JOHNSEN ARCHER LLP

TAXATION · ACCOUNTING · ASSURANCE

RECENT CHANGES TO THE US TAX LAW

Dear Valued Client:

I hope all is well and that you had a great Holiday season and a Happy New Year.

You may have read in the news that the U.S. passed a fairly significant tax reform bill in December 2017 that will generally become effective for the 2018 tax year and forward. This tax reform bill may have impacts on you, your family members, and/or your business partners.

For your convenience, we have asked one of our U.S. cross border tax specialists to highlight some of the key implications to folks living in Canada:

Are you a U.S. citizen or U.S. green card holder living in Canada?

- Overall Lower U.S. Individual Tax Rates Structure – This will likely not benefit U.S. citizens or green card holders living in Canada much as the Canadian individual income tax rates are likely going to be higher than the U.S. individual income tax rates. As such, U.S. citizens or green card holders living in Canada will end up paying the higher of the two countries' rates –most likely Canada in this case.

- Imposition of a One Time Acceleration of Tax on Deferred Profits of a Canadian Corporation - For U.S. citizens or green card holders living in Canada who own 10% or more of a Canadian corporation which is considered a controlled foreign corporation (e.g. a corporation controlled greater than 50% by vote or value by U.S. citizens or otherwise U.S. tax residents) with undistributed retained earnings - the new law triggers a deemed dividend for all the corporate E&P of the company. There is an effective 15.5% tax on cash and cash equivalents and an 8% repatriation tax on illiquid assets. There is a deferral election where you can defer the inclusions over eight years. A simple, but common, example of these implications: A doctor who is a U.S. citizen living in Canada has been working and accumulating earnings in his/her 100% owned medical corporation over the last several years and investing it for their eventual retirement. With this new U.S. tax reform bill - this doctor will have to include the entire company's retained earnings as personal taxable income on his/her U.S. individual income tax return in 2018 (the income can be elected to spread out equally over 8 years) as a deemed dividend. If he/she does not do proper planning between their U.S. / Canadian income tax, it can result in potentially double taxation on this income.
  This can be very punitive to you if you are a business owner in Canada who is a U.S. citizen or green card holder. There are some potential tax planning strategies to mitigate the effect of this new rule but they have to be implemented proactively.

- Increased Estate and Gift Tax Exemptions – The U.S. doubled the exemption thresholds for the U.S. estate and gift tax which reduces the amount of estates that will be subject to the U.S.

doubled the exemption thresholds for the U.S. estate and gift tax which reduces the amount of estates that will be subject to the U.S. estate tax. If you haven't reviewed your estate planning recently, it might be a good idea to reevaluate your planning under these new rules. Are you a Canadian (not a U.S. citizen or U.S. green card holder) with investments, real estate, or business activity in the U.S.?

- Lower Corporate Income Tax Rates – The U.S. reduced the Federal corporate tax rate to a flat 21% compared to a tiered rate system that had a max rate of 35%. This brings the U.S. Federal corporate tax rate more competitive with the Canadian corporate tax rate. Historically, the U.S. corporate tax system was punitive with the high tax rates so a lot of planning was done with transfer pricing or other complicated partnership structures to mitigate this effect. With the reduced Federal corporate tax rate, if you have investments, real estate, or other business activity in the U.S., you may want to reconsider your overall cross border tax structure. Please note that there were no changes with the state income tax expense – if your U.S. investments / business activity is in a state tax has a corporate tax rate then this should be considered in addition to the Federal tax planning.
- Net Operating Loss Carryover Limitations – Net operating loss deductions are now limited to 80% of the current year taxable income. For example; if you have a $100k net operating loss carrying forward from a prior tax year in the U.S. but you show a 2018 taxable income of $10k - the corporation would still have $2k of taxable income for 2018 – the rest of the loss would then continue to carry forward to offset 80% of future years. This should be taken into account for cash flow and income allocation planning.
- Increased Estate and Gift Tax Exemptions – The U.S. doubled the exemption thresholds for the U.S. estate and gift tax which reduces the amount of estates that will be subject to the U.S. estate tax. If you haven't reviewed your estate tax planning for your assets subject to U.S. estate tax recently (for example - if you own U.S. real estate, U.S. securities held individually, in a brokerage account and/or RRSP account, cash in a U.S. bank account, a note receivable to a U.S. resident, or other U.S. situs assets), it might be a good idea to reevaluate your planning under these new rules.

As we mentioned, this U.S. tax reform bill has a number of significant changes which may have impacts on you, your family members, and/or your business partners. Our intention of this overview was not to provide you with any specific U.S. income tax planning – but to alert you to some of the resulting changes that may affect your worldwide tax situation. If you would like to discuss how this tax reform bill might have an effect on your personal / corporate tax situation and discuss possible planning opportunities that may be available, please let us know and we can arrange a time for a planning discussion with one of our U.S. cross border tax specialists.

As always, we thank you for your business.

Your JA Team
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