

What to know before you go

Tax costs for spending time in the US

Are you a Canadian resident who spends a substantial portion of the year in the United States? Whether you divide your time between Canada and the United States for business obligations, vacation time or to manage your investments, you should be aware that the amount of time you spend in the US may come with tax costs.

Depending on the number of days you spend in the United States each year, the IRS may consider you a US resident for income tax purposes. This means that in addition to your Canadian tax obligations, you will also be **required to file US tax returns** and other information reporting forms. This could be complicated and costly depending on your financial accounts and holdings. In addition, you can also face **significant penalties** for not complying with these requirements.

Time is money – Substantial presence test

Generally, whether a Canadian resident has US tax obligations depends on the number of days spent in the United States. Specifically, if your physical presence in the US totals **183 days or more in a three-year period**, you will be deemed a US resident and have **filing requirements**, unless you can meet one of the available exceptions. The time you spend in the US includes the number of days you were in the United States in the current year, plus:

- **One-third of the number of days** spent in the United States in the prior year, and
- **One-sixth of the number of days** spent in the United States in the second prior year

Example:

For the current year, you determine that you spent 140 days in the US in 2021, 90 days in 2020 and 150 days in 2019.

2021: 140 days
+ 2020: 30 days ($1/3 \times 90 = 30$)
+ 2019: 25 days ($1/6 \times 150 = 25$)
= 195 days

Since this number exceeds 183, you are considered a resident in the US for 2021.

Closer connection exception

Even if you are in the United States for 183 days or more according to the substantial presence test, you may have limited US filing obligations where you meet one of the available exceptions to these rules.

If you weren't in the United States for at least 183 days in the current year, but you still meet the test's threshold, such as in the previous example, you may qualify for the "closer connection" exception. In this case, you may not be considered a US resident for tax purposes where you had a closer connection to Canada than to the United States. In addition to having a tax home in Canada, the IRS looks at such factors as:

- Where is your permanent home
- Where your family is located (spouse and children)
- The location of your automobile and personal belongings
- The location of your social, religious, cultural and political organizations to which you belong
- Where your driver's licence was issued
- Where you are registered to vote
- Where you derive the majority of your income for the year
- Whether you are covered by provincial health insurance in Canada.

To rely on the closer connection exception for a particular year, you must file Form 8840 by June 15 of the following year.

Tax treaty “tie-breaker” rule

If you were in the United States for 183 days or more in the current year, you can still qualify for an exception under the Canada-US tax treaty. Specifically, you can be considered a non-resident in the United States if you can establish that you have stronger ties in Canada than the United States under the treaty’s “tie breaker” rule. This determination depends on factors including the location of your permanent home, or centre of vital interests.

To claim this treaty exception, you must file a US non-resident tax return. You will not be subject to US tax on your worldwide income, but you will also be required to report to the IRS:

- Your non-US bank and financial accounts (FinCEN Form 114)
- Transfers to and distributions from non-US trusts, including Canadian TFSAs and certain RESPs (Forms 3520 and 3520-A)

- Receipts of certain foreign (non-US) gifts and bequests (Form 3520)
- Certain non-US corporate and partnership holdings (Form 5471).

Note that there are significant penalties for failure to file these information forms, **ranging from US\$10,000 per form, to US\$100,000 or 50% of certain account balances** for willful non-compliance.

Take action to avoid becoming a US resident

If you take frequent trips to the United States, you may want to consider whether it’s possible to reduce the amount of time you spend in the United States.

Rule of thumb: If you spend 182 days or fewer in the United States each year, you can minimize your US filing obligations. Additionally, if you can avoid spending more than 121 days in the US in any calendar year, you will not be subject to the substantial presence test.

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