

Buying [past tense] US mutual funds and stocks from Canada

Note: Now that the regulators have cracked down to "protect" Canadians from buying lower cost US mutual funds and paying lower US brokerage fees on stocks, it's no longer possible for all but the most determined Canadian investors to do so. This page remains as a testament to the effectiveness of our regulators in "serving" the Canadian public.

With all the low-MER Canadian-based index funds, Canadian-based ETFs and US-based ETFs that are now available through Canadian brokers, there's also less *need* to own Vanguard funds than there used to be. Indeed even Vanguard now offers ETFs called VIPERS. However, most of the information on taxation of US securities still remains valid and now also applies to US-based ETFs.

This page is divided into three sections:

1. A history of the latest regulatory crackdown on US brokers.
2. A set of Frequently-Asked Questions on buying mutual funds and stocks in the US. [Some of the information, e.g. on US discount brokerage accounts, is now obsolete.]
3. A set of related links.

Canada's regulators "protect" us from the "evil" US securities industry

So you really thought NAFTA was going to encourage cross-border trade, increase competition and benefit Canadians?

06Oct01 [The Myth About Cross-Border Trades](#) U.S. laws **do** protect Canadians with accounts south of the border.

20Jun01 Provincial securities regulators "protect" Canadian investors from US discount brokers who offer dramatically lower stock trading fees and provide access to lower cost US mutual funds. TD Waterhouse US, Ameritrade and Datek are each fined \$800,000 for failing to register in Canada. Canadian investors will lose many times that much in higher fees.

Related news stories:

[The regulators save the day](#) [20Jun01]

26Feb01 Canadians who managed to keep their TD Waterhouse US brokerage accounts receive letters from TD advising that Waterhouse Investors Prime credit cards are being terminated for "non-US residents." Instead of a free card that pays a 1% rebate on all purchases TD wants Canadians to switch to TD Canada's \$US Advantage card. The only *Advantage* in this card is to TD because clients now get to pay US\$25 per year in fees with no rebate. As a sop they will give clients the current 1% rebate on purchases up to 31March. The final rebate will appear on, now get this, "your April 2001 TD Waterhouse brokerage statement." In effect TD acknowledges that there still are Canadians who have US brokerage accounts. How can this be? Didn't they repatriate everyone in December?

08Feb01 Some US brokers are still doing business with Canadians. For more information check out the thread "U.S. brokers currently accepting Canucks" at [The Boomer](#) website's **Wealth [discussion forum](#)**

02Jan01 If you have a US IRA but now live in Canada, it may now be possible to trade on that account without using a US address under new [National Instrument 35-101](#). For more information check out the thread "[Canadians can now trade on their IRA's using Cdn addresses](#)" at [The Boomer](#) website's [Wealth discussion forum](#)

13Dec00 As of today TD Waterhouse US is carrying out its eviction of Canadian accounts.

Related news stories:

[Bid to resolve U.S. broker dilemma](#) [01Dec00]

[OSC expects 'happy' resolution of trading dispute](#) [04Nov00]

[Stay-at-home rule enrages investors](#) [03Nov00]

[Canadians told to trade at home](#) [02Nov00]

31Oct00 Received in the mail from Michael Curcio, Executive Vice President, TD Waterhouse US:

We have been advised by the Canadian securities regulatory authorities that we, as well as other US registered broker-dealers, must refrain from providing any investment services to residents of Canada. Accordingly ... we will no longer be able to meet your investing needs through TD Waterhouse in the US.

The letter goes on to say that we've got 30 days to transfer our accounts out (in kind) to a Canadian broker or else they'll automatically transfer our accounts to TD Waterhouse Canada.

Send your complaints to their "special hotline" in the US at 1-800-530-1333, in Canada at 1-866-839-9907, your MPP and your provincial [dictionary definition: *limited in perspective; narrow and self-centered*] securities regulator.

For more information about this go to [The Boomer](#) website's [Wealth discussion forum](#) and look for related threads.

13Oct00 Several people have recently indicated that TD Waterhouse US rejected their new account applications because they used a Canadian address. In addition, all of the following have reportedly also declined to open accounts with Canadians:

- Accutrade
- AmeriTrade
- Brown & Co.
- Datek
- DLJ Direct
- Dreyfus
- NDB
- Salomon Smith Barney
- Vanguard

The following still appear to accept Canadian accounts since their new account application forms provide for Canadian addresses and for "Non-Resident Alien" status, however, they do not offer Vanguard mutual funds. [**N.B.** Bylo has no experience with these brokers.]

- [MyDiscountBroker](#)
- [SureTrade](#) [01Feb01]
- [Interactive Brokers](#) [20Oct00]

In the meantime BGI and SSgA (and soon even Vanguard) have introduced [ETFs](#) that track many popular indexes. While these securities can be purchased in Canada, the brokerage fees are still much higher than in the US. Moreover, a number of ultra-low cost (US\$2 to \$3) US brokers have emerged that cater to longterm, buy-and-hold investors including [Buy-and-Hold](#) and [Sharebuilder](#). It's not known yet if they accept accounts with Canadians.

Why buy mutual funds or stocks in the US?

Until recently Canadians who wanted low management expense ratio (MER) mutual funds, especially index funds, had no alternative but to look south to the United States. In the US, [Vanguard](#) has been the pioneer in low-cost index mutual funds. A testament to their success is that they're now not only the second-largest US mutual fund complex, but also they manage more assets than the entire Canadian mutual fund industry. The problem was/is that few US mutual fund companies, and in particular Vanguard, would sell to Canadians. Some of us have "circumvented" this barrier by opening brokerage accounts with US discount brokers and then buying mutual funds over the Internet from them.

At the same time many US discount brokers now offer not only trading over the Internet but also welcome accounts from Canadians. The best-known of these is [TD Waterhouse US](#) (Waterhouse). It's now the second-largest discount broker in the world. It also happens to be owned right here in Canada by the Toronto-Dominion Bank as part of its global [TD Waterhouse](#) (formerly TD Greenline Investors Services) discount brokerage operation.

The information presented here is oriented to the purchase of Vanguard funds through Waterhouse because that's what I do. It also lets me use their funds, fees, rules, etc. as "typical" examples in this presentation. While you shouldn't construe this as an endorsement of either Vanguard or Waterhouse, FWIW I happen to be a highly satisfied customer of both organisations.

Waterhouse offers many other mutual funds besides Vanguard and Vanguard offers many more mutual funds besides those that are available through Waterhouse. If you find some good non-Vanguard funds or a broker who offers a wider selection of Vanguard funds than Waterhouse, please [e-mail](#) me the information.

Recently some Canadian mutual fund companies, primarily some of the banks and Altamira, have introduced lower-cost index funds. Still, these funds generally have MERs at or above 0.50%. That's more than double what Vanguard charges. What's more, those MERs appear to be subsidised by the fund sponsors; they could go up at any time (on 60 days notice, of course.)

In addition, there are now many lower-cost Exchange-Traded Funds (ETFs) available to Canadians, including XIU, SPY, QQQ, iShares et al. For many people these securities may be a viable alternative to Vanguard, but others like myself still find many benefits to dealing with a US discount broker.

Q Are there more reasons to buy mutual funds or stocks in the US?

A In addition to the reasons given in the above introduction:


1. Vanguard's Total Stock Market index fund, which tracks the entire US stock market (Wilshire 5000 index), is probably the best single US mutual fund one can buy. John Bogle certainly thinks so, and so do I (not to suggest that our opinions should carry equal weight! :-)) Most available-in-Canada index funds and index

participation units track the S&P 500, so they have no exposure to mid and small caps. [OTOH, CIBC now has a Wilshire 5000 index fund, but it's relatively new and the MER is generally 0.90% (compared to Vanguard's 0.20%.)]

2. While the MER for US ETFs like SPY and DIA is comparable to Vanguard, the MERs for iShare country funds (WEBs) are still rather high at 0.84%. Vanguard doesn't have country funds, but they do offer Europe, Asia/Pacific and Emerging Market funds for around 0.3% or 0.35%. [There are now Canadian EAFE index funds with MERs of 0.50% to 0.90%. Some are even fully RRSP-eligible. However this latter feature also makes these derivative-based index funds poor choices for non-registered accounts. It's also not clear (a) what additional costs related to the purchase of index futures are incurred by such funds and (b) which of these funds are currency hedged. But these are further digressions...]
3. For those who want the flexibility to create more diverse portfolios, Vanguard offers by far the widest selection of index funds. In addition US brokers give you access to a much broader selection of actively-managed mutual funds (from Vanguard as well as many other companies) than are available in Canada at MERs that are roughly half of what we're used to. You just can't create the kind of "slice and dice" portfolios advocated by the likes of Frank Armstrong, Bill Bernstein, Larry Swedroe et al using just Canadian-operated mutual funds.
4. You can trade ETFs and US stocks in the US for much lower brokerage fees than in Canada. Waterhouse charges US\$12 a transaction. Others are as low as US\$8 and dropping.
5. US brokers generally offer free DRIPs for ETFs as well as ordinary stocks -- even when the issuer of the security does not offer their own DRIP. These in-house DRIPs also feature a consolidated statement of all holdings, reinvestments, etc. And it's even possible (though rather awkward) to download some US broker statements from their website into software packages like Quicken.
6. US brokers offer \$US money market funds (MMF) with automatic fund sweeps. This means that every night they automatically transfer any cash in your account into a MMF. Similarly when you buy a security they automatically sell enough MMF on settlement day to pay for your purchase. Usually US brokers offer a variety of MMFs at competitive rates. Some of these MMFs even pay bonuses like American Airlines AAdvantage miles!

To summarise, no, this isn't for everyone, but I for one am happy I made the move south.

What can you buy?

 Generally you can buy a wide variety of mutual funds. The selection varies from broker to broker but generally your choice is restricted to only the most popular funds. Unfortunately newer Vanguard funds, and especially their tax-managed funds, aren't yet available.

Generally you can buy any stock that trades on the NYSE, AMEX, NASDAQ and OTC markets. Few if any US brokers offer stocks from the TSE, however, many Canadian large-cap and high-technology stocks also trade on the NYSE or NASDAQ.

What does it cost?

A Waterhouse charges US\$24 per buy/sell transaction for Vanguard mutual funds. Remember, since Vanguard doesn't pay any remuneration to brokers, this fee helps Waterhouse to pay for the costs of executing your transactions and sending you monthly statements, etc. Also, if you could deal directly with Vanguard, while you wouldn't have to pay transactions fees, if your account was smaller than US\$10,000 you would have to pay US\$10 per year.

For stock transactions Waterhouse charges US\$12 per trade. Compare that to US\$25 to US\$30 if you trade US stocks through a Canadian broker. Also with Waterhouse you get a free Dividend Reinvestment Plan (DRIP), there are no extra fees to make odd-lot (less than 100 shares) transactions, no charge to get a registered stock certificate, etc.

Q With which US broker should I do business?

A Check out the US broker ratings links below. Call or e-mail candidate brokers to confirm that they'll open an account with Canadians and to ask them to send you a new account application. Be prepared for some surprises. For example, E*Trade won't open accounts with people in Canada or Australia, apparently because they have local brokerage operations in those countries. However, Waterhouse doesn't seem to have the same restriction even though they also operate in both Canada and Australia. Go figure.

Q Is this legal?

A Yes and no. I'm not a lawyer, so all I can do is tell you what the regulators have told me.

Yes, according to the US Securities and Exchange Commission (SEC) in response to my inquiry:

"There is no restriction under United States law barring you from opening a brokerage account with a US broker."

No, according to the Ontario Securities Commission (OSC) in response to my inquiry:

"A party [dealer/broker] cannot trade in Ontario (which includes trading with someone outside of Ontario) unless he/she is registered as a dealer or an exemption applies."

Also this from the [OSC website](#):

Q: Can I open an Internet trading account with a dealer in another province, territory or country?

A: Not unless that dealer is properly registered to trade in your province or territory.

Q: Can I invest in securities via the Internet?



A: Yes, but only if you are investing through the Internet site of a securities dealer that is registered to trade securities in your area.

Also some investors living British Columbia have been denied US accounts by Waterhouse due to BCSC regulations.

US brokers generally aren't registered in Canada. And why should they be? US brokers should be registered and regulated in the US. If you're concerned about this issue, then consult a lawyer.

Q How is income from US securities taxed?

A When you open an account with a US broker you should include:

1. an IRS [W-8](#)  Certificate of Foreign Status to declare yourself a non-resident foreigner (you're considered to be a non-resident *alien* by US authorities)
2. an IRS [1001](#)  Ownership, Exemption or Reduced Rate Certificate to indicate that you do not have a U.S. Social Security number or Federal Taxpayer ID number and to ensure that taxes on mutual fund distributions and stock dividends are withheld at the reduced rate of 15% (rather than the usual 30%) under US-Canada tax treaties.

While the 15% tax is annoying, realise that it's a credit on your Canadian tax return. After each year-end you'll get an IRS 1042S information slip (equivalent of the Canadian T-5) that you can use to claim the credit on your Canadian tax return.

The bottom line is that you still have to pay regular Canadian taxes on this income, but at least you're not double-taxed by the IRS.

There's no tax withheld on capital gains that arise when you sell a US stock or mutual fund. It's your responsibility to track and report this to Revenue Canada.

Q Are there any other Canadian tax issues?

A Starting with your 1998 tax return you must include a [T1135](#) form if you own foreign assets whose cost value exceeds CA\$100,000. For more information: [Foreign Income Verification](#). If you own units in a non-resident mutual fund trust, you must file form [T1142](#) in respect of trust distributions, unless you have filed form T1135.

Q Are there any estate planning considerations?

A There may be. In general US estate tax becomes an issue only when your portfolio exceeds US\$1.2M or if you own real estate in the US. Read the items linked-to below, and to be safe, consult an accountant or tax lawyer who is familiar with both Canadian and US regulations.

Q Are there any other advantages?

A Yes. Waterhouse for example offers free US\$ credit cards. These can be particularly useful if you travel to the US. You can choose between VISA and Mastercard. Be sure to request a gold card. Not only are the cards free but you even get a rebate of 1% of the value of your purchases at the end of each year. The cards come with the familiar green TD logo. Since TD doesn't offer Mastercards in Canada, another bonus if you get one from Waterhouse are the bar bets you can win with Canadian TD employees :-)

Related Pages

[So you *really* want to open a U.S. broker account and trade on the Internet](#) [Mar99]

[Brain drain, meet investor drain](#) [NP 26Feb00]

[There's no need to block access to cut-rate U.S. brokers and funds](#) [NP 01Jun99]

[Bylo's "VanMail" Campaign](#)

🌀 FundLib Threads

[Buying US Mutual Funds from Canada - I](#) [15-Jul-97]

[Buying US Mutual Funds from Canada - II](#) [20-Jan-98]

[Buying US Mutual Funds from Canada - III](#) [26-Feb-98]

[We e-mailed Vanguard](#) [27-Feb-98]

[Move US Stocks to US Broker?](#) [19-Oct-98]

The Taxman Always Rings (at least) Twice

[Taxes grind down US holdings](#) [Taxation of US securities held in and out of RRSPs]

[ETF holders get tax surprises](#) [Taxation of Distributions From Foreign ETFs]

[Tim Cestnick: Uncle Sam's long arm can even reach Canadian investors](#)

[BDO: US Estate Tax Issues for Canadians](#)

[US Estate Tax Planning for Canadians](#)  [AIM Trimark]

[US Estate Tax: Strangi Upheld](#) ["*Strangi* may also support any attempt by the IRS to look through certain Canadian holdcos that are used to own US stock and securities and other US-situs non-personal-use property."]



No, this is **not** an advertisement. Vanguard has **not** paid for it. They probably don't even know that it's here.

So why **is** it here?

Simple. If someone should happen to follow this link and open an account with Vanguard, then it's just my modest contribution to help keep "our" fund expenses as low as possible. In a sense, it makes this site a "mutual mutual" funds website.

Disclaimers

1. **Caveat investor.** Information changes on an almost daily basis. The funds, fees, terms, conditions, tax

regulations, etc. may (or may not) have changed between the time I wrote this and the time you read it. **Always investigate or consult a qualified financial planner, accountant or tax lawyer *before* you invest.**

2. This material is oriented to Canadians who want to buy US securities through a US broker. It may (or may not) also apply to citizens or residents of other countries.

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