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“Our mission is to help you find your path to success.”

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Index

- Mistakes Canadians make with U.S. taxes
- Update on COVID-19 federal government support
- Preserve Cybersecurity While Working Remotely
- Cleaning out your financial closet under quarantine

Mistakes Canadians make with U.S. taxes



Tax requirements in the United States are quite different than those of other countries around the world. This article will outline some of the common mistakes Canadians make when it comes to U.S. taxes. Do you recognize yourself in any of these scenarios ...?

Not filing a U.S. tax return when required

The United States is one of the few countries in the

world that imposes taxes on citizenship as well as residency and source of income. Other countries typically tax based only on residency and source of income.

If someone is a U.S. citizen or a U.S. green card holder (also known as a U.S. lawful permanent resident), they are required to file a U.S. resident return (Form 1040), even if they are living outside of the U.S. Their worldwide income is reported on Form 1040, and the use of mechanisms such as the foreign earned income exclusion or foreign tax credits will reduce or eliminate double taxation on the income reported in both countries.

Being physically present in the United States can also trigger a U.S. tax filing requirement. The substantial presence test involves a calculation based on the past three years of physical presence in the United States. Generally, each day in the current year counts as a full day, each day in the first previous year counts as one-third of a day, and each day in the year before that counts as one-sixth of a day. If the calculated number of eligible days is 183 or more, then the individual meets the substantial presence test, is considered a U.S. tax resident and must file a U.S. tax return.

Corporations or partnerships may also have U.S. filing requirements if they earn revenues from U.S. sources. Corporations must still file a Form 1120-F with a *Treaty-Based Return Position Disclosure* (Form 8833) if they are taking a treaty position that their business profits are only taxed in the country where it is permanently established.

Not filing the correct forms

Individuals meeting the U.S. substantial presence test are considered U.S. tax residents and by default would be required to report their worldwide income on a Form 1040 return. However, you can file as a U.S. non-resident and only be subject to U.S. tax on your U.S.-sourced income. If you meet the substantial presence test and are physically present 183 days or more in the current year alone, you must file a Form 1040NR return with a Form 8833 treaty position in order to be treated as a U.S. non-resident for tax purposes.

Alternatively, if you meet the substantial presence test and are physically present less than 183 days in the current year alone, the *Closer Connection Exception Statement* (Form

8840) may be all that is required, unless you had income from U.S. sources, in which case you should attach the Form 8840 to a Form 1040NR.

It should be noted that the treaty positions do not preclude the individual from other U.S. resident required tax filings such as the *Reporting of Foreign Bank and Financial Accounts* form (FBAR).

Not only could there be a U.S. federal tax filing to complete, you may also need to complete various state tax filings. Each state has their own rules on individual filers, as well as different registration and reporting requirements for corporations or partnerships doing business in each particular state. Corporations or partnerships may also have U.S. payroll reporting, Form 1099 reporting, or Form 1042-S reporting to complete if they have U.S. employees or contractors.

Unknown exposure to U.S. estate taxes

Even though an individual may not be a U.S. citizen or green card holder or meet the U.S. substantial presence test, they may still have assets south of the border that expose them to U.S. estate tax liabilities. If you fit this description, know that the U.S. federal estate tax employs a graduated rate that can reach as high as 40%. There may also be additional state estate taxes.

An obvious way you may have U.S. estate tax exposure would be if you own U.S. real estate. U.S. taxes will apply to the fair market value of this investment.

A perhaps not-so-obvious area of U.S. estate tax exposure would be if you hold securities or stocks of U.S. companies inside a Canadian brokerage account. Canadian mutual funds that hold shares of U.S. companies would not be classified as “U.S. situs property,” but the direct stocks of those companies would. These investments would be subject to U.S. estate taxes on their fair market value, not just on the gain portion of the investments.

U.S. non-residents can take a treaty position to claim a pro-rated unified credit exemption to gain some relief from U.S. estate taxes. This formula consists of U.S. situs property over worldwide assets multiplied by the unified credit exemption limit (\$11,580,000 USD for 2020). To rely on this treaty position, you must arrange to have Forms 706-NA and 8833 filed nine months after the date of death of the estate owner (unless an extension was granted), even if no U.S. estate tax is due. Without this treaty position, you are entitled to a credit of \$13,000 USD, which exempts \$60,000 USD in value of U.S. situs property from your U.S. estate tax obligation.

You can correct your mistakes

To avoid the large penalties that could be assessed on late or incorrect filings, you can catch up and correct delinquent tax filings without fear of penalties. Voluntary disclosure programs and delinquent filing programs are available through some states and the Internal Revenue Service (IRS). However, you are advised to do so as soon as possible, as it has been mentioned that these programs may not be available in the future.

If you have U.S. estate tax exposure, you can use one or more of these remedies:

- You could liquidate your U.S. situs property or limit the amount you purchase or gain in future.
- Utilize a trust structure to hold the U.S. situs property.
- Secure sufficient life insurance to cover any U.S. estate tax exposure.

Whether you have committed one or more of these common mistakes, forewarned is forearmed when it comes to preventing and correcting them going forward. There may be other U.S. tax implications in your situation not covered here. If you want to be more certain about your situation, talk to a professional who specializes in U.S. taxes.

Update on COVID-19 federal government support



As was covered in the last issue, the COVID-19 pandemic has resulted in unprecedented strains on our economy and our personal financial situations. The federal government announced several programs offering targeted support for individuals, businesses and other organizations. The following outlines the updates and amendments to these programs from May 13 to July 1.

All individuals

The government had extended the filing deadline for most personal tax returns from April 30 to June 1; on May 25, it announced that it will not assess late filing penalties if those returns are filed by September 1, which is also the date by which any balances due must be paid.

Extending the deadline for filing personal tax returns would normally mean delays in the 2020/21 Goods and Services Tax credit, Canada Child Benefit and Guaranteed Income Supplement (GIS) payments, which all start in July 2020 and are based on net income reported on the 2019 tax return. However, estimated payments based on 2018-reported net income will continue until the end of September 2020. If you are eligible for these benefits, file your 2019 tax returns as soon as possible to avoid an interruption in these benefits.

The previously announced Canada Emergency Response Benefit (CERB) provides \$500 per week for up to 16 weeks to eligible workers who have stopped working or whose work hours have been reduced because of COVID-19. The federal government announced in June that these payments will be extended by an additional eight weeks to August 29. The draft legislation released on June 10 included additional flexibility, e.g., for short-term loss of employment, as well as restrictions intended to encourage those receiving the benefit to seek employment.

The Canada Revenue Agency (CRA) released guidance on international tax issues raised by the crisis. For example, while residency for income tax purposes is normally a question of fact, a “sojourner” who is physically present in Canada for 183 days or more in any taxation year will be deemed resident throughout the year and is therefore taxable in Canada on their worldwide income. When an individual has remained in Canada and is unable to return to their country of residence solely because of the COVID-19 travel restrictions, the CRA will not count those days towards the 183-day limit for deemed residency. The CRA may apply similar flexibility to corporate residency issues on a case-by-case basis, and to whether a corporation is carrying on a business or has a permanent establishment in Canada.

Students

The Canada Emergency Student Benefit (CESB) opened for applications on May 15. It provides support to students and new graduates, who are not eligible for the CERB or Employment Insurance benefits, or who are unable to work due to COVID-19; from May to August 2020, the CESB will be \$1,250 per month for eligible students or \$2,000 per month for eligible students with dependents or a disability. Students can earn up to \$1,000 during each four-week period without affecting their CESB eligibility.

Applications for the new Canada Student Service Grant (CSSG) opened on June 25 to students who choose to do national service and serve their communities. It will provide grants of between \$1,000 and \$5,000 based on the number of hours they serve.

Seniors and people with disabilities

Seniors who are eligible for the Old Age Security pension (OAS) will receive a one-time tax-free payment of \$300 in early July; those who also receive the GIS will receive an additional \$200.

Individuals who hold a valid Disability Tax Credit certificate as of June 1 will also receive a one-time tax-free payment of \$600; if they also receive both the OAS and GIS, they will receive an additional \$100, while those who receive only the OAS will receive \$300.

Small business

The CRA has further extended the due date to September 1 for corporations to file a T2 tax return and for trusts to file a T3 tax return, which would have been due in June, July or August. The government also announced support for the new Business Resilience Network operated by the Canadian Chamber of Commerce, which provides financial planning advice and information about tax rules and government programs to small- to medium-sized businesses, not-for-profit organizations and charities.

Support to fill wage gaps

The Canada Emergency Wage Subsidy (CEWS) enables eligible employers to re-hire their employees and avoid layoffs. Since it was first announced, the program has broadened its definition of “eligible employees” and been extended from a June 6 to an August 29 end date, along with other amendments to increase access and clarify eligibility requirements.

Loans for small businesses, not-for-profit organizations and commercial property owners

The federal government provides interest-free loans of up to \$40,000 for small businesses and not-for-profit organizations through the Canada Emergency Business Account (CEBA). To qualify, the organization must have had 2019 payroll expenses of between \$20,000 and \$1.5 million. In June, access to the CEBA was extended to businesses with payroll of less than \$20,000 and eligible non-deferrable expenses of between \$40,000 and \$1.5 million; this makes the program accessible to sole proprietors earning business income directly and to family-owned corporations that remunerate through dividends rather than payroll.

The Canada Emergency Commercial Rent Assistance (CECRA) program provides support to commercial property owners who forgive a portion of the April, May and June rent of eligible small business tenants. Applications opened in late May. On June 30, it was announced that the CECRA would be extended for the month of July. Businesses located on federal lands, such as national parks and historical sites, will also be eligible for rent relief on terms similar to those of the CECRA.

Programs for other circumstances

The previous article identified targeted programs to meet the needs of organizations that do not qualify for other COVID-19 programs or that are considered to need more support.

- Additional support has been announced through the Women Entrepreneurship Strategy Ecosystem Fund.
- A new Emergency Processing Fund will provide funding for up to 50% (25% for larger enterprises) for eligible COVID-19 response and strategic investment expenditures incurred by small- and medium-sized enterprises in the agricultural

food processing or manufacturing industries. Applications must be processed by July 31.

- Support will also be available to fish, seafood and aquaculture processors through the Canada Seafood Stabilization Fund, and to the tourism industry through the Atlantic Canada Opportunities Agency and through Canada Economic Development for Quebec Regions.

As these programs are being updated or amended frequently, please check www.canada.ca for the most current information.

TECHNOLOGY

Preserve Cybersecurity While Working Remotely



Most organizations have moved their workforces to some form of remote work as a result of the COVID-19 pandemic. Surprisingly, remote work has proven effective for many organizations, and they are now contemplating updating their remote work policies to allow employees more flexibility in a post-COVID-19 world. However, from a cybersecurity standpoint, remote work presents unique challenges and risks.

Employees may be accessing sensitive corporate data from their personal devices, or they may be using company-issued devices for corporate *and* unauthorized personal use. In both instances, hackers will prey on these distracted employees: sending them phishing emails in hopes of gaining access to the organization's network, or stealing credentials which they sell to criminals who may then launch cyberattacks.

Use these technical tips for a more secure network

That said, there are some basic steps organizations can take to improve their cybersecurity posture. Here are few technical steps you can use as a good starting point.

1. **Multi-factor authentication (MFA).** Having a strong password is no longer sufficient. Organizations that allow employees to access their work accounts with a simple username and password often fall prey to hackers. If hackers steal a user's credentials, MFA will offer an extra layer of protection since the hacker will not be able to access the additional unique, randomly-generated code.

The extra step in the MFA process could be an email or text message confirmation, a biometric method, such as facial recognition or a fingerprint scan, or something physical like a USB fob.

2. **Updates and patches.** During the pandemic, most IT departments were focused on moving a large portion of the organization's workforce to remote work. This may have put other IT tasks on hold, such as patching and implementing non-critical updates.

Hackers will take advantage of this delay to access networks and potentially steal data. Thus, implementing any updates and patches as quickly as possible should be a priority.

3. **Securing home routers.** Employees working from home are relying on the Internet and Wi-Fi access at their residence. Did they change their router password after it was first installed? If not, their home network may be vulnerable.

It is important to take simple steps to protect home networks and prevent hackers from having access to connected devices. While changing a router password is a good first step, your employees should take additional measures. For example:

- Ensure that firmware updates are installed, so that security vulnerabilities can be patched.
- Make sure the encryption is set to WPA2 or WPA3.
- Restrict inbound and outbound traffic.
- Use the highest level of encryption available.
- Switch off WPS.

Employees needing help with these measures should connect with your IT department.

4. **Beware of remote desktop tools.** Many employers allow staff to access their work networks via remote desktop protocols ("RDPs"). While this access method *can* be secure, several studies have found security problems with some of the most popular RDP tools for Linux and Windows. Ensuring that these tools are properly configured and tested for security is a critical step to take.
5. **Strong password protocols.** Everyone knows the importance of having strong passwords. Unfortunately, many still use the same password across multiple accounts. This means that all it takes is one compromised password for a criminal to take over all accounts associated with that user. They take leaked usernames, passwords, and attempt to log into other online accounts, a tactic commonly known as "credential stuffing."

Passwords should be unique for every account and should comprise a long string of upper- and lower-case letters, numbers and special characters. Additionally, organizations should consider implementing shorter periods for password resets, for example, going from a 90-day to a 30-day reset cycle.

Help your employees stay “cyber-vigilant”



While implementing strong technical safeguards is essential to having a strong cybersecurity posture, the most important risk to organizations remains its people, when they fall victim to phishing campaigns.

Phishing emails are sent by hackers to steal information that can be used in further targeted phishing attacks, credit card and wire fraud, and in installing malicious

software on the victim’s device or on the networks they access.

During this pandemic, there has been a marked increase in the number of phishing campaigns that target remote workers in a bid to steal their personal information or gain access to company accounts.

The key to avoiding this vulnerability lies in employee training and reminders to constantly be vigilant. For example:

- If an email appears unusual or requests immediate action (even when it comes from a “known” source), your employees should have the reflex to pause and proceed carefully.
- If the email contains a URL, they should know to hover their cursor over the link to validate the source, and to not open any unexpected attachments.
- If they suspect that they may have inadvertently fallen for a hacker’s ruse, their reflex should be to immediately report the incident to IT, rather than trying to resolve the issue themselves or ignoring it.

The pandemic has shown that remote work is an effective way for organizations to continue operating, so it is likely that some form of remote work will be part of how organizations operate in the future. That said, being aware of the risks and taking some basic steps can significantly reduce your chances of becoming victim of a cyberattack while working remotely.

WEALTH MANAGEMENT

Cleaning out your financial closet under quarantine

Sheltering in place has been tough; not being able to meet with family or friends, nor being able to step outside your home for a break required us all to adjust. There were some positives to the lockdown, though, including finishing off home projects you've been putting off. Another "to-do" that you might want to think about is whether there have been changes in priorities that could impact your financial affairs.

If you haven't addressed this yet while spending more time at "home base," here are some recommendations which I hope will inspire you to get organized, feel empowered and emerge confident in your financial future.

Review your spending, saving and cash on hand

The recent pandemic and the economic shock that ensued certainly made clear that having an emergency cash on reserve for times like this is highly important. The idea behind an emergency fund is to see you through a period of uncertainty concerning your employment or health, without the need to run up debt or tap into your retirement savings.

For the size of your emergency fund, recommendations vary from three months to a year of expenses. The amount will vary based on your specific circumstances; however, at a bare minimum, you should store away three months of spending for a "rainy day," like the type of events we've seen during COVID.

Building an emergency fund and creating sustainable wealth requires that you calculate and understand the most material parts of your cash flow situation. Here is an example of how to make this calculation, along with some comments to make the process easier.

An easy way to calculate your cash flow

Annual estimate	Cash flow example	Adam's comment
Income \$	\$100,000	T4 income on your last tax return will do, or you can calculate annual income based on your most recent pay stub
Taxes \$	\$23,708*	Use the Ernst & Young combined income tax calculator to calculate your expected taxes based on your income estimate
Savings \$	\$12,000	You might save a monthly amount, say, of \$1,000 per month, or instead do a lump sum for \$12,000 at the RRSP deadline each year
Spending \$	\$64,292	(Assuming you are not hiding money under your mattress), this figure is the result after deducting your taxes and savings from your annual income

* This tax figure is for an Ontario resident in the 2020 tax year

Revisit your investment plan

You are likely contributing the savings you are setting aside to a Registered Retirement Savings Plan (RRSP) or a Tax-Free Savings Account (TFSA). These are tax-efficient investment accounts and a good place to grow your savings. If the recent downturn in the stock market had you up all night, then it is likely that your investment plan does not fit your expectations. Your investment plan should be based on two key, interrelated factors: your ability to tolerate risk (facts about you, such as your age) and your willingness to tolerate risk (feelings you have, such as whether investment risk makes you anxious).

If you set your investment plan up correctly, then even in challenging markets like we had recently, being clearer on your expectations should help quell any anxiety.

Protect your family through an insurance and estate plan

Protecting your family from the COVID-19 virus has been a priority for many parents and families recently. Purchasing face masks, hand sanitizer and disinfecting wipes are some of the investments many have made to combat the virus. Over the long term, life insurance coverage is something that can protect your family as well.

Although we don't like to ponder our mortality, the recent pandemic has obviously made us hyperaware of the fragility of life. Given the current situation, today, many insurance companies are providing life insurance coverage faster and easier than ever before. Since having a paramedical nurse come to your house to take your blood, etc. is no longer acceptable in the time of COVID, you can now acquire up to \$2 million in life insurance coverage simply through a telephone review with a nurse.

Are your documents in order and easy to find?

Just as you would organize the garage or kitchen cupboard, make sure you sort and store your financial records (i.e., will, insurance policies, investment statement and online passwords) in a safe place. Why is this important? If you happen to pass away, your loved ones and executors will need to be able to retrieve these documents to deal with your estate efficiently.

If you have been avoiding completing or updating your will and power of attorney, now is always the right time to engage a lawyer to help you complete those critically important documents. A will and power of attorney don't just protect and organize your financial assets; they also ensure that any dependents you have (your children) go to the care givers you designate.

Also, make sure to review the beneficiaries on your registered investment accounts (RRSP, TFSA, etc.) to ensure that you have designated a specified living beneficiary. Updating this information could save your estate and loved ones thousands of dollars in unnecessary tax.

Take the next steps – a financial advisor can help

Not comfortable cleaning out your own financial closet? Don't have an investment plan in place? Now's a good time to get one! Then, consider meeting with a financial professional who can establish a financial and investment plan so that you will know what to expect. At my investment practice, we create financial and investment plans for each of our clients. As a result, our clients understand what they can expect from their wealth in challenging times and the potential risks to their plans. In the end, our clients are more confident in their future and walk away with the "peace of mind" of knowing they can weather future events like COVID-19.

To learn more about how you can become more confident and comfortable in your financial future, contact a financial advisor.

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