



**February 2009**

# U.S. TAXFACTS

## **CURRENT TOPICS IN U.S. & CROSS BORDER TAX**

Kotler van den Brink & Company has been providing U.S. and cross-border (Canada-U.S.) tax consulting and compliance services to accounting and legal professionals since 1988. Our practice has recently relocated and expanded. After a five year lapse, we have renamed our newsletter and are pleased to announce the re-launch of the **U.S. TAXFACTS** (formerly *U.S. TAXFAX*).

### **What is the U.S. TAXFACTS?**

The U.S. TAXFACTS is a newsletter that we developed to provide general information regarding typical cross-border tax situations that professionals in the Canadian market encounter on a regular basis. It is designed to alert you to issues and planning opportunities that will enable you to better serve your clients.

This edition will briefly discuss current U.S. tax issues that we are seeing in our practice. Future editions will cover these topics in much more detail. We have also attached a historical summary of the Canada - U.S. foreign exchange rates which we think you might find useful this tax season. Previous editions of this newsletter can be found on our website at [www.kvdb.com](http://www.kvdb.com).

### **Treaty Protocol Ratified in December of 2008**

The most important change to cross-border taxation in recent years is the 5<sup>th</sup> protocol to the Canada – U.S. Tax Treaty which was ratified in December of 2008. Most of the provisions will become effective January 1, 2009. If you are involved in cross border

transactions, it is imperative that the 5<sup>th</sup> protocol be reviewed.

### **Application for IRS Individual Taxpayer Identification Number (ITIN)**

The IRS introduced changes to the ITIN application process in 2007 which has made it more difficult and time consuming to obtain an identification number. A W-7 application must now (with limited exceptions) accompany a valid U.S. tax return at the time of submission. Processing time is 6 to 8 weeks and may take longer if the applications are not completed properly or are submitted without proper documentation. Kotler van den Brink & Company is a Certifying Acceptance Agent registered with the IRS to process W-7 applications.

### **Capital Loss Carrybacks**

Client portfolios declined substantially in 2008 due to the world economic crisis. For Canadian purposes, capital losses can be carried back 3 years to recover the taxes paid on capital gains in previous years. Caution should be exercised when carrying back capital losses in Canada for U.S. citizens. The U.S. does not allow capital loss carrybacks, only carryforwards. Consequently, a capital loss carryback on a Canadian individual income tax return will at the very least require an amendment of the corresponding year U.S. tax return to adjust foreign tax credits. It can also create a U.S. tax liability in the amended year if the foreign tax credits are no longer large enough to eliminate tax.

### **U.S. Citizens with Canadian Bank Accounts**

U.S. citizens or residents must file Form TD F 90-22.1 to disclose all non U.S. bank accounts if the cumulative amount in all foreign accounts exceeds

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\$US10,000 at any time in the year. This information form is due on June 30 without exception. The extensions which apply to U.S. income tax returns DO NOT apply to this information reporting form. For any clients that prepare this form themselves, it should also be noted that the form has been substantially revised for the 2008 tax year.

For forms filed after December 31, 2008, the IRS has indicated they will begin enforcing penalties on late filed forms. This is one of several areas in which the IRS appears to be taking a much more aggressive position in regards to U.S. citizens living in Canada.

### **U.S. Citizens with Canadian Corporations**

U.S. citizens or residents that own or control an interest in a foreign (non U.S.) corporation must file Form 5471 along with their individual income tax return, Form 1040. The IRS recently published its intent to automatically assess penalties for failure to file Form 5471 effective January 1, 2009.

In response to criticism of their inability to appropriately assess penalties, the IRS has begun mailing out notices to taxpayers that were previously late in filing these forms, informing them of the new automatic penalty.

### **State Tax Departments Sharpen Their Pencils**

Due to recent large budget deficits, many states are increasing collection efforts to help make up the short falls. The states are establishing programs to identify lack of compliance and unreported income tax and excise tax transactions. Many states are targeting internet sales activity to identify unreported sales and use tax transactions. State voluntary disclosure programs generally offer taxpayers the opportunity to come clean without the incidence of penalties. Unforeseen state tax liabilities can blindsides unsuspecting taxpayers.

### **Obama Tax Proposals**

U.S. tax practitioners are anxiously awaiting the effect of President Obama's economic recovery stimulus package. New credits and payments are expected to assist low income taxpayers and stimulate segments of the economy. Other taxes, including capital gains, are expected to increase. It is expected that the Estate tax will remain after 2009 - in what form, we can only guess. Current proposals will retain the unified credit exemption at 2009 levels of \$3.5 million as well as retaining the maximum estate tax rate of

45%. Corporate tax changes include enhanced depreciation rates and bonus depreciation for 2009. Another interesting proposal is to allow a 5 year carryback of net operating losses (currently two years). If the 5 year carryback is elected, taxpayers will have to permanently reduce the net operating loss by 10%.

### **Unexpected U.S. Estate Taxes**

As the aging population moves forward, tax practitioners are dealing with Estates much more frequently. Have you ever stopped to consider estate tax planning for your U.S. citizen clients? Often elderly couples pass away within years or even months of each other. Simple estate planning techniques can ensure that a U.S. citizen spouse does not inherit an unexpected U.S. estate tax liability from their non U.S. citizen spouse. Other simple techniques include doubling up on the tax-free estate tax exemption (currently \$3.5 million).

### **U.S. Vacation/Rental Homes**

With U.S. real estate values and interest rates at all time lows, Canadians are purchasing vacation properties in the sunbelt at record rates. Many clients are purchasing U.S. properties with the intention of renting them out now and enjoying them as their second home later in retirement. Most clients are alarmed to learn that they will incur a tax liability when they convert the rental property to a personal use property. Additionally, they are surprised to find out that interest paid on their Canadian mortgage credit lines is not deductible on their U.S. tax return. RESULT - current tax liability in the U.S. with no credit available in Canada. Bottom line is, don't let your clients make such a significant purchase without gathering the facts first.

### **Canadian Departures post September 17, 2000**

If you had any clients relocate to the U.S. after September 17, 2000, there is a substantial opportunity to increase the tax costs of assets held at the time of departure for U.S. tax purposes which may reduce U.S. taxes upon disposition of these assets. A future edition of U.S. TAXFACTS will discuss the changes to Article XIII of the Treaty included in Protocol 5 in detail.

*Please remember, the information presented is general in nature and does not constitute professional advice. It is recommended that accounting, legal or other professional advice should be sought before acting upon any of the information contained within this edition of the U.S. TAXFACTS.*



# KOTLER van den BRINK & COMPANY

Providing U.S. & Cross Border tax consulting and compliance services to other professionals since 1988

## CANADIAN - U.S. DOLLAR EXCHANGE RATES

	2008			2007			2006		2005		2004		2003	
	Yr.Over	Monthly	Month	Yr.Over	Monthly	Month	Monthly	Month	Monthly	Month	Monthly	Month	Monthly	Month
	Yr.Avg.	Average	End	Yr.Avg.	Average	End	Average	End	Average	End	Average	End	Average	End
JANUARY	1.0603	1.0111	1.0038	1.1355	1.1759	1.1770	1.1573	1.1390	1.2253	1.2412	1.2960	1.3248	1.5410	1.5215
FEBRUARY	1.0460	0.9991	0.9844	1.1384	1.1707	1.1366	1.1489	1.1366	1.2397	1.2335	1.3290	1.3357	1.5124	1.4840
MARCH	1.0322	1.0020	1.0265	1.1384	1.1682	1.1546	1.1574	1.1680	1.2161	1.2096	1.3284	1.3113	1.4759	1.4678
APRIL	1.0221	1.0139	1.0072	1.1397	1.1343	1.1101	1.1438	1.1180	1.2360	1.2585	1.3425	1.3721	1.4585	1.4334
MAY	1.0142	0.9994	0.9930	1.1392	1.0949	1.1015	1.1095	1.1015	1.2555	1.2552	1.3783	1.3634	1.3845	1.3685
JUNE	1.0101	1.0167	1.0197	1.1349	1.0652	1.1162	1.1138	1.1162	1.2402	1.2254	1.3577	1.3338	1.3523	1.3475
JULY	1.0070	1.0127	1.0240	1.1282	1.0503	1.0668	1.1292	1.1316	1.2227	1.2241	1.3219	1.3295	1.3815	1.4048
AUGUST	1.0067	1.0544	1.0620	1.1242	1.0582	1.0562	1.1183	1.1053	1.2040	1.1871	1.3117	1.3130	1.3957	1.3857
SEPTEMBER	1.0094	1.0583	1.0642	1.1165	1.0254	0.9948	1.1162	1.1177	1.1776	1.1627	1.2878	1.2616	1.3632	1.3499
OCTOBER	1.0269	1.1848	1.2045	1.1042	0.9752	0.9447	1.1286	1.1231	1.1776	1.1812	1.2469	1.2180	1.3218	1.3186
NOVEMBER	1.0478	1.2182	1.2370	1.0876	0.9671	1.0000	1.1362	1.1669	1.1811	1.1669	1.1961	1.1860	1.3126	1.2991
DECEMBER	1.0671	1.2345	1.2180	1.0740	1.0031	0.9913	1.1530	1.1654	1.1610	1.1630	1.2191	1.2020	1.3128	1.2965
	<b>2008</b>			<b>2007</b>			<b>2006</b>		<b>2005</b>		<b>2004</b>		<b>2003</b>	
Yearly Average:	<b>1.0660</b>			<b>1.0748</b>			<b>1.1341</b>		<b>1.2116</b>		<b>1.3015</b>		<b>1.4015</b>	

	2002		2001		2000		1999		1998		1997		1996	
	Monthly	Month	Monthly	Month	Monthly	Month	Monthly	Month	Monthly	Month	Monthly	Month	Monthly	Month
	Average	End	Average	End	Average	End	Average	End	Average	End	Average	End	Average	End
JANUARY	1.6003	1.5873	1.5032	1.4989	1.4489	1.4456	1.5192	1.5078	1.4408	1.4556	1.3486	1.3470	1.3665	1.3734
FEBRUARY	1.5958	1.602	1.5218	1.5361	1.4511	1.4496	1.4973	1.5078	1.4340	1.4237	1.3552	1.3679	1.3755	1.3704
MARCH	1.5870	1.5942	1.5585	1.5763	1.4606	1.4494	1.5175	1.5087	1.4163	1.4198	1.3718	1.3844	1.3653	1.3591
APRIL	1.5814	1.5685	1.5575	1.5366	1.4684	1.4801	1.4874	1.4570	1.4370	1.4370	1.3976	1.3400	1.3591	1.3620
MAY	1.5497	1.528	1.5415	1.5384	1.4955	1.4965	1.4620	1.4740	1.4450	1.4450	1.3805	1.3783	1.3690	1.3688
JUNE	1.5317	1.5162	1.5244	1.5141	1.4768	1.4806	1.4691	1.4630	1.4653	1.4653	1.3840	1.3805	1.3655	1.3637
JULY	1.5459	1.5829	1.5304	1.5325	1.4779	1.4870	1.4888	1.5063	1.4876	1.5119	1.3771	1.3783	1.3693	1.3747
AUGUST	1.5679	1.5588	1.5402	1.5508	1.4825	1.4715	1.4923	1.4925	1.5353	1.5685	1.3905	1.3878	1.3718	1.3683
SEPTEMBER	1.5758	1.5872	1.5677	1.5785	1.4862	1.5035	1.4768	1.4674	1.5213	1.5312	1.3869	1.3811	1.3692	1.3619
OCTOBER	1.5778	1.5575	1.5712	1.5887	1.5123	1.5225	1.4773	1.4713	1.5450	1.5429	1.3867	1.4084	1.3506	1.3383
NOVEMBER	1.5714	1.565	1.5924	1.5718	1.5422	1.5360	1.4675	1.4745	1.5394	1.5331	1.4133	1.4238	1.3384	1.3514
DECEMBER	1.5593	1.5776	1.5775	1.5928	1.5224	1.4995	1.4733	1.4433	1.5422	1.5333	1.4267	1.4305	1.3618	1.3706
	<b>2002</b>		<b>2001</b>		<b>2000</b>		<b>1999</b>		<b>1998</b>		<b>1997</b>		<b>1996</b>	
Yearly Average:	<b>1.5704</b>		<b>1.5484</b>		<b>1.4852</b>		<b>1.4858</b>		<b>1.4831</b>		<b>1.3844</b>		<b>1.3636</b>	