Investment Issues

CHALLENGES WITH CROSS-BORDER PENSION PLANS

By Darren Coleman

Are you an HR advisor for an organization that straddles the Canada-U.S. border? Do your Canadian employees often take on assignments for a lengthy time in the U.S., or do American employees ever assume postings in Canada? If so, significant issues can arise for expatriate employees who have pension and retirement programs established by their employer. This is especially true when the employee returns to their home country.

Many cross-border workers are caught in a frustrating, confusing web of compliance and regulatory issues, sometimes with bizarre complications. This happens because the regulators want to catch money launderers, terrorist financiers and tax cheats, but they create havoc in the personal financial planning of innocent business people.

HR professionals are well positioned to help their expatriate staff navigate the dilemma that occurs when someone wants to come back across the border. Indeed, many situations can result for employees with retirement plans provided by their companies, such as Defined Contribution or Defined Benefit Pensions or group RSPs in Canada, or 401(k) and IRAs in the U.S. Often, the issues will not be identified by a tax or legal advisor because these people may not be well versed in such scenarios.

For one example, a group of executives were returning home to Canada after successful careers in the U.S. They established residency back in Canada, but discovered that their IRA provider would no longer maintain their accounts.

The issue is not that the IRA or 401(k) becomes immediately taxable. Once the plan participants return to Canada, they may continue to enjoy tax-deferral benefits of their IRA, 401(k) plan and Roth IRA balances just as if they were still U.S. residents. This explains why it often goes unnoticed by many tax and HR professionals who advise employees about moving across the border.

In another example, a certified professional accountant told their client not to expect adverse tax consequences when returning to Canada. Imagine how shocked this person was to receive a notice from her U.S. brokerage firm that her IRA had to be transferred or moved or within 90 days. If not, it would be cashed out, and she faced a tax that she didn't expect of over a quarter-million dollars.

To the untrained eye, this may not initially look like a tax problem, but a regulatory-compliance issue that later becomes one. By then, however, it may be too late.

U.S. brokers will not maintain IRA accounts for individuals who move back to Canada because of recent changes from the Canadian Securities Administrators regarding the registration requirements for all broker-dealer and advisor firms doing business in Canada.

How big a problem is this? Many brokers figure it's not worth the trouble – in cost and complexity – to retain the client's accounts after reviewing exemption requirements for

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individual investors and registration requirements for dealers. So, they let this business go and ask for the accounts to be transferred to another firm.

The taxpayer left in the lurch must then search for an institution that will take on a new account for a Canadian resident, and this can be an ordeal. Usually, Canadian investment firms cannot open IRAs because these are U.S. plans. It is possible for IRA proceeds to be moved to an RRSP, but that's the exception rather than the rule.

There have also been situations involving Canadian expatriate executives who participate in their employer's 401(k) plans. While the 401(k) can be moved to an IRA, the employee and their HR department may be surprised to learn that the 401(k) provider will not roll over the plan to an IRA when the participant retires, as is commonplace for U.S. employees.

Likewise, Americans working in Canada face similar challenges when they return home. While Canadian investment firms have the ability to manage RRSP and RRIF plans for U.S. residents in most states, not all firms will. Why? This ability was primarily intended for Canadian snowbirds, not permanent U.S. residents. Unless they are licensed, registered and able to do business in the United States, Canadian financial advisors are not permitted to advise and solicit trades from U.S. residents in their non-registered accounts.

If that isn't enough, another problem can arise, too. Some investments are not portable across the border. For example, people who invest in mutual funds cannot hold them outside their original jurisdiction; U.S. mutual funds cannot be held by Canadian investors, and vice versa. In many cases, when an investor moves back to Canada they are forced to liquidate, and must face a tax bill on any unrealized capital gains. Other investments, such as shares traded on the NYSE or NASDAQ, do not have this issue. So, the choice of investment type becomes critical for the ex-pat investor if they wish to minimize their tax bill and avoid complications.

It is estimated today that over one million Americans live and work in Canada, and an even larger number of Canadians live and work in the U.S. Thus, these financial issues affect a lot of people.

The solution? Have the human resources professional and expatriate staff member consult with a financial advisor who is familiar with cross-border investment issues, and licensed to do business in *both* countries. ■

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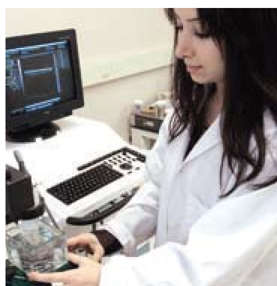

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