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United States – Relief for Individuals with Interests in Canadian Retirement Plans

by KPMG LLP's Washington National Tax practice, Washington, D.C. (KPMG LLP in the United States is a KPMG International member firm)

Eligible U.S. citizens and residents with interests in certain Canadian retirement plans will be treated as automatically making an election, under a provision of the United States-Canada income tax treaty, to defer U.S. income tax on income accruing in their Canadian retirement plans until a distribution is made, according to an advance copy of Rev. Proc. 2014-55, released on October 7, 2014, by the U.S. Internal Revenue Service (IRS).¹

The Rev. Proc. provides that eligible individuals will be treated as having made the election in the first year in which they would have been entitled to make the election under the treaty – i.e., the relief is retroactive.

The Rev. Proc. also removes a previous annual reporting requirement with respect to interests held in the identified Canadian retirement plans – registered retirement savings plans (RRSPs) and registered retirement income funds (RRIFs)

Why This Matters

The revenue procedure provides retroactive relief for eligible taxpayers who failed to properly elect relief under the prior IRS guidance. Accordingly, individuals with RRSPs and RRIFs automatically qualify for tax deferral similar to that available to participants in U.S. individual retirement accounts (IRAs) and 401(k) plans.

Moreover, administrative burdens are eased for taxpayers with such accounts, as the guidance eliminates a special annual reporting requirement on Form 8891 for taxpayers with interests in these Canadian retirement plans.

Background

U.S. tax law generally provides that an individual who is a citizen or resident of the United States and a beneficiary of a Canadian retirement plan is subject to current U.S. income taxation on income accrued in the plan – even though the income is not currently distributed to the beneficiary.

However, such individuals generally would not be subject to Canadian income taxation with respect to the accrued income until the income is actually distributed from the plan. Because of this “mismatch” between the timing of the U.S. tax and the Canadian tax, there could be instances of double taxation.

Article XVIII(7) of the United States-Canada income tax treaty (as added by a 1995 Protocol) was intended to address this timing mismatch and basically provided relief to an individual with an interest in a Canadian pension plan (by allowing an election to defer taxation in the United States). This treaty relief provision was further amended by a 2007 Protocol.²

The IRS issued guidance – first, Rev. Proc. 2002-23 and then two IRS notices were issued in 2003 – for making an election under Article XVIII(7) of the income tax treaty.

Rev. Proc. 2014-55

Rev. Proc. 2014-55 replaces the existing procedures that an individual would use to make an election to defer U.S. tax under Article XVIII(7) of the income tax treaty with respect to a Canadian retirement plan.

Rev. Proc. 2014-55 provides that any election made under the guidance issued on October 7, 2014, is made on a plan-by-plan basis, and that these rules apply whether or not the beneficiary was a resident of Canada at the time the contributions were made to the retirement plan.

As explained by the IRS in a separate release³ (IR-2014-97) Rev Proc. 2014-55 provides retroactive relief to eligible taxpayers who failed to properly elect relief under the prior IRS guidance. Accordingly, individuals with RRSPs and RRIFs automatically qualify for tax deferral similar to that available to participants in U.S. IRAs and 401(k) plans. In general, U.S. citizens and resident aliens qualify for this special treatment as long as they filed and continue to file U.S. returns for any year they held an interest in an RRSP or RRIF and include any distributions as income on their U.S. returns.

KPMG Note

Taxpayers who may have already reported on their U.S. federal income tax returns undistributed income that has accrued in a Canadian retirement plan during a tax year, need to note that under Rev. Proc. 2014-55, they are not “eligible individuals” and will remain currently taxable on the undistributed income. These taxpayers, if they now want to make an Article XVIII(7) election with respect to a Canadian retirement plan, must seek the consent of the IRS Commissioner.

The IRS also is eliminating a special annual reporting requirement on Form 8891 for taxpayers with interests in these Canadian retirement plans. Taxpayers are no longer required to file Form 8891.

KPMG Note

The revenue procedure does not modify any other U.S. reporting requirements that may apply (e.g., FinCEN Form 114 (FBAR) filings required under the Bank Secrecy Act and Form 8938 filings as required under section 6038D).

Footnotes:

1 For Revenue Procedure 2014-55, see: <http://www.irs.gov/pub/irs-drop/rp-14-55.pdf> .

2 For prior coverage of the 2007 Protocol, see the following issues of GMS *Flash Alert* (formerly “*Flash International Executive Alert*”): [2008-152](#) (September 16, 2008), [2008-025](#) (January 28, 2008), [2007-166](#) (September 24, 2007), and [2007-163](#) (September 20, 2007).

3 For IR-2014-97 (October 7, 2014), see: <http://www.irs.gov/uac/Newsroom/IRS-Simplifies-Procedures-for-Favorable-Tax-Treatment-on-Canadian-Retirement-Plans-and-Annual-Reporting-Requirements> .

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A New Video is Now Available from KPMG's Global Mobility Services Practice

To get a better understanding about why income tax treaties and social security agreements are important for international assignees and their multinational employers, we encourage you to view the following video on the Tax Watch Web page on www.kpmg-institutes.com:

See: [Update on U.S. Income Tax Treaties and Social Security Totalization Agreements](#) (app. 9 minutes)

In this recently released GMS video, we look at the important role income tax treaties and social security agreements play in mitigating costs and fostering cross-border business between the United States and other countries. This video highlights the social security agreement with Slovakia, which entered into force a few months ago, and the revised agreement with Switzerland, which entered into force on August 1.

The following information is not intended to be "written advice concerning one or more Federal tax matters" subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230 as the content of this document is issued for general informational purposes only.

The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser.

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