‘Don’t mess with the IRS’ and four other useful tax tips for snowbirds

As days grow shorter and nights get colder, things heat up for Canadian accountants who help snowbirds – Canadians 55 and older who spend at least 31 days down south to escape winter – deal with taxation questions. How long are they allowed to stay in the United States? What happens if they want to sell or rent out their oceanfront condo in Florida? And what exactly is a Form 8840 again?

Considering that snowbirds must grasp rules and regulations not only from Canada Revenue Agency but also the Internal Revenue Service south of the border, too, it’s little wonder so many are confused, confounded and asking for professional tax guidance. Here are five of the most common tax head-scratchers and concerns accountants are fielding questions about right now.

1. You can’t flub. At least, not any more

That’s right. There used to be a time when snowbirds could get, well, creative, at the border when telling Canada Border Services Agency officers how long they’d been sunning in Florida, Texas or Arizona. But now, with better communications technology and a push by the IRS to track tax residents, the organizations are able to more easily monitor comings and goings, and even financial holdings.

It makes sense. With approximately one million snowbirds entering the United States each year, there’s a lot of money at stake, which could help alleviate U.S. deficit and debt woes. Not that this reason makes it any easier on snowbirds, who find themselves meticulously tracking days and filling out forms each year.

“People who have been going down to the U.S. for years are suddenly saying, ‘What do you mean I have to change the way I do things?’” says Cleo Hamel, senior tax analyst for American Expat Tax Services in Calgary. “Information has always flowed back and forth between the countries, but now you can’t keep a secret any more.”

2. Do the math

So, exactly how long can you stay in the United States without tripping the tax wire? This is the main question Shawn Roussy, a chartered professional accountant and partner at Logan Katz in Ottawa, gets when he gives snowbird tax presentations these days. And the answer can be complicated.

“There’s a misconception out there that if you spend under 183 days in the U.S., then you’re okay. That’s actually incorrect,” he says.

While 183 days is the magic number for someone who visits for just one year, for snowbirds who travel down each winter, they need to use the IRS formula, called the “substantial presence test” to determine if they’ve become a U.S. tax resident.

It goes like this:

1. You have to be present in the United States for at least 31 days during the current year.

2. You also have to calculate the total days you've been there in the current year plus the two years before. They have to add up to at least 183 days.

3. You calculate that sum by counting all the days in the present year, one-third of the days in the prior year, and one-sixth of the days in the second year before the current year.

Clear as mud, right? So, just remember this: If you stay in the United States fewer than 120 days each year, you won't be considered a resident of the United States and typically won't have to file a U.S. tax return, unless you're renting out, buying or selling property. (More on that later.)

Just remember that even partial days stateside count as a full day (yes, that quick jaunt to Buffalo or Seattle counts) and you're counting a 12-month period, not a calendar year. So you can forget trying to divvy up the days by taking separate trips in December and February.

3. Don't panic, there's a form for that

Because there's a tax treaty between Canada and the United States, you'll never be double-taxed, but it's important to fill out the proper forms so as to not pay penalties and get into trouble with the IRS and CRA.

For example, a snowbird who discovers he's indeed a tax resident, because he meets the substantial presence test requirement, can fill out a two-page IRS document called the Closer Connection Exception Statement for Aliens, also known as Form 8840. You'll reveal where you live, work, vote, have a driver's license and bank, among other details.

Mr. Roussy says that many newbie snowbirds are unaware that they can bypass filing a U.S. tax return by simply filling out the 8840 each year.

"But the veteran snowbirds? They're all over this form," he says.

4. The $299,999 home

With the Canadian dollar weak and the U.S. real estate market rebounding, many Canadian snowbirds are thinking about selling their vacation homes. Unfortunately, they may have to pay a 10-per-cent withholding tax when the deed is done.

But there's a way of getting around that. If the home is worth less than $300,000 (U.S.) and it's sold to a U.S. citizen who plans to make it a permanent home, that tax is waived.

"Some people will lower their expectations on the sale price just to get below that $300,000 threshold," says Mr. Larson.

One more thing. If you'd rather rent out your U.S. house for part of the year to make some cash on the side, you're obligated to file not just a tax return in the United States but also include the earnings on your Canadian tax return as well.

"Many people think, oh, since it's in the U.S., I don't have to deal with it on my Canadian tax return, but you do. You're a Canadian tax resident," says Terry Ritchie, director of cross-border wealth services for Cardinal Point, a Canada-U.S. cross-border wealth management company in Calgary.

Snowbirds have to include the same profit and loss information on their T1, using a T776 – the Statement of Real Estate Rentals – in Canadian dollars. If the property is more than $100,000, they may be required to submit a T1135, the foreign income verification statement, as well.

Don't do it, and the CRA will impose a maximum penalty of $2,500 (Canadian).

5. Don't mess with the IRS

Speaking of penalties and proper tax filing, Ms. Hamel offers this advice for snowbirds who want to continue to enjoy their time down south: Don't cross the IRS.

"The CRA is a pussycat compared to the IRS," she says. "The CRA can freeze your bank account and there are anecdotes about them coming to your house, but it's actually hard to find proof of that. But in the IRS, they're more stringent. People who fear the IRS fear them for the right reason."

Even those who are doing everything right can find it challenging to deal with the U.S. tax agency. Mr. Larson admits he has spent 40 minutes on hold with them – only to get the message that the expected hold time is 60 minutes more. And getting written responses? That's another three to four months.

"I understand their budget hasn't gotten any bigger in 20 years," he says, diplomatically, "but in the meantime, you're in limbo."

Ultimately, snowbirds need to keep three rules in mind when it comes to tax time: File right. File on time. And don't even think about pulling any fast ones. Hiring an accountant to file a U.S. tax return typically costs between $400 and $1,000 each year, but it's likely money well spent.

"Look after yourself," says Ms. Hamel. "Make sure you're keeping track of days and filing appropriately – and you'll save yourself grief."