

Stranded Canadians Taxed in the Time of Covid-19

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As Covid-19 continues to spread, many countries, including the United States and Canada, are increasingly closing their borders in an attempt to slow the rate of infection. This precaution may, however, have unintended tax consequences for Canadians who find themselves stranded on the U.S. side of the border for the duration of the shutdown.

Under the substantial presence test, Canadians who are present in the United States for at least 31 days during the current year, and 183 days in the aggregate during the current calendar year and the two preceding calendar years, will be considered U.S. residents for U.S. federal income tax purposes. Specifically, this three-year test is calculated by adding: (i) all days present in the United States during the current year; *plus* (ii) one-third of any days present in the United States during the previous year; *plus* (iii) one-sixth of any days present in the United States for the year before that. If that sum equals or exceeds 183 days, then such Canadian citizen may be subject to U.S. federal income tax on their worldwide income. Accordingly, it is important for Canadians that are currently stranded in the United States to take proactive steps to avoid this potentially adverse result. To do so, there are a number of measures an individual can take depending on their circumstances.

If a Canadian citizen is in the United States based on a certain type of visa (e.g., teachers, trainees, or students) or overstays due to a medical condition that prevents them from leaving, then such individual may be able to exclude days from the substantial presence calculation by filing an IRS Form 8843. This form allows the individual to claim an exemption and maintain their status as a nonresident of the United States for U.S. federal income tax purposes. Alternatively, Canadian citizens that are not in the United States under a qualifying visa or prevented from leaving due to a medical condition may file an IRS Form 8840 to claim a “Closer Connection Exemption.” Under this exemption, Canadian citizens that meet or surpass the 183-day threshold can still be treated as nonresidents of the United States by substantiating that they have closer connections to Canada based on residential ties including, without limitation, family, location of principal home, social ties, economic ties, etc. However, the Closer Connection Exemption is only

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available if the Canadian citizen was present in the United States for fewer than 183 days during the *current* taxable year.

If neither of the above exemptions apply, a stranded Canadian citizen can still avoid U.S. taxation by claiming an exemption under the United States-Canada Tax Treaty. To do so, the individual should file an IRS Form 1040NR, i.e., a U.S. Nonresident Alien Income Tax Return, and attach a completed IRS Form 8833, which specifies the treaty provisions under which the taxpayer is claiming an exemption. If pursuing this course of action, Canadian filers should be sure to include reference to Covid-19-related travel bans as justification for meeting the substantial presence test. To further bolster their position, a stranded Canadian citizen should also maintain documentation that evidences their attempts, as well as inability, to return to Canada, which could help further corroborate their position as a non-U.S. resident.

While little can be done about the current shutdown, stranded Canadian citizens can consider prudent measures to take in the meantime so as to avoid any unnecessary U.S. tax liability. Dorsey & Whitney regularly represents taxpayers in navigating the above process. If you have any questions or would like to learn more, please contact us.