Wealth Management

INVESTMENT, TAX AND LIFESTYLE PERSPECTIVES FROM RBC FAMILY OFFICE SERVICES

Foreign Income Verification Statement – Form T1135

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

If you own "specified foreign property" with a total cost in excess of C$100,000 at any time during the taxation year, you are required to report certain information relating to this property on Form T1135 – Foreign Income Verification Statement. Filing Form T1135 does not impose any additional taxes; it only requires the disclosure of information about the ownership of foreign property. However, you may face significant consequences if you do not file or you make errors on the form.

This article provides an overview of the Form T1135 reporting rules, such as who has to file the form, the types of property and information that you must report, and penalties for failing to complete and file the form.

Consequences of failing to file accurately and on time

Different types of penalties can apply when you do not comply with the specified foreign property reporting rules. For example, if you fail to file Form T1135 by the due date, you may face a financial penalty. The penalty is $25 per day, subject to a minimum amount of $100 and a maximum of $2,500. Further penalties may apply if the failure to file or if errors or omissions were made knowingly or resulted from gross negligence. These penalties can be significant.

In addition, failure to comply with the requirements of Form T1135 or to report income from a specified foreign property on your income tax return may result in other tax consequences. Normally, the Canada Revenue Agency (CRA) has three years from the date of original assessment of a year to reassess your tax return. A three-year extension to this normal reassessment period may apply to your entire tax return. This means your tax return will not be statute-barred until six years after the date of the original notice of assessment or reassessment. This allows the CRA to review your entire return for the particular year, meaning their review is not restricted to just the information related to your foreign property.

Voluntary disclosure program (VDP)

If you have not met your Form T1135 filing obligations, you may want to consider the VDP. The VDP allows you to make an application to correct inaccurate or incomplete information, or to disclose information not previously reported on your tax return or the tax-related filings. Your disclosure must be voluntary, complete, include information that is one year past due and include payment of the estimated tax owing if any. If you satisfy all of the VDP conditions, the CRA may waive some or all penalties with respect to the disclosure.

Due date for filing Form T1135

Form T1135 is due on or before the due date of your income tax return. For individuals, the filing deadline is generally April 30 of the following year (June 15 for self-employed individuals). When a due date falls on a Saturday, a Sunday, or a public holiday, the due date is extended to the next business day.

Who has to report?

Canadian resident taxpayers who own specified foreign property with a total cost amount of more than C$100,000 *at any time in the year* are required to file Form T1135. The reporting requirement applies to Canadian resident individuals, corporations and certain partnerships and trusts. Individuals are not required to file Form T1135 for the year in which they become a resident of Canada. For a new resident, the cost amount of foreign property is its fair market value at the time you first became resident in Canada. You use this fair market value in determining your Form T1135 filing requirement in future years.

The threshold of C$100,000 applies to the cost of all specified foreign property you own *at any time in the year*. This means you need to keep track of the total cost of all specified foreign property you own on a daily basis, not just at year-end or each month-end. The following example demonstrates this concept.

You own shares of a U.S. public corporation in a non-registered Canadian investment account with a cost of C$75,000. You held this investment for the entire year. For three months during the year, you also had a bank account in the U.K. with C$35,000 on deposit. However, during the year, you used the cash deposited in the U.K. bank account to travel. At the end of the year, the only foreign property held was the U.S. public company shares. As the total specified foreign property exceeded C$100,000 ($75,000 + $35,000 = $110,000) at one point during the year, you would be required to file Form T1135 for the tax year even though you only held C$75,000 of specified foreign property at the end of the year.

The threshold of C$100,000 applies to the cost of all specified foreign property you own at any time in the year. This means you need to keep track of the total cost of all specified foreign property you own on a daily basis, not just at year-end or each month-end.

What property do you have to report?

Specified foreign property generally includes (but is not limited to):

- Funds deposited or held outside of Canada, even Canadian dollar funds deposited outside of Canada;
- Intangible and tangible property situated outside of Canada (e.g. land and buildings outside of Canada);
- Shares of foreign corporations, even if held in an investment account in Canada;
- An interest in a non-resident trust that was acquired for consideration (e.g. foreign mutual funds and exchange traded funds listed on a U.S. exchange);
- Shares of a Canadian corporation if held outside of Canada (e.g. if you hold RBC shares in an investment account in the U.S.);
- An interest in a partnership that holds a specified foreign property, unless the partnership is required to file Form T1135;
- An interest in, or right with respect to, an entity that's a non-resident (this could include an option to purchase shares of a foreign corporation);
- Property that's convertible into, exchangeable for, or confers a right to acquire a property that's specified foreign property;
- Debt owed by a non-resident, including government and corporate bonds, debentures, mortgages, and notes receivable;
- An interest in a foreign insurance policy; and
- Precious metals, gold certificates, and futures contracts held outside of Canada.

The following are common types of property not considered specified foreign property:

- Foreign property held in registered accounts such as RPPs, RRSPs, RRIFs, RESPs, RDSPs, locked-in retirement plans and TFSAs;

- Units of Canadian mutual fund trusts or mutual fund corporations that invest in foreign securities (e.g. RBC U.S. Equity Fund) or are held in a foreign currency;
- Personal-use property (e.g. vacation homes, vehicles, jewellery, artwork, etc.); and
- Property used or held exclusively in carrying on an active business (e.g. foreign real estate where you operate your active business).

What information do you need to report?

The information you need to report and the reporting method you use depends on the total cost amount of the specified foreign property you hold during the year.

Simplified reporting method

The simplified reporting method is available to you, if you own specified foreign property with a total cost of more than C$100,000 at any time in the year but less than C$250,000 throughout the year. The amount of information required under the simplified reporting method is significantly less than the detailed reporting method. The simplified reporting method requires you to:

- Check a box for each category of specified foreign property you held (the seven categories are listed later in this article);
- Report the top-three country codes based on the maximum cost amount of specified foreign property held during the year. In general, where the specified foreign property is located or where the issuers of the property are located determines the country codes. The month-end cost amount of all specified foreign property should be aggregated on a country-by-country basis. From those amounts, you can then choose the top-three countries based on the highest month-end cost amount.
- Report the income from all specified foreign property; and
- Report the gains (losses) from the disposition from all specified foreign property.

Detailed reporting method

If you own specified foreign property with a total cost of C$250,000 or more at any time in the year, you will need to report using the detailed reporting method. For detailed reporting, the Form T1135 is divided into seven categories that correspond to the different types of specified foreign property:

1. Funds held outside of Canada
2. Shares of non-resident corporations (other than foreign affiliates)

The information you need to report and the reporting method you use depends on the total cost amount of the specified foreign property you hold during the year.

3. Indebtedness owed by non-resident
4. Interests in non-resident trusts
5. Real property outside of Canada (other than personal use and real estate used in an active business)
6. Other property outside of Canada
7. Property held in an account with a Canadian registered securities dealer or a Canadian trust company

The following information is required for each specified foreign property in categories 1 to 6:

- The name of the foreign entity holding the property, name of corporation issuing shares, description of debt/property or name of foreign trust;
- The country code for each property — this is the country of residence of the issuer or trust or the country where the property is located;
- The maximum cost amount of the property during the year;
- The cost amount at year-end; and
- The amount of any income/loss that the particular foreign property generated in the year, as well as any capital gain/loss realized during the year for each foreign property.

The cost amount is generally the acquisition cost of the property. You can use the month-end highest cost amount of a particular specified foreign property to determine the maximum cost amount during the year.

As an example, let's assume you purchased 1,000 XYZ shares for a cost of C$100 in March, then you purchased an additional 100 XYZ shares for C$10 in July. You purchased an additional 200 XYZ shares in November for C$20 but before the end of November, you sold all of your XYZ shares. The highest cost amount would be based on July's month-end cost of C$110. Although the highest cost amount that you held was in November when you held 1,300 XYZ shares with a cost amount of C$130, you can report July's month-end cost amount as the maximum cost. This is possible because you are allowed to base the maximum cost amount during the year on the month-end maximum. In this example, the cost amount at year-end would be C$0.

Aggregate reporting – Property held in an account with a Canadian registered securities dealer or Canadian trust company (category 7)

If you hold specified foreign property with a Canadian registered securities dealer or Canadian trust company (as defined in the Income Tax Act), you may report it on Form T1135 in category 7. The advantage of aggregate reporting in category 7 is that you don't have to provide detailed information on every single specified foreign property held at these institutions. Instead, you may report the aggregate amount of specified foreign property you hold with a particular institution, as long as it's broken down and reported on a country-by-country basis. Alternatively, you may choose to report the aggregate totals for each account at a particular institution on a country-by-country basis.

For all specified foreign property held with a particular Canadian registered securities dealer or Canadian trust company, you will need to provide the following information on a country-by-country basis if you choose this method of reporting:

- The name of the registered security dealer/trust company;
- The country code for each country reported;
- The maximum fair market value during the year for each country reported — this may be based on the maximum month-end fair market value for each country;
- The fair market value at year-end for each country reported;
- The total income (loss) earned on the property during the year for each country; and
- The total gain (loss) realized on the disposition of the property during the year for each country reported.

It's important to note that if you choose to report under category 7, you will need to determine the country code for each foreign security held during the year, regardless of whether you hold that security at the end of any month or at the end of the year. This determines all of the countries that have to be reported in category 7 on Form T1135. You can find a description of how to determine country codes in the instructions on Form T1135.

Foreign currency conversion

All amounts reported on Form T1135 need to be in Canadian dollars (there are rare exceptions). Generally, when converting amounts from a foreign currency into Canadian dollars, you should use the exchange rate in effect at the time of the transaction (i.e. the time the income was received or when the property was purchased or sold). However, if you receive income throughout the year, it is also acceptable to use the average exchange rate for the year.

> The foreign reporting rules may require you to provide a significant amount of detailed information to the CRA, especially if you hold specified foreign property with a total cost amount of C$250,000 or more at any time in the year.

For category 7 on the T1135, you should use the average exchange rate for the year to determine the maximum fair market value during the year. However, the CRA has said that it's also acceptable to use the exchange rate in effect at the time of a transaction for this purpose. You should use the exchange rate at the end of the year to determine the fair market value at year-end.

Next steps

The foreign reporting rules may require you to provide a significant amount of detailed information to the CRA, especially if you hold specified foreign property with a total cost amount of C$250,000 or more at any time in the year. In addition, not filing on time or making errors on Form T1135 could result in penalties and an extended reassessment period. For these reasons, consider gathering the information required to complete the form as early as possible to ensure you can file accurately and on time. For further information regarding filing Form T1135, contact a qualified tax advisor.