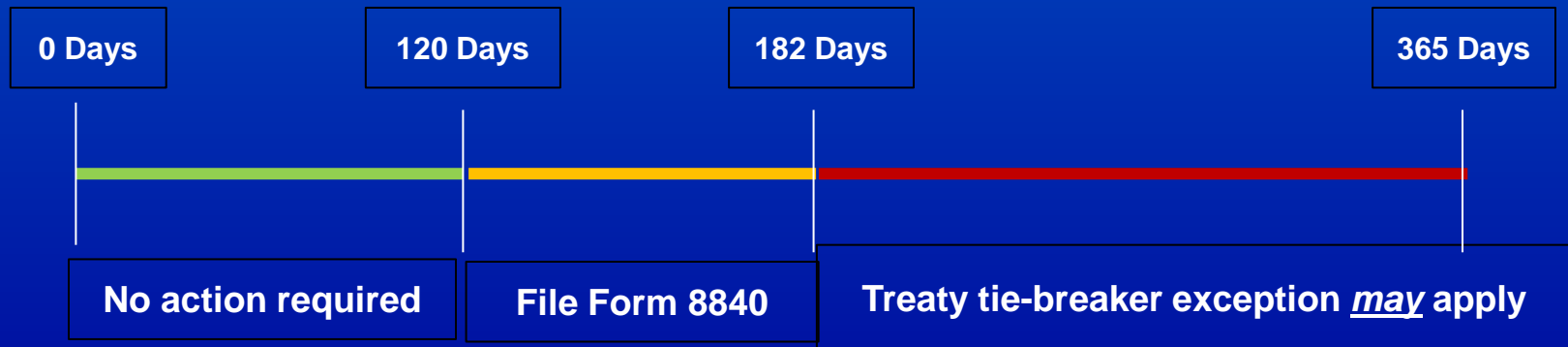
IMMIGRATION



CONSEQUENCES TO “UNLAWFUL PRESENCE”

- > 180 but < 365 = 3 year bar
- > 365 = 10 year bar

180 Days in Rolling 12 Months – Treaty, “Closer Connection”, and “Substantial Presence” are irrelevant



Overstaying your welcome

- INA s.222(g): Visa overstay; overstay; cancellation of visa; visa shopping
 - Cancellation of the nonimmigrant visa used by alien to enter the United States
 - Alien permanently restricted to applying for future nonimmigrant visas at a consular office in country of nationality, unless extraordinary circumstances exist
- Triggered by:
 - Entered on a nonimmigrant visa; and
 - Remained in the United States "beyond the period of stay authorized by the Attorney General"

Overstaying your welcome

- INA s.212(a)(9)(B): unlawful presence; 3- and 10-year bars
 - 3-year bar to readmission to the United States if alien voluntarily departs the United States after being unlawfully present for more than 180 consecutive days, but less than 1 year
 - 10-year bar to readmission to the United States if the alien departs (voluntarily or involuntarily) after being unlawfully present for 1 consecutive year or more
- Triggered by:
 - Present in the United States "after the expiration of the period of stay authorized by the Attorney General"; or
 - Entered the United States without being admitted or paroled; and
 - Remained unlawfully present for more than 180 consecutive days; and
 - Departed the United States

Doing Business in the U.S.

February 11, 2014

Stanley Abraham
416-640-2228



MEMBER

TAX SPECIALIST GROUP

WWW.TAXSPECIALISTGROUP.CA

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Issues to Consider When Doing Business in the U.S.

- Avoiding withholding, if possible.
- Federal income tax issues.
- State income/franchise tax issues.
- State sales tax issues.
- Structuring in the U.S.
- How you will get caught.

Doing Business in the U.S. Withholding

- Filing Form W-8ECI (see next slide)
- Need to apply for U.S. I.D. #, Form SS-4 (can be obtained same day by phone)
- Creates an ongoing U.S. filing obligation

Form **W-8ECI**

(Rev. February 2006)

Department of the Treasury
Internal Revenue Service

Certificate of Foreign Person's Claim That Income Is Effectively Connected With the Conduct of a Trade or Business in the United States

▶ Section references are to the Internal Revenue Code. ▶ See separate instructions.
▶ Give this form to the withholding agent or payer. Do not send to the IRS.

OMB No. 1545-1021

Note: Persons submitting this form must file an annual U.S. income tax return to report income claimed to be effectively connected with a U.S. trade or business (see instructions).

Do not use this form for:

- A beneficial owner solely claiming foreign status or treaty benefits W-8BEN
- A foreign government, international organization, foreign central bank of issue, foreign tax-exempt organization, foreign private foundation, or government of a U.S. possession claiming the applicability of section(s) 115(2), 501(c), 892, 895, or 1443(b) W-8EXP
- A foreign partnership or a foreign trust (unless claiming an exemption from U.S. withholding on income effectively connected with the conduct of a trade or business in the United States) W-8BEN or W-8IMY
- A person acting as an intermediary W-8IMY

Note: See instructions for additional exceptions.

Part I Identification of Beneficial Owner (See instructions.)

<p>1 Name of individual or organization that is the beneficial owner</p>	<p>2 Country of incorporation or organization</p>															
<p>3 Type of entity (check the appropriate box):</p> <table style="width: 100%; border: none;"> <tr> <td><input type="checkbox"/> Individual</td> <td><input type="checkbox"/> Corporation</td> <td><input type="checkbox"/> Disregarded entity</td> </tr> <tr> <td><input type="checkbox"/> Partnership</td> <td><input type="checkbox"/> Simple trust</td> <td><input type="checkbox"/> Complex trust</td> </tr> <tr> <td><input type="checkbox"/> Government</td> <td><input type="checkbox"/> Grantor trust</td> <td><input type="checkbox"/> Estate</td> </tr> <tr> <td><input type="checkbox"/> Private foundation</td> <td><input type="checkbox"/> International organization</td> <td><input type="checkbox"/> Central bank of issue</td> </tr> <tr> <td></td> <td></td> <td><input type="checkbox"/> Tax-exempt organization</td> </tr> </table>		<input type="checkbox"/> Individual	<input type="checkbox"/> Corporation	<input type="checkbox"/> Disregarded entity	<input type="checkbox"/> Partnership	<input type="checkbox"/> Simple trust	<input type="checkbox"/> Complex trust	<input type="checkbox"/> Government	<input type="checkbox"/> Grantor trust	<input type="checkbox"/> Estate	<input type="checkbox"/> Private foundation	<input type="checkbox"/> International organization	<input type="checkbox"/> Central bank of issue			<input type="checkbox"/> Tax-exempt organization
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<input type="checkbox"/> Private foundation	<input type="checkbox"/> International organization	<input type="checkbox"/> Central bank of issue														
		<input type="checkbox"/> Tax-exempt organization														
<p>4 Permanent residence address (street, apt. or suite no., or rural route). Do not use a P.O. box.</p> <p>City or town, state or province. Include postal code where appropriate.</p> <p style="text-align: right;">Country (do not abbreviate)</p>																
<p>5 Business address in the United States (street, apt. or suite no., or rural route). Do not use a P.O. box.</p> <p>City or town, state, and ZIP code</p>																
<p>6 U.S. taxpayer identification number (required—see instructions)</p> <p style="text-align: center;"><input type="checkbox"/> SSN or ITIN <input type="checkbox"/> EIN</p>	<p>7 Foreign tax identifying number, if any (optional)</p>															
<p>8 Reference number(s) (see instructions)</p>																
<p>9 Specify each item of income that is, or is expected to be, received from the payer that is effectively connected with the conduct of a trade or business in the United States (attach statement if necessary)</p> <p>.....</p> <p>.....</p> <p>.....</p> <p>.....</p> <p>.....</p> <p>.....</p> <p>.....</p> <p>.....</p> <p>.....</p> <p>.....</p> <p>.....</p>																

Part II Certification

Sign Here	<p>Under penalties of perjury, I declare that I have examined the information on this form and to the best of my knowledge and belief it is true, correct, and complete. I further certify under penalties of perjury that:</p> <ul style="list-style-type: none"> • I am the beneficial owner (or I am authorized to sign for the beneficial owner) of all the income to which this form relates, • The amounts for which this certification is provided are effectively connected with the conduct of a trade or business in the United States and are includible in my gross income (or the beneficial owner's gross income) for the taxable year, and • The beneficial owner is not a U.S. person. <p>Furthermore, I authorize this form to be provided to any withholding agent that has control, receipt, or custody of the income of which I am the beneficial owner or any withholding agent that can disburse or make payments of the income of which I am the beneficial owner.</p> <p>.....</p> <p>Signature of beneficial owner (or individual authorized to sign for the beneficial owner) Date (MM-DD-YYYY) Capacity in which acting</p>
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Doing Business in the U.S. Federal Filing Issues

- PE = Full U.S. filing
- No PE = Treaty Disclosure + Deduction Protection Statement

Doing Business in the U.S. Federal Filing Issues

What creates a PE?

- concluding contracts in the U.S.
- an office or fixed place of business in the U.S.
- certain construction projects

Doing Business in the U.S.

Federal Filing Issues

- Failure to file with a PE = disallowance of deductions after a certain amount of time
- Failure to file without a PE = \$10,000 penalty (per transaction?)

Form **8833**

(Rev. December 2013)
 Department of the Treasury
 Internal Revenue Service

**Treaty-Based Return Position Disclosure
 Under Section 6114 or 7701(b)**

► Attach to your tax return.

► Information about Form 8833 and its Instructions is at www.irs.gov/form8833.

OMB No. 1545-1354

Attach a separate Form 8833 for each treaty-based return position taken. Failure to disclose a treaty-based return position may result in a penalty of \$1,000 (\$10,000 in the case of a C corporation) (see section 6712).

Name	U.S. taxpayer identifying number	Reference ID number, if any (see instructions)
Address in country of residence	Address in the United States	

- Check one or both of the following boxes as applicable:
- The taxpayer is disclosing a treaty-based return position as required by section 6114 ►
 - The taxpayer is a dual-resident taxpayer and is disclosing a treaty-based return position as required by Regulations section 301.7701(b)-7 ►
- Note.** If the taxpayer is a dual-resident taxpayer and a long-term resident, by electing to be treated as a resident of a foreign country for purposes of claiming benefits under an applicable income tax treaty, the taxpayer will be deemed to have expatriated pursuant to section 877A. For more information, see the instructions.
- Check this box if the taxpayer is a U.S. citizen or resident or is incorporated in the United States ►

<p>1 Enter the specific treaty position relied on:</p> <p>a Treaty country _____</p> <p>b Article(s) _____</p>	<p>3 Name, identifying number (if available to the taxpayer), and address in the United States of the payor of the income (if fixed or determinable annual or periodical). See instructions.</p>
<p>2 List the Internal Revenue Code provision(s) overruled or modified by the treaty-based return position</p>	
<p>4 List the provision(s) of the limitation on benefits article (if any) in the treaty that the taxpayer relies on to prevent application of that article ►</p>	
<p>5 Is the taxpayer disclosing a treaty-based return position for which reporting is specifically required pursuant to Regulations section 301.6114-1(b)? <input type="checkbox"/> Yes <input type="checkbox"/> No</p> <p>If "Yes," enter the specific subsection(s) of Regulations section 301.6114-1(b) requiring reporting ► _____</p> <p>Also include the information requested in line 6.</p>	
<p>6 Explain the treaty-based return position taken. Include a brief summary of the facts on which it is based. Also, list the nature and amount (or a reasonable estimate) of gross receipts, each separate gross payment, each separate gross income item, or other item (as applicable) for which the treaty benefit is claimed _____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p>	

Doing Business in the U.S. Federal Filing Issues – Challenges

- Branch profits tax issues (\$500,000 exemption)
- LLC ownership issues
- Interest expense fungibility
- State worldwide issues

Doing Business in the U.S. State Income and Sales Tax

- In order to be subject to tax in a state, one must have nexus in a state
- The threshold for sales tax nexus is lower than for income/franchise tax nexus
- Generally, the states do not adopt treaty exemptions
- Physical presence in the state is a compelling nexus creating fact

Doing Business in the U.S.

State Income/Franchise Tax Nexus

- P.L. 86-272 prohibits a state from imposing a net income tax on a corporation organized in another state if its only activity is:
 - solicitation of orders in the state
 - sales of tangible personal property
- Rule does not apply to sales tax, gross receipts tax (e.g. Texas, Ohio, etc.)

Doing Business in the U.S.

State Income/Franchise Tax

Common Nexus Triggers (non-exhaustive):

- inventory in a state
- licensing software, trademark, etc.
- leasing of property
- solicitation of sales for real estate, intangible and services
- non-salesperson working from a home office
- training, seminars
- repairs

Doing Business in the U.S.

State Income/Franchise Tax

State Tax Traps

- Worldwide taxation trap – could be problematic if there are U.S. losses
- Bonusing down to small business exception
- Having one activity taint another activity

Doing Business in the U.S. State Sales Tax Matters

- No P.L. 86-272 protection
- “Warm Body” test – if there was a warm body in the state, they will want to tax

Doing Business in the U.S.

State Sales Tax

- Sales tax may differ by zip code
- Exemption certificates (e.g. resale, etc.) are required
- File “NONE” returns

Doing Business in the U.S.

State Sales Example

- Canco manufactures store fixtures for a U.S.-based retailer. The retailer would like Canco to manage the installation of the store fixtures. As well, Canco is very profitable and bonuses out to its sole shareholder on an annual basis.

Doing Business in the U.S. Structuring Considerations

- Determining U.S. taxable income under transfer pricing principles (particularly for U.S. subsidiary)
- Higher corporate tax rates in the U.S. (40% vs. 26.5%)
- LLC – Treaty benefits denied (e.g. branch profits tax at 30% rather than zero)
- Interest Deductibility
 - Cash basis rules (IRC §267(a)(3))
 - Earnings stripping
 - Thin capitalization

Doing Business in the U.S.

How Will I Get Caught?

- The Large Business and International Division of the IRS had announced that withholding on foreign payments would be designated as a Tier 1 withholding issue. New standard IDRs have been developed for foreign payments.
- The heat is on U.S. businesses to withhold absent documentation failing which they are responsible
- FATCA, as will/has been discussed
- States are desperate to balance budgets and have resorted to desperate measures:
 - Audits of in-state companies have become “fishing expeditions” for companies they are doing business with
 - Sophisticated approaches including wireless technology
 - Amnesty programs and post-amnesty program penalties