
U.S. Taxation — Defining U.S Residency

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There are many Canadian residents who have some connection to the the United States (“U.S.”) and may be unaware that their income may be subject to U.S. taxation. Some may already know that Canada imposes tax based on residency, while the U.S. imposes tax on all U.S. persons. However, many may not be aware of who is considered a U.S. person and may unintentionally become non-compliant with U.S. individual tax filing obligations.

The consequences of failing to file U.S returns and forms may be severe, ranging from financial penalties to denial of entry into the U.S. Should the Internal Revenue Service (“IRS”) determine that a person has willfully failed to file a return, criminal penalties may result.

To assist in addressing U.S. individual tax filing obligations, this article provides information on U.S. persons, taxable income in the U.S. and tax filing requirements.

Who is a U.S. person?

In general, the following individuals may be considered U.S persons for tax purposes:

- < U.S. citizens (born in the U.S.) or Naturalized citizens (“NC”)*
- < Those with at least one parent who is a NC
- < Those born outside of the U.S. and who have at least one parent who is a U.S. Citizen**
- < Green card holders
- < U.S. tax residents
- < Those who elect to be treated as a U.S. resident
- < Those who are deemed to be a U.S. resident but who elect to be a non-resident of U.S.

One may also be considered as a U.S. tax resident if they are physically present in the U.S. for 183 days or more in the current year, or by meeting the Substantial Presence Test (“SPT”) by spending an average of 122 days or more in the U.S. for the three most recent prior years (more information on the substantial presence test is discussed in the article “Canadian Snowbirds in the U.S.”). Even if one meets any of the conditions above, they can still file an exception form or apply the Canada-U.S. Income Tax Treaty (the “Treaty”) to elect to be a U.S. non-resident.

Furthermore, there are options for U.S. non-residents to elect to be treated as U.S. residents if certain criteria are met.

* Naturalized citizens are foreign nationals who have acquired U.S. citizenship by meeting the requirements established in the U.S. Immigration and Nationality Act

** Generally, a child “acquires” U.S. citizenship if one parent was a resident in the U.S. prior to child’s birth and the parents were married at the time the child was born. If only one parent is a U.S. citizen, then one must consider the length of the parent’s period of residence in the U.S. prior to and after the child’s birth

What is taxable?

A U.S. person (including U.S. citizens and green card holders living outside of the U.S.) is subject to U.S. taxes on their worldwide income from all sources. Gross income is reduced by itemized deductions and personal exemptions to arrive at taxable income. Progressive tax rates are applied based on the income level and filing status of the tax return. Non-resident aliens of the U.S., who are non-citizens who don't have a green card and do not meet the SPT, are subject to U.S. income tax only on their U.S. source income (i.e. rental income from U.S. properties, U.S. employment income).

U.S. income tax filing requirements

Generally, the U.S. Individual Income Tax Return is due April 15th of the following year and there is an automatic extension of the filing deadline to June 15th for the U.S. persons living abroad on April 15th. However, the due-date for payment of any tax owing would remain April 15th. Late filing of the U.S. tax returns or late payment of the tax liability will be subject to a penalty with a maximum of 25% of the balance due. U.S. state tax returns may also be required depending of the State tax rules and sources of income earned by the individual.

U.S. foreign reporting requirements

In addition to the annual tax return filing obligations, U.S. persons are also required to file a number of reporting forms for assets held outside of the U.S. Please refer to the "U.S. Reporting Forms" table for further details. Failure to file these forms may result in significant penalties being levied.

Summary

The determination of U.S. residency can have significant tax implications.

Speak with your tax advisor to determine if you may have tax obligations in the U.S.