



# Foreign Properties: To Report or Not Report?

## FORM T1135

**C**anadian residents are taxed on income earned worldwide.

In the last few years, CRA has been concerned that

- Canadians would invest offshore and not report the income, or
- new immigrants to Canada would maintain assets in their country of origin and not report the income.

At the more sophisticated level, the concern is that complex tax schemes are designed to move funds to offshore trusts, using tax plans that are sound, but then CRA would lose track of the funds transferred and potentially lose the income tax on the earned income.

In 1996, CRA announced a new set of rules designed to require the reporting of offshore investments, transfers, and income. The rules impose substantive reporting requirements and significant penalties for failure to comply.

The rules encompassed the following transactions.

- Transfers and loans to foreign trusts
- Distribution received and debts to foreign trusts
- Foreign property holdings

Starting in 1998, every Canadian resident who met the requirements had

to file separate forms with CRA, form T1141, form T1142, and form T1135. If the taxpayer did not have to file a tax return because no tax was payable, those forms still had to be filed.

For the 2014 taxation year, the rules are still in effect but the form T1135 requires more detailed information to be reported. For the purpose of this article, we will focus our attention on the requirements of form T1135.

**In 1996, CRA announced a new set of rules designed to require the reporting of offshore investments, transfers, and income.**

Canadian resident individuals, corporations, and trusts that hold “specified foreign property” with an aggregate cost amount of more than CAN\$100,000 at any time in the year are required to file form T1135.

- For individuals, the form is due on the same day as the personal tax return (April 30 or June 15 for self-employed individuals and their spouses).
- For Corporations and trusts, the form is due when their tax returns are due.

New immigrants do not have to file the form in the year they become Canadian residents.

### Specified Foreign Property

1. Deposits or intangible property held outside of Canada, for example, foreign bank accounts or shares of Canadian companies held by a foreign broker
2. Tangible property located outside of Canada
3. Any interest in or a right to a nonresident entity, like shares of a foreign company but not including a foreign affiliate that is subject to different reporting. A foreign affiliate is a nonresident company in which the Canadian resident’s equity percentage is not less than 1 percent and the total of the equity percentages of the taxpayer and each related person is not less than 10 percent. Shares of foreign corporations held in a Canadian brokerage account constitute Specified Foreign Property.
4. Debts owed by nonresident persons, for example, bonds issued by foreign companies and loans to nonresidents
5. Interest in partnerships unless 90 percent or more of their income or loss would be attributable to nonresidents
6. Interest in nonresident trusts
7. Interest or units in offshore mutual funds
8. Any property that is convertible to or exchangeable for Specified Foreign Property

## Property not included in Specified Foreign Property

1. Property that is used exclusively on an active business of the reporting person, for example, inventory and equipment or a building used in a business
2. Property that is used for the personal use and enjoyment of the reporting person or a related person. The property must be primarily for personal use, defined as 50 percent or more of the use. If the Canadian resident owns a vacation property in Mexico that is used 1 month of the year for personal use but then rented for the remainder of the year, he or she would have to report this property because it is not used primarily for personal use and it is considered a Specified Foreign Property.
3. Property held in a registered account such as an RRSP or TFSA

## Penalties

1. Failure to file or comply with the rules on Foreign Properties results in severe penalties. There is a general penalty for failure to file the form T1135 of \$25 per day for up to 100 days—a maximum of \$2500.
2. For failure to furnish foreign-based information, when done knowingly or in circumstances amounting to gross negligence, the penalty is \$500 per month for up to 24 months—a maximum of \$12,000.
3. When there is a demand to file by CRA and the information is not provided, the penalty doubles to \$1000 per month—a maximum of \$24,000.
4. After 24 months, there is an additional penalty that raises the penalty to 5 percent of the unreported amounts, if greater than the \$24,000 penalty mentioned above.
5. For false statements or omissions on a filed T1135 form made knowingly or in circumstances amounting to gross negligence, the penalty is the greater of \$24,000 and 5 percent of all the amounts

that should have been reported on the return.

6. If a Canadian resident realizes he or she has not filed the foreign verification form T1135 according to CRA's rules, the individual can avoid the penalties by filing under the Voluntary Disclosure Program, making sure all the forms for the years that were required to be filed are completed and filed with the Voluntary Disclosure Application.

Amendments to the *Federal Income Tax Act* were proposed in 2013 to extend the re-assessment period by 3 years if a taxpayer fails to report income from a Specified Foreign Property and form T1135 was not filed on time or a Specified Foreign Property was not identified or was improperly identified on the form.

**I have heard many clients asking the \$10 million question: "How would CRA find out if I have a property in La La Land?"**

## \$100,000 Cost-Amount Threshold

Cost amount is defined as the adjusted cost basis, which usually includes the purchase cost of the property.

For real estate properties, any renovations or additions must be added to the total cost. It is important to track the cost of the foreign property to see if at any time in the year the \$100,000 is exceeded, triggering the reporting requirements. The cost is in Canadian dollars so every time a foreign property is acquired, the Canadian equivalent cost should be calculated using the exchange rate from the Bank of Canada service.

## Form T1135 for 2014

Starting with 2014, the form T1135 will require more details than in previous years.

For each Specified Foreign Property, the property must disclose

- the country where it is located,
- the maximum cost amount during the year,

- the cost amount at year-end,
- the income or loss generated during the year, and
- whether there were any gains or losses from disposition.

For foreign properties held in an account with a Canadian registered securities dealer or a Canadian trust company, the form allows the reporting of the aggregate amounts held in the account but on a country-by-country basis.

Also, the information to be provided is the maximum market value during the year and the fair market value at year-end, and the income or loss and any gain or losses on disposition.

Most of the Canadian brokerage firms have revised their year-end statements to their clients to provide this information, which makes it very useful when completing form T1135.

The CRA website has information on this topic. For help in determining the filing requirements and the information needed to complete the form, please visit [http://www.cra-arc.gc.ca/tx/nrrsdnts/cmmn/frgn/1135\\_fq-eng.html](http://www.cra-arc.gc.ca/tx/nrrsdnts/cmmn/frgn/1135_fq-eng.html).

During my years in public practice, I have heard many clients asking the \$10 million question: "How would CRA find out if I have a property in La La Land? The income earned from the property will never come to Canada and I will spend it all when I go on vacation." Unfortunately, there is no answer to that question, but all it takes is a disgruntled employee or an ex-spouse to make a call to CRA to spill the beans.

Heavy penalties are in place to discourage a nonreporting attitude. ▲

*Please consult a financial professional to discuss your specific situation.*

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