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July 2016

Canadian farmers selling products in the U.S.

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With an increasingly global farm commodity market and a lower Canadian dollar, Canadian farmers are finding it much easier to sell their products in the United States. However, it is important that producers are aware of potential U.S. tax issues and filing requirements, particularly if this is common practice on their farm operation.

When/what to file

If you are selling your farm products in the U.S., consider these strategies to avoid penalties imposed by the Internal Revenue Service (IRS):

1. If you have a permanent establishment in the U.S., you must file a U.S. federal income tax return. You are considered to have a permanent establishment when a physical location is present (either owned or rented), or potentially if there are regular sales occurring in the U.S. For example, if you rent a U.S. warehouse facility and ship product from your operation in Canada to that location, in order to store that product and sell it at a later date in the U.S., that facility would qualify as a permanent establishment and there would be filing requirements.

   Since few farmers in Canada will be considered to have a permanent establishment in the U.S., most farmers need only file a protective filing or treaty-based return in the U.S. These returns are information filings with the IRS that claim U.S. federal income tax relief due to the Canada-U.S. Income Tax Treaty rules. Canadian farmers pay income tax in Canada on the sale of these products and are not subject to withholding tax in the U.S. These information returns inform the IRS of any sales that are considered to be sourced in the U.S., regardless of whether income tax is owed on the sales.

2. There are several ways Canadian farmers can reduce the likelihood of having to file a U.S. return. These strategies help to suggest that the sale of product was initiated in Canada and was not a U.S.-sourced sale, as the title of the product, the risk of loss, or the economic transfer occurred in Canada:

   a. Include shipping terms on invoices that clearly identify that the U.S. customer is solely responsible for the product after it leaves the farm in Canada.

   b. Ensure the invoice indicates that the point of sale is in Canada.

   c. Use an independent trucking company to ship the product across the border (either Canadian or American).

   d. Consider the use of a sales agent who can arrange for the transaction to occur in Canada. The agent should do this work full time and have multiple customers to ensure that they are actually "independent."

Forms required

Canadian farmers should consider completing several different forms to address any potential U.S. filing requirements that may exist based on their individual circumstances:

- **W-8BEN** – If you are a member of a U.S.-based co-op and are receiving payments that are subject to withholding tax (e.g. patronage dividends), consider filling out a W-8BEN form to reduce the withholding tax.
- **SS-4** – This form secures a business number in the U.S. for the farmer. The business number will help when filing a treaty return and/or a protective filing that claims revenue in the U.S., but where the farmer has no permanent establishment in the U.S.

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- **1120F/1040NR & 8833** – The 1120F is the actual tax return that a farmer must file for a corporation. The 1040NR is for an individual farmer. The 8833 is the treaty exemption form mentioned above, which must be filed with either the 1120F or the 1040NR.

Canadian farmers should also consider that each individual U.S. state has its own filing requirements, and they may need to file a state return in addition to a federal return. Generally, however, if the only activity is the sale of product into the state via an independent carrier, there is no Nexus filing requirement. The Nexus filing, if applicable, does not necessarily follow the Canada-U.S. Income Tax Treaty rules.

As each farmer will have unique circumstances surrounding their operation, it is important to get professional guidance before making a final decision on whether you have filing requirements in the U.S. Most importantly, do not just ignore any filing requirements that may exist in your specific situation. Penalties can be significant if you are found not to be in compliance, including the IRS denying expenses related to sales in the U.S., thus increasing income tax owing. Contact your Collins Barrow advisor for help and more information.

Some information for this article was obtained from "Important Advice for Selling Your Grain in the U.S." in the July/August issue of AgriSuccess, an FCC publication (http://www.slideshare.net/farmcreditcanada/fcc-agrisuccess-julyaug-2016).

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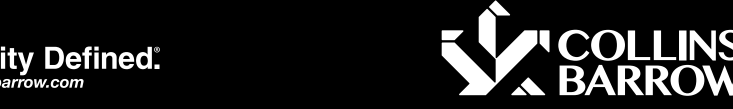

Collins Barrow regularly publishes *Farm Alert* for its clients and associates. It is designed to highlight and summarize the continually changing farming and agricultural scene across Canada. We always recommend that you seek professional advice before taking specific planning steps.