

Canadian Deductibility of 401(K) Contributions and **U.S.** **Deductibility of RRSP** **Contributions**



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CROSS-BORDER WEALTH MANAGEMENT



Are Your 401(K) Contributions Deductible in Canada?

You might recognize this situation. You are a Canadian resident working in the USA on a TN visa. Your employer offers a 401(K) plan that includes a matching contribution. You know contributing to the 401(K) plan lowers your taxable income in the U.S. Does the same hold true for your taxable income in Canada? Are the matching contributions made by the employer taxable in Canada?

Provided certain conditions are met, you may deduct, for Canadian tax purposes, the contributions you make to a 401(k) plan in the U.S. As well, although the employer contributions are taxable in Canada and need to be reported as additional employment income, due to the tax treaty between Canada and the U.S., this additional income may also be deducted.

For example, let's assume you are a resident of Canada who is employed in the USA and you contribute to your employer-sponsored 401(K). Under the U.S.-Canada tax treaty, your contribution to the plan (up to your remaining RRSP deduction room) may be deductible for Canadian tax purposes. But you need to be careful because your 401(K) deduction on your Canadian return is limited to your RRSP contribution room. So if you have maxed out your RRSP contributions for the year and also made 401K contributions, you would not be



able to deduct the 401K contributions because the RRSP contributions have eliminated the available room. As such, if you participate in a 401K plan, then you need to reduce your RRSP contributions accordingly if you plan on claiming a deduction for your contributions. Although the 401K deduction eliminates your RRSP room, participating in the 401K plan would still be worthwhile due to the matching contributions from the employer. Note that the deduction to eliminate the employer matching contributions that have been included in employment income is not subject to RRSP room limitations.

It is also important to confirm that you meet the conditions outlined by the U.S. – Canada tax treaty and that the proper form is filed with your Canadian tax return. In this particular example, we are dealing with a Canadian who is commuting to the U.S. so the conditions outlined on Form RC268 would need to be met and RC268 would need to be completed and filed with your Canadian tax return. Don't be surprised if CRA requests additional support and documentation at a later date.

In addition, keep in mind that IRA contributions are NOT treated the same way as 401(K) contributions and are not deductible in Canada.

Are Your RRSP Contributions Deductible in the U.S.?

In the above scenario, we discussed deducting 401(K) contributions for purposes of Canadian taxation. Now we turn our attention to whether or not contributions to an RRSP are deductible for purposes of US taxation.

John is a dual U.S.-Canadian citizen who has been living and working in Canada for over 5 years. As a result, John files a Canadian tax return because he is a tax resident of Canada and he also files a 1040 return because he is a U.S. citizen residing abroad.

If John makes a deductible contribution to a RRSP on his Canadian tax return, then will this contribution also be deductible on his U.S. tax return? Generally, a RRSP contribution is not deductible on a U.S. tax return.



There is, however, an exception under the Canada-U.S. tax treaty that allows a RRSP deduction in certain situations. In particular, if the RRSP contribution is made via employee contributions to an employer sponsored group RRSP plan, then the contribution is deductible on the U.S. tax return.

But there is a limit on how much you can contribute. Specifically, the RRSP contribution is limited to the lower of your RRSP deduction limit in Canada or your 401(K) limit (currently at \$20,500 for those under the age of 50).

Form **8833**
(Rev. December 2021)
Department of the Treasury
Internal Revenue Service

**Treaty-Based Return Position Disclosure
Under Section 6114 or 7701(b)**
▶ Attach to your tax return.
▶ Go to www.irs.gov/Form8833 for the latest information.

OMB No. 1545-1354

Attach a separate Form 8833 for each treaty-based return position taken. Failure to disclose a treaty-based return position may result in a penalty of \$1,000 (\$10,000 in the case of a C corporation) (see section 6712).

Name	U.S. taxpayer identifying number	Reference ID number, if any (see instructions)
Address in country of residence	Address in the United States	

Check one or both of the following boxes as applicable.

- The taxpayer is disclosing a treaty-based return position as required by section 6114 ▶ ☐
- The taxpayer is a dual-resident taxpayer and is disclosing a treaty-based return position as required by Regulations section 301.7701(b)-7 ▶ ☐

Note: If the taxpayer is a dual-resident taxpayer and a long-term resident, by electing to be treated as a resident of a foreign country for purposes of claiming benefits under an applicable income tax treaty, the taxpayer will be deemed to have expatriated pursuant to section 877A. For more information, see the instructions.

In addition, you will need to notify the IRS that you are lowering your taxable wages by the RRSP contribution. You do this by filing a Form 8833 with your U.S. return and claiming an exemption under the tax treaty.

At Cardinal Point, we are here to assist residents on both sides of the border with their cross-border tax filing requirements and retirement planning scenarios.

Contact Cardinal Point for more information

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