Investment Partnership Accounting for Canadian Members in a U.S.-Based Investment Club

Prepared by myICLUB.com
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Introduction

Non-U.S. residents who participate in U.S.-based investment clubs and U.S.-based investment clubs with non-U.S. partners are generally subject to additional IRS tax filing requirements. Various tax treaties between the U.S. and other countries may be in effect to govern the specific requirements that the partnership and the partners may need to fulfill, so consulting a tax professional is advised.

Requirements to Support Canadian Members in a U.S. Investment Club

The following describes the general requirements of U.S. based investment clubs who wish to include Canadian residents as partners.

First, the partnership would be required to withhold and remit taxes each year for the foreign partners. All "Effectively Connected Taxable Income" to the U.S. could be subject to withholding, but income derived from security trading with a U.S. brokerage is not considered "Effectively Connected Taxable Income," so a different section of the tax code applies. From our research, income that is subject to withholding includes dividends and interest income. It appears that capital gain income is not included, unless real property in the U.S. generated the gain (but a BetterInvesting-style investment club should not have a real estate gain).

Canadian partners will need to do the following:

- Get a US Tax ID Number (TIN). Some may be eligible to get a Social Security Number, but if not, they can use IRS form W-7 to apply for a US TIN.
- File an IRS Form W-8 with the partnership. This lets the club formally know they are a foreign partner and provides that partner's US TIN.
- File a US tax return on IRS Form 1040NR each year (if they want a refund of tax withheld from their investment club account).

The club will need to do the following:

- Keep on file each IRS Form W-8 provided by the Canadian partners.
- Withhold taxes each year at the appropriate tax treaty amount for the Canadian partners. The IRS has a schedule of treaty withholding amounts by country. For Canada, the amount is 15%.
- File IRS Form 1042 each year to report and pay the tax amounts withheld.
- File form 1042-T along with a form 1042-S for each Canadian partner each year to report each partner’s share of taxable income and tax withheld.

- Provide a copy of form 1042-S to each Canadian partner to meet IRS regulations for informing each foreign partner of their share of tax withheld each year.

Investment Club Accounting & Tax Reporting for Canadian Partners & U.S. Partnerships

The **myICLUB.com** (www.myICLUB.com) club accounting tool provided by ICLUBcentral Inc. does not directly support foreign partners or tax withholding. As a workaround, after preparing the year-end Allocation of Income and Expenses for the investment club, the treasurer would need to perform a partial withdrawal for each Canadian partner in the amount of 15% of each partner's allocated interest and dividend income for the year. That withdrawn amount would then be remitted to the IRS along with IRS Forms 1042 and 1042-S, which would be completed manually.

The club could use the **myICLUB.com Federal Club Tax Printer** to prepare the required Form 1065 return. The instructions for filing the 1042 forms do not include a provision to file these forms as part of the partnership tax return so it appears possible to e-File the 1065 return and paper file all the additional forms 1042 separately. All 1042 forms are mailed to the IRS Center in Ogden, Utah.

For More Help and Information

The Internal Revenue Service has published a list of tips for partnerships with foreign partners: www.irs.gov/individuals/international-taxpayers/helpful-hints-for-partnerships-with-foreign-partners

IRS publication 515 may also be helpful: www.irs.gov/forms-pubs/about-publication-515

Please note that information may change over time, and the above is meant to provide general guidance only and may not replace consultation with a qualified tax professional.