2016 TAX FILING SEASON NEWSLETTER

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It's that time of year once again, taxes are due, and, as per usual, the American and Canadian governments are looking at taxpayers living abroad or owning foreign property with suspicion. In the minds of these agencies, you are likely a tax evader despite any and all evidence to the contrary. If you are earning a high income on top of that, Canada in particular has planned out ways to make you suffer by penalizing you through newly increased tax rates.

Instead of being compelled to say a few expletive words, we'd say take a deep breath and get organized and ready. And if looking for an excuse to beat the system, take a note to the lessons learned by those who have tried this strategy before. The following excuses are known to tax agencies and did not work the first time, so take heed, good citizens:

1. My tax papers were left in the shed and the rat ate them
2. I'm not a paperwork-oriented person - I always relied on my sister to complete my returns but we have now fallen out
3. My accountant has been ill
4. My dog ate my tax return
5. I will be abroad on deadline day with no internet access so will be unable to file
6. My laptop broke, so did my washing machine
7. My niece had moved in - she made the house so untidy I could not find my login details to complete my return online
8. My husband ran over my laptop
9. I had an argument with my wife and went to Italy for 5 years
10. I had a cold which took a long time to go

Wishing all of you an uneventful tax season!
We hope you will rely on us for assistance

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US TAX CHANGES FOR 2015

US Passport Revocation

Life in the FAST lane (just make sure you're clear with the IRS)

Obama and Republicans finally agreed on something in common: Passing the Fixing America's Surface Transportation Act in order to continue the crackdown on tax evaders, aka Americans living abroad.

The FAST Act is a 5-year policy that enables the government to collect taxes to pay for transportation-related projects such as roads, bridges or rail networks. In the past, policy for transportation relied on financing from gas tax. However, cars are getting more efficient which has limited the amount of funding the government can generate. So, staring a $16 billion shortfall in the face, the government decided to add a mechanism to the Act that ensures the IRS can collect from a guaranteed 6 to 8 million Americans.

The mechanism they came up with? The ability for the State Department to deny, revoke or limit a passport for any American who is "seriously delinquent" in paying their taxes. FAST defines delinquent as anyone who owes $50,000 USD or more in unpaid taxes, including penalties and interest. (Individuals paying off debts in a timely manner or who have requested a hearing to contest a collection are exempted.)

Before FAST, the IRS could not disclose tax information to the State Department and, in turn, the State Department could not deny, revoke or limit a passport based on a citizen's tax payments. Now, the IRS will be sharing tax information with the State Department and issuing a certificate that orders the State Department to deny, revoke or limit a passport so its holder can only travel back to the U.S.

Besides delinquency, Americans applying or renewing passports can expect fines if they owe a child support payment over $2,500 USD or any other type of federal debt or if they fail to provide their social security number.

FAST's provision to deny or limit a passport is a harmful way for the IRS to ensure Americans living outside the U.S., particularly in Canada, for whom having a valid passport is critical, remain vigilant in filing their returns.

Reminder: US law requires US citizens, including dual nationals, to enter and depart the U.S. with proper US documentation to avoid being barred or delayed at the port of entry.

Update on OVDP and Streamlined Procedures

Own up to tax evasion (intentional or not): Get it done while the gettin's good

Outstanding or incomplete returns haunt some of us, and the IRS knows it. For those of you living abroad according to a completely different calendar, you have a better excuse than your peers living on American soil. But even so, chances are you can never quite forget that perhaps you haven't filed a return in years or reported that foreign bank account. If this is you, do not despair -- there is salvation that will mute your guilty conscience and save you the hefty penalties you're dreading: Your saviour is called **the Streamlined Filing Compliance Procedures**.

The Streamlined Procedures is a special program designed for delinquents like you who have yet to file years worth of returns. The program is an amnesty-style program that tax delinquents have to voluntarily enter into. And here's why people do it voluntarily; if you reside outside of the U.S., there are no late penalties. I repeat, there are **NO late penalties**.

To begin clearing your slate with the IRS through the Streamlined Procedures you must file delinquent income tax returns for the last 3 years (2012, 2013, 2014) and FBAR forms (aka FinCen form 114) for the last 6 years (2009 - 2014), if filed before June 15 and June 30, 2016, respectively (or past the said due dates if tax year 2015 is filed or extended timely).

What are the penalties you'd be facing if it wasn't for the Streamlined Procedures? Well, let's count it up: A missed form or an account can mean a civil penalty of $10,000 or more per account or form, including a criminal penalty. **Which forms are commonly required for expats?**

- Form FinCen 114 – Foreign bank and financial accounts (aka FBARs)
- Form 8938 - Form declaring offshore foreign financial accounts and assets (aka FATCA)
- Form 8621 - Report by a shareholder of a Passive Foreign Investment Company (this would be for certain mutual funds held outside of pensions and RRSPs/RRIFs)
- Form 3520 – Annual return for transactions with foreign trusts (RESPs and certain TFSAs)

(Note: If you reside within the U.S. but hold accounts outside the U.S. then there is a 5% penalty, based on the highest aggregate account balance measured over up to six years given you did not intentionally withheld such information from your originally filed returns.)

Now, if you don't qualify to settle the score with the IRS through the Streamlined Procedures and they or one of their foreign partners have not tracked you down yet, the IRS can avail you to come forward through the ironically named **Offshore Voluntary Disclosure Program**. The **OVDP** requires more onerous paperwork and a penalty to the tune upto 50% of the aggregated highest balances in your overseas bank and financial accounts in addition to several other civil penalties. This "awesome" deal is in exchange for a waiver from a criminal prosecution.

Though the OVDP is less of a break than the Streamlined Procedures, both processes allow for you to square off unpaid taxes without having to pay the full penalties you owe. This is a system the US government says it will keep in place for the time being. However hints are being dropped that *the system will not last forever*. Officials said in December that after a certain point the government will stop accepting expats claim of ignorance and begin assuming any tax delinquency as a willful evasion and presumably cease the Streamlined Procedures and the OVDP. Of course, they say they'll give us all ample warning before this happens but as with most things it's always prudent to act sooner rather than later.

Remitting US taxes
So you owe Uncle Sam…

If the worst case happens this year, here's how to pay the IRS from abroad:

- The old school way: via check, money order, cashier's check or cash
- The super old school way: via telephone at 1 800 555 4477
- The way of the 21st century: Electronic transfer
- The way of the shopaholic: by card, credit or debit. Contact us to find out details

If the tax debt is too large for you to pay off in one go, here's how to successfully bargain:

- Put off the inevitable for a little. Request a short term agreement wherein the IRS grants you 120 days to fully pay off your tax debt. You request this time extension through the "Payment Agreement" available on their website and there's no charge applied.
- Apply for a monthly payment plan. If you owe less than $50,000 you can apply using the "Payment Agreement" online. If you owe more, complete Form 433F, Collection Information Statement, and pay user fees. Both plans used direct debit to collect the money right from your account. The upside? No missed payment and no damaged credit.
- Make them an offer they can't refuse. Hey, I can't pay you what I owe now or never, it's just not possible and here's my "Offer-in-Compromise" application to prove it. What I can do is pay you [insert number after which you will sell your firstborn child] with this timeframe [insert number of months]. Who says the IRS isn't reasonable?
- Get a fresh start. This IRS initiative is for individuals and small businesses to pay back their taxes over a prolonged period of time and avoid credit-damaging tax liens.

Finally, how to make sure paying the IRS never happens again in case when you are employed in the U.S.: Tell your employer to increase the taxes they withhold from your salary. You can calculate this amount using the IRS' "Withholding Calculator" on their website.

FIRPTA Changes

A little bit of good. Yeah with a little bit of bad

Foreign investors are not typically charged US taxes on capital gains from disposition of US property unless it is US real property, stocks or other beneficial interests related to US real estate (few other exceptions also apply). All these instances are treated as income connected with a US trade or business and tax is charged through a mandatory withholding mechanism.

This practice dates back to the 1980s when foreign ownership made Americans anxious about a foreign takeover of the US real estate market and so created a 30% withholding tax on all real estate investments by foreigners. The only aspect of real estate this didn't apply to was real estate investments trusts (REITs) so long as the foreign investors owned less than 5% of a trust's stock. The governing legislation keeping it in place is FIRPTA, the **Foreign Investment in Real Property Tax Act.**

2015 saw several changes made to FIRPTA including the adjustments to the rates of withholding and exemption. First, foreign pensions investing in US real property are no longer subject to FIRPTA. Secondly, foreign investors can now safely hold upto 10% of a publicly traded REITs and still avoid FIRPTA implications on any distributions and dispositions made by the REIT. And finally, unless subject to a limited exclusion, starting February 16, 2016, Canadians and other non-US residents will be required to remit 15% instead of 10% on sale of US real estate, whether held outright or through an entity.

ITIN Changes

The IRS is taking a lesson from The Big Short to heart; always scrutinize applications for validity before creating CDOs, or in the IRS' case, issuing ITINs to non-resident aliens or American residents who are ineligible to work in the U.S. or collect Social Security. The process of verifying these applications was severely flawed: Since 1996, only a quarter of ITINs issued have been used to file tax returns or pay taxes.

So if you are one of the rare birds who has or intends to get an ITIN, listen up because the IRS is smartening up.

Starting on January 1, 2013, ITINs are only valid if a tax return has been filed for the past three years consecutively. If the three-year reporting window is missed, the ITIN will expire on Dec. 31 of the third year. So the moral of the story, if you wish to keep the number, file your taxes. That said, the rules will differ for any ITINs granted before January 1, 2013.

For ITINs obtained before January 1, 2013, depending whether the three-year window for consecutive reporting was upheld or not, the ITIN has been scheduled to expire on December 31 between 2016 to 2019. After this one-time renewal, your ITIN will be for life so long as you continue filing a tax return for at least three consecutive years.

Pro tip: If you wish to file disclosures like **Form 8840** (Closer Connection Exception Statement for Aliens) or **Form 8843** (Statement for Exempt Individuals and Individuals with a Medical Condition) you may want to file them alongside 1040NR returns since only tax returns and not the forms can guarantee the retention of the ITIN.

FATCA
Is nowhere sacred anymore?

About 155,000 US citizens residing in Canada along with US citizens from 94 other countries may now have their account information handed over to the IRS by the local tax agencies. The sharing of information between the agencies are a result of intergovernmental agreements which were supposed to be activated in September 2015.

The sharing is part of the **Foreign Account Tax Compliance Act** (FATCA) which is aimed at reducing the capacity of Americans to evade taxes with foreign accounts, interest earned in those accounts or residence abroad.

Financial information about Americans' accounts with a balance over $50,000 will be automatically shared with the IRS through the country of the financial institution. To incentivize foreign governments to agree to mandate their financial institutes to share information with the IRS, the IRS under FACTA imposes a 30% withholding tax on any financial institutions which refuse to cooperate and yet service US account holders. To avoid the punitive 30% umbrella withholding, the recalcitrants must give up servicing to any existing or new US citizen clients and customers.

The IRS imposed a deadline for agreeing participants to begin submitting information by September 30, 2015, though some countries received a year-long extension. By October 22, at least 28 countries, including Canada submitted Americans account information to the IRS. It is yet unknown to how many of these participants the United States divulged similar information about their citizens account holders in the U.S. on a reciprocal basis.

New repair regulations
They listened to the mass outcry against the $500 repair regulation

These changes date back to 2013 when the IRS after spending 8 years at last introduced the New Repair and Capitalization Regulations which offered a major overhaul since the mid-80s to how business assets depreciate.

The New Repair Regs impacted virtually any taxpayer or a business owning tangible or real property, including American citizens or non-residents who have US tax filing obligations in relations to their rental or small business activities. They allowed for a break, known as **the safe harbor** for individuals and small businesses, to automatically deduct repairs and maintenance costs up to a certain threshold from income beginning in tax year 2014, instead of making the owners to capitalize and depreciate such costs as was in the past. Deductions could also include materials, supplies, spare parts and even acquisition costs. It all sounded great, until the IRS said the threshold was $500.

After numerous complaints to increase the safe harbour, many reasoning costly electronic purchases that easily surpass $500, in November the IRS announced they were now **increasing the safe harbour to $2,500 of expenses per invoice or item**. Many are still saying this isn't large enough, it's a start. For businesses or individuals who want to claim deductions greater than $2,500 they must submit an applicable financial statement (audited by a CPA) up to a deductible threshold of $5,000. To maximize the write offs beyond $2,500, it's recommended that taxpayers create a written policy to document and support their claimed deduction.

The only drawback? **The revised safe harbour goes into effect in tax year 2016.**

New IRS form
The new kid on the block

The IRS has introduced a new form which will tell the IRS and the beneficiaries of a deceased's estate the value of the property they receive and which they will use as the basis for future transactions.

Form 8971 was released in draft in December and the final version of the form and instructions to submit it, are to be released in the coming days. The form will be required for all estate returns filed made after July 31, 2015 with the first round of submissions scheduled by February 29, 2016.

Form 8971 is due 30 days after the filing date of the IRS' Forms 706, 706-NA or 706-A -- all of which are forms the IRS formerly used to report the value of the decedent's estate (including the US situs assets of a non-US resident decedent). Now these forms in conjunction with Form 8971 will do the job.

Why was an additional form required?

Form 8971 will reportedly standardize the valuation of properties received from an estate which is then reported on a 706, but only if the latter needs to be filed. **Unfortunately, the executors of all the estates of Canadian decedents with US assets valued more than $60,000, will be obligated to file 8971.**

As per usual, if Form 8971 is filed incorrectly or not filed, a penalty as high as $3 million may be imposed on executors.

Note: Starting after July 1, 2015, the IRS no longer automatically issues closing letters for filed estate tax returns. This means that you may have a delay in transferring a property title. Taxpayers must wait for at least four months before making requests for closing letters by phone or obtaining transcripts on line. Please contact us if you need n assistance in requesting a closing letter from the IRS.

2016 Inflation and Other Adjustments

- The annual exclusion for gift tax purposes remains at $14,000
- The annual exclusion for gifts to a non-US citizen spouse is $148,000 (up from $147,000)
- The unified exemption against gift and estate tax will be $5.45 million (up from $5.43 million) which means a US citizen couple will shield the first $10.9 million from US estate and gift taxes. This also means that a Canadian resident decedent, who is not an American and survived by a spouse, will have no US estate tax payable if the value of the worldwide estate is less than $5.45 million. **EVEN IF NO TAX PAYABLE IS DUE, US ESTATE FILING REQUIREMENTS STILL EXIST!**
- The GST tax exemption increases to $5.45 million (up from $5.43 million)

CANADIAN TAX CHANGES FOR 2015

New provisions under Liberal government

How easily can the Liberals reduce high-income earners to tears?

The Vogue-model, aka Canada's current Prime Minister, Justin Trudeau has made notable progress in one significant area and the Tories among you are not going to be resting easy. Trudeau's Liberals have made sweeping changes to Canada's tax laws and there are big implications on how higher income brackets will be taxed.

For instance, if you plan to earn more than $200,000 you will have an increased tax liability in 2016 with the top federal income tax rate jumping from 29% to 33% as part of the Liberals' new tax bracket. What does this mean to you? As an Ontario resident making over $200,000 you will now keep only 46.47% of your earnings with the other 53.53% being taxed away. **Let's repeat – you are keeping 46.47% and giving away 53.53%.**

How can you fight a losing battle against the CRA to protect your money? If possible, reduce your income for 2016 by gifting, lending, deferring income or setting up retirement plans. The new 33% federal tax will also apply to trusts and estates with the exception of qualified disability trusts and the newly created Graduated Rate Estates (GREs) which are discussed in more details later.

In addition, the federal tax donation credit for individuals earning over $200,000 per year will increase to 33% on donations over $200 made after 2015. Donations made in prior years but claimed in 2016 or subsequent years will not be eligible for the increased credit.

True to their middle class support base, however, the federal income tax rate for individuals who make between about $45,000 to $95,000 per year will fall from 22% to 20.5%, which equates to a tax savings of approximately $679 per taxpayer

Among other changes, the Liberals have cancelled the income-splitting teaser which is available on 2014 and 2015 tax returns to families with children under 18 to reduce income tax by up to $2,000. A new child benefit is reported to be on its way in July 2016.

Finally, to test how many tears can be shed as a result of income tax changes, the Liberals have rolled back the **Tax Free Savings Account** (TFSA) limits. The limits now return to $5,500 in 2016 and will follow inflation and round up to the nearest $500 from now on. The limit for 2015 will remain at $10,000 and anyone who has not made additional contributions will be able to carry forward the amount for future years.

The scary part is they are just getting started. The Liberals have yet to release their annual federal budget which is expected to include a 4% increase on the overall tax investment on Canadian-controlled private corporations. Here's hoping.

CRA changes for letters/payments
The CRA goes digital and forces you to follow suit

Remember when cellphones first came out and they were such a luxury and novelty? Now everyone has one and you are a dinosaur of epic proportions if you continue to eschew the presence of technology in your life. Well if we extend this metaphor to the CRA's digitization of its services, the Agency is an ample example of the pervasiveness of online services.

Gone are the days of CRA cheques. The CRA has officially moved into the 21st century and **will only issue money through direct deposit**. This means any recipient of government money, including tax refunds, must provide the CRA with a bank account information by the May 2, 2016 deadline in order to receive their payments in a timely manner. The major benefit is the timing of the processing; instead of payments taking weeks, it will now take a matter of hours.

Sign up can be done through *My Service Canada Account* which allows you to securely view your personal information and numerous slips, including T4RSP, T4RIF, T3, T5, T5008, RRSP contributions slips, T5007 as far as 10 years back!

The CRA has also improved the notice of assessment. The new simpler format provides the most important information about your assessment on the first page. The new notice of assessment can be received through an online mail service starting in the summer of 2016 if the CRA receives your email address provided on your 2015 tax return. The CRA is planning to furnish more correspondence via the online service.

CDN tax changes for testamentary trusts
Extending CRA's reach beyond the grave

The new testamentary trust tax rules came into effect on January 1, 2016 and will affect existing and future trusts. In brief, **the change no longer allows for the lower graduated tax rates that some trusts currently enjoy.** Another significant twist affects the decedent's beneficiaries who will now be required to pay tax on accrued gains in spousal, alter ego and joint partners' trusts instead of the trusts themselves.

At length, the estates will now be referred to as "**graduated rate estate**" or **GRE** in short. If a decedent dies with multiple estates, only one can be designated as a GRE in the first taxation year. The benefits of a GRE will last for up to 36 months and upon the conclusion of this time period, the estate will be deemed to have a year-end when it reverts back to its non-graduated status in addition to a second year-end on December 31.

Under the rules, testamentary trusts and estates, other than GRE, will be taxed at the top tax rate (federal 33%). Depending on the province, the combined tax rates range from 47.7% to 58.75% which means estates could face more than $15,000 increase in taxes as a result of this change.

Note: In addition to GRE, these new rules do not apply to Qualified Disability Trusts (QDT).

For testamentary trusts and non-GREs the following exemption benefits will no longer be available:

- Quarterly tax installment remittances
- $40,000 Alternative Minimum Tax
- Tax on the designated income of certain trusts like Canadian capital gain allocated to non-resident beneficiaries

In addition, the testamentary trusts and non-GREs lose the ability to allocate investment tax credits to beneficiaries and to file a notice of objection over 90 days extended time period.

The benefit to the new rule comes into play for charitable donations. Prior to these changes, the donations were considered to be made prior to the deceased's passing which meant the full benefit of their donation was often lost. Under the new rules, donations will be considered from the time of the actual donation and the tax credit can be applied to any of the five subsequent tax years, a prior year or the current year giving much greater flexibility to executors and trustees.

In light of these changes, all individuals are recommended to ensure their affairs are in order and their intention is fulfilled in spite of these new changes.

T1135 Revisions
Save at home, Canada

Yet another revision of T1135, effectively disincentivizes foreign property owners to outright invest outside of Canada or face a truckload of complex, expensive paperwork.

The changes to Form T1135 give taxpayers a simplified reporting method for foreign properties they own (both through a Canadian-based custodian and outright abroad) so long as the combined property cost falls between $100,000 and $250,000. The former detailed reporting method remains unchanged for foreign properties with combined cost $250,000 or more.

The simplified Form T1135 reporting will require the following information from the taxpayer: the type of property (options provided to choose from), the country the property is located in and lastly, the total amount of income and gains/losses in aggregate. This form may not seem so different from the previous one, however its real benefit comes for taxpayers whose property is not registered with a Canadian Registered Securities Dealer and had to track down relevant information independently.

Many in the tax community have raised concerns over the new form, namely many had been campaigning for a higher cost amount to fall under Form T1135's jurisdiction. However the changes this year are a result of previous campaigning so, in short, there is hope for next year.

Border Tracking System Implemented to stop non-residents cashing in on Benefits

Enough freeloading, the CRA has said to the Canadian population at large; they will find you and they will take away your benefits regardless of who you are. The tracking system - be it a land border or by air – is in the works to catch Canadians whose insufficient presence in the country disqualifies them from certain benefits. Once the tracking system is in place, it should allow Canada to save between $194 million and $319 million over five years.

The CRA is instating a planned border tracking system which will alert them of Canadians who are residing outside of Canada and are therefore ineligible for social benefits. The benefits at issue include Old Age Security, Unemployment Insurance, Child Tax benefits and others.

In order to be cleared by the CRA to receive your child tax benefits, you must be present in the country for at least 183 in a calendar year. To be eligible for Old Age Security benefits, you need to be a resident of Canada for as little as 10 years and as long as 20 years depending on the country of residency at the time the benefits are collected.

The tracking system has already been instituted for foreign nationals and permanent residents of Canada and the U.S. but this next phase will be sharing information about both country's citizens. Canada is also expanding its sources of gathering information to include travellers leaving by air and ground.

2015 COMBINED FEDERAL AND ONTARIO PERSONAL TAX RATES

Taxable Income	Salary/Interest	Capital Gain	Eligible Dividends	Non-Eligible Dividends
First $40,922	20.05%	10.03%	(6.86%)	5.35%
40,923 – 44,701	24.15	12.08	(1.20)	10.19
44,702 – 72,064	31.15	15.58	8.46	18.45
72,065 – 81,847	32.98	16.49	10.99	20.61
81,848 – 84,902	35.39	17.70	14.31	23.45
84,903 – 89,401	39.41	19.70	19.86	28.19
89,402 – 138,586	43.41	21.70	25.38	32.91
138,587 – 150,000	46.41	23.20	29.52	36.45
150,001 – 220,000	47.97	23.98	31.67	38.29
Over 220,000	49.53	24.76	33.82	40.13

2016 COMBINED TOP MARGINAL PERSONAL TAX RATES

PROVINCE	Salary/Interest	Capital Gain	Eligible Dividends	Non-Eligible Dividends
British Columbia	47.70%	23.85%	31.30%	40.61%
Alberta	48.00	24.00	31.71	40.24
Saskatchewan	48.00	24.00	30.33	40.06
Manitoba	50.40	25.20	37.78	45.69
Ontario	53.53	26.76	39.34	45.30
Quebec	53.31	26.65	39.83	44.23
New Brunswick	58.75	29.38	43.79	51.75
Nova Scotia	54.00	27.00	41.58	46.97
Prince Edward Island	51.37	25.69	34.22	43.87
Newfoundland	48.30	24.15	38.47	39.40

TAX-FREE SAVINGS ACCOUNT (TFSA) CONTRIBUTION LIMIT

Years	TFSA Contribution Limit	Total
2009-2012	$5,000 per year	$20,000
2013-2014	$5,500 per year	$11,000
2015	$10,000	$10,000
		$41,000
2016	$5,500	$5,500
		$46,500

REGISTRED RETIREMENT SAVINGS PLAN (RRSP) CONTRIBUTION LIMIT

Year	RRSP Contribution Limit	Earned Income Required in Prior Year
2014	24,270	134,833
2015	24,930	138,500
2016	25,370	140,945
2017	26,010	Indexed