RBC Wealth Management Services

The Navigator

IRS Reporting for U.S. Persons with RRSPs and RRIFs

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U.S. Form 8891 – U.S. Information Return for Beneficiaries of Certain Canadian Registered Retirement Plan

If you are a U.S. person and the annuitant of a Canadian Registered Retirement Savings Plan (RRSP) or Registered Retirement Income Fund (RRIF) you should be aware of the U.S. tax and filing requirements that apply to these plans. A U.S. person includes a U.S. citizen, U.S. green-card holder or a U.S. resident (e.g. a Canadian who moves to the U.S.).

The Internal Revenue Service (IRS) requires a U.S. person who is the annuitant of an RRSP/RRIF to complete and file IRS form 8891 (U.S. Information Return for Beneficiaries of Certain Canadian Registered Retirement Plans) annually for U.S. federal income tax purposes in order to disclose information about the plan. The information that must be disclosed for each RRSP/RRIF is the plan balance at the end of the year, distributions received from the plan during the year and in certain cases contributions made to the plan.

Form 8891 also can be used to make an election pursuant to Article XVIII(7) of the Canada-U.S. income tax treaty to defer U.S. income tax on income earned by an RRSP/RRIF that has been accrued, but not distributed. Although for Canadian tax purposes income and gains earned in an RRSP/RRIF are tax deferred until distributions are made, for U.S. tax purposes a deferral is only permitted when an election on form 8891 is made. When an election is not made, income and gains earned must be disclosed on form 8891 and included as taxable income on your U.S. income tax return. This may result in double taxation due to the possible timing mismatch between Canadian and U.S. income tax rules for reporting the income and gains in your RRSP/RRIF.

Note: This article is for information purposes only and does not provide tax or legal advice. You should obtain professional advice from a qualified tax or legal advisor specializing in cross-border tax to assist you with any

A separate form 8891 must be filed for each RRSP/RRIF.

questions on the topics discussed. This will ensure that your own circumstances have been considered properly and that action is taken on the latest information available.

Filing Requirements of Form 8891

Form 8891 and its general instructions can be downloaded from the IRS website: www.irs.gov.

A separate form 8891 must be filed for each RRSP/RRIF. If you and your spouse file a joint U.S. income tax return, each of you must file your own form 8891 for the RRSP/RRIF of which you are the annuitant.

The IRS has indicated that taxpayers must retain supporting documentation for the information required to be reported, including RRSP contribution receipts, Canadian tax slips T4RSP, T4RIF or NR4, and periodic or annual statements issued by the custodian of the RRSP/RRIF.

Annuitant and Beneficiary is One and the Same Person

Assistance from your tax advisor in completing form 8891 is highly recommended due to the complexities. For example, the general instructions for completing the form make a distinction between the “annuitant” and the “beneficiary” of the RRSP/RRIF. The instructions define “beneficiary” as a person who has to pay U.S. income tax on RRSP/RRIF investment earnings if a treaty election is not made and “annuitant” as an individual who is designated under the RRSP/RRIF as the annuitant.

Although the definitions in the general instructions appear to indicate the annuitant and beneficiary are two separate individuals, they are actually one and the same. Therefore, you may follow the instructions for the beneficiary, which require you to provide treaty-election information in section 6 of form 8891, instead of following the instructions for the annuitant, which skip the treaty-election procedure.

Election to Defer U.S. Tax on Accrued Income in RRSPs/RRIFs

To make a valid treaty election, attach a completed form 8891 to your U.S. income tax return (form 1040) annually. Since the election allows you to defer U.S. taxation of income accrued in your RRSP/RRIF until distributions are made, the taxation of distributions from your RRSP/RRIF will be realized in the same taxation year for both Canadian and U.S. income tax purposes. This enables you to claim a foreign tax credit on your U.S. income tax return, which reduces the potential for double taxation.

If you decide not to make a treaty election to defer tax, you must report the undistributed earnings in section 10 of form 8891 and on your U.S. tax return (form 1040).

Note: If you live in the U.S. in a state that levies income tax, you should be aware that although you are required to complete form 8891 for U.S. federal tax purposes, certain U.S. states may not allow a tax-deferral on income accrued in your RRSP/RRIF. These states do not accept form 8891. As a result, income and gains accrued in your RRSP/RRIF may be taxable on an annual basis for U.S. state tax purposes, even if there is a tax-deferral for U.S. federal tax purposes. In this case, double taxation may occur. Speak to a cross-border tax advisor if you live in the U.S. and are uncertain of the tax obligations for your RRSP/RRIF under U.S. state tax laws.

> If you are a non-resident of Canada when the distributions are made, you will be subject to non-resident withholding tax at source.

Canadian Tax on Distribution from Your RRSP/RRIF

For Canadian tax purposes, you are able to deduct RRSP contributions on your Canadian tax return based on your RRSP deduction limit. However, when distributions are made from your RRSP/RRIF, the whole amount distributed is subject to taxation in Canada.

Distributions made to residents of Canada are reported on their Canadian income tax return and together with other taxable income are subject to tax at graduated tax rates.

If you are a non-resident of Canada when the distributions are made, you will be subject to non-resident withholding tax at source and are not required to file a Canadian income tax return. The Canadian non-resident withholding tax rate is 25%. This rate may be reduced if there is a tax treaty with the foreign country. For example, the Canada-U.S. income tax treaty reduces the rate to 15% for distributions made to residents of the U.S. where the payments qualify as "periodic pension payments". Periodic pension payments generally include payments from a RRIF during the calendar year that are less than the greater of i) twice the minimum withdrawal required for the year or ii) 10% of the fair market value of the RRIF at the beginning of the year.

It is possible for non-residents of Canada to elect under section 217 of the Canadian Income Tax Act to file a Canadian s.217 non-resident income tax return to report the RRSP/RRIF income. This return allows for the distributions to be taxed at graduated tax rates on a Canadian income tax return as opposed to a fixed non-resident withholding tax rate. Note that the graduated tax rates used to calculate the Canadian tax liability takes into account your worldwide income level. This may result in a higher effective tax rate than the fixed non-resident withholding tax rate. Therefore, electing to file a Canadian s.217 tax return may only make sense if the tax at graduated tax rates is lower than the tax at the fixed non-resident withholding tax rate. The election to file a Canadian s.217 return is completely voluntary. You should discuss with your tax advisor whether it makes sense for you to make this election.

U.S. Tax on Distribution from Your RRSP/RRIF

For U.S. tax purposes, contributions made to your RRSP are not tax-deductible (except for contributions to group RRSPs). For this reason, the portion of the RRSP/RRIF distribution relating to non-deductible contributions is generally not taxable when withdrawn. The non-deductible contributions form part of what is referred to as your "basis" in the RRSP. In other words, the basis in the plan is the portion that is not taxable. If you do not make an election with form 8891 to defer taxation of the income accruing in an RRSP/RRIF the income that is taxed annually for U.S. tax purposes is also added to your basis in the plan.

When distributions are made from your RRSP/RRIF, you will be required to calculate the taxable portion taking into consideration your basis in these plans. A discussion of the complex calculation used to determine the taxable portion of the distributions is beyond the scope of this article. You should seek professional tax assistance from your cross-border tax advisor, who can assist you with the calculation.

The taxable portion is reported on form 8891 and on your U.S. income tax return and will be subject to U.S. income tax. To reduce or eliminate double taxation you can claim a foreign tax credit on your U.S. tax return for the Canadian tax incurred.

Canadians with large accrued gains in their RRSP/RRIF who are planning to move to the U.S. should consider whether it makes sense to increase their basis in the plan to potentially reduce their exposure to U.S. taxation. The basis in the plan can be increased by selling and repurchasing assets in the RRSP/RRIF before you leave Canada. Note: the sale and repurchase of securities in an RRSP/RRIF will not trigger Canadian income tax but there may be service/commission fees incurred. Before you move to the U.S., speak to your tax advisor for guidance on whether this strategy for increasing the basis in your RRSP/RRIF is appropriate.

Please contact us for more information about the topics discussed in this article.

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