

TAX ALERT



TAX ALERT is a commentary on topics of current interest – usually topics relating to recent changes in tax law, new CRA administrative practices or current interpretations arising from tax cases. Professional advice should be obtained before acting on any of this information. *ed.1/08*

REPORTING FOREIGN PROPERTY HOLDINGS

Tax season always brings certain filing issues to light but the requirement to file form T1135 to report foreign property assets on your tax return is important but perhaps overlooked. This prompted us to revise a Tax Alert issued at the end of April 2007.

We strongly suggest that people with foreign investment portfolios and other foreign assets such as rental properties or inheritances, take a close look at their reporting obligations. Many portfolios may have foreign investments hidden in exchange-traded funds and other special structures. Your investment advisor should be able to help.

Foreign Property

Taxpayers are required to show at the top of page 2 of the personal return if they owned any foreign property (specified foreign property) with a total cost in excess of \$100,000 at any time in the year. If so, you must complete Form T1135. You must also report the location of such properties and the total income derived during the year. The same reporting applies to trusts, partnerships and corporations.

Reportable properties include the following:

- ◆ Shares of foreign corporations (investment portfolio)
- ◆ Foreign bank accounts
- ◆ Interest in foreign trusts (non Canadian mutual funds)
- ◆ Other foreign indebtedness (bonds, T-bills, loans etc.)
- ◆ Real estate
- ◆ Intangible property (patents, trademarks etc.)
- ◆ Tangible property (precious metals, gold certificates, futures etc.)
- ◆ Amounts owed to you by non-resident persons
- ◆ US treasury bills
- ◆ Shares of Canadian corporations on deposit with foreign brokers
- ◆ Foreign securities included in Exchange Traded Funds (ETF's)

There are several exclusions to the properties listed above some of which are as follows:

- ◆ Property used to carry on an active business
- ◆ Assets held in Canadian registered plans (RRSP's etc.)

- ◆ Property held *primarily* for personal use (vacation property, art, antiques etc.)
- ◆ An interest in a US Investment Retirement Account (IRA)
- ◆ Foreign securities contained in Canadian mutual funds

Portfolios

Taxpayers with large diversified portfolios should look at them to determine if they contain foreign securities. Ask your broker or investment advisor for a detailed list of foreign stocks and other foreign securities that you have owned. Exchange traded funds and similar investment structures may contain foreign securities you haven't considered

Detailed Rules

The rules are difficult and broad in application so taxpayers should take some time in deciding if they need to report. Following are some of the other rules.

- ◆ You must file Form T1135 if the aggregate *cost* of foreign assets exceeds \$100,000 *at any time in the year*
- ◆ Husband and wife report separately. Assets for each spouse could either include a 50 % interest in a jointly owned property or all of it depending on who paid for it.
- ◆ If you are not required to file a personal tax return, you still must file Form T1135 if it applies
- ◆ If you rent out your foreign condo more than you use it personally in any year, it would not be primarily used for personal use and therefore must be included in foreign assets
- ◆ Rental properties outside of Canada must be included
- ◆ You do not need to file Form T1135 for the year you move to Canada

Cost of Property

If you inherited property or received it as a gift, its cost is the value of the property when you received it. If you came to Canada owning foreign property, the cost is its market value at the time you immigrated to Canada. Be sure to convert foreign currency amounts to Canadian dollars in your reporting.

Form Details

Form T1135 requires you to list the major types of properties separately and asks whether the cost of your assets in each category exceeds or is less than certain levels (i.e. under \$100,000, over \$100,000, over \$300,000 etc.). This keeps the bookkeeping to a minimum. You must indicate the various geographical areas where all of the properties were located (United States, UK, Europe, other, etc.) but thankfully not on a property-by-property basis.

Penalties for Not Filing

If you *knowingly or through gross negligence* fail to file form T1135 a penalty of \$500 per month can apply for the first 24 months. The longer you hold off filing the higher the penalty can get. More severe penalties may apply to taxpayers and advisers if a false statement or omission is involved. The penalty increases after 24 months. The wording of the penalty section has a strong presumption of *intention* not to file and so if the form was simply not filed because you were unfamiliar with the broadness of the provision, hopefully CRA will see it that way too. For those who may want a reference, sections 162(10) and 163(2.4) have specific application.

Other Forms

CRA has new forms to file if you have loaned or transferred property to a non resident trust (Form T1141) or received property from or become indebted to a non resident trust (Form T1142).

Conclusion

Taxpayers with large portfolios should do a serious review of their investments to see if they should be filing Form T1135. Investment advisers should be able to help. If you rent out your vacation condo you may need to include it too. Sooner or later CRA is going to make this an audit target so be ready!

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