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inBrief

Canada edition

Planning for Non-Residency: Doing it Right

By James Bowden | 4 October 2021

Where you choose to be resident is obviously driven by more than just the tax consequences, but for many people tax is a major factor in that decision. Canada, like most other countries, taxes on the basis of residency. If you are a Canadian "resident" for tax purposes, you pay Canadian income tax on your worldwide income, and you have broad reporting obligations to the Canada Revenue Agency (**CRA**) on your foreign interests. There are many ways for a Canadian resident to optimize their tax position both in life and upon death, but none are quite as effective as becoming non-resident. When you are non-resident, you are not subject to Canadian income tax (with some exceptions regarding Canadian source income) and this article aims to provide a general overview of what you should consider when planning for non-residency.[1]

First, be sure you really do cease being resident for tax purposes. Canada's definition of "residency" relies on assessing your life as a whole and identifying the number and importance of so-called "connecting factors" that you have in Canada. This is a widely written about issue and will not be discussed in any detail here, other than to remind you to make sure you really do break ties with Canada sufficiently to ensure you are indeed a non-resident.[2] Next, and a point that seems to be strangely overlooked more often than one might think, is that you also need to clearly obtain and keep residency status somewhere else, otherwise the CRA will not agree that you have sufficiently severed your residential ties to Canada. Living a mobile lifestyle where you spend a few months here and a few months there without putting down roots anywhere, may not be enough to cut ties in the CRA's view.

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James is an experienced transactional and corporate and commercial practitioner, having trained in both Ontario and with Afridi & Angell in Dubai for many years. He has developed significant expertise in a number of specialisations, most notably commercial advisory and transactional work, onshore and offshore trusts structures, asset protection, and tax and estate planning. James spearheaded the firm's initiative to establish its Toronto office (Afridi & Angell Professional Corporation), which he now heads, taking advantage of the firm's many Canadian ties and bringing the Afridi & Angell service standard to Canadian clientele. James is a member of the Ontario bar and received his L.L.B., from Queens University, Canada, in 2004.

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[1] As a quick aside, note that Canadian citizenship is not the same as residency; a Canadian citizen can become non-resident forever and still retain citizenship.

[2] Consider obtaining a copy of the CRA's form NR73, which includes a list of questions about your ties to Canada. If you answer yes to 5 or more questions, you may need to break more ties or seek advice for more guidance. Refer to the NR73 for your own reference only, but I do not suggest filing one. Filing your "final tax return" is generally sufficient and the preferred approach.

You should also be aware that you will trigger a taxable event upon your exit from Canada. You are deemed to have disposed of many of your capital assets and realised any latent gain (or loss) on them, and you will be taxed on the gain, and this includes assets worldwide (and virtual assets like cryptocurrencies). There are important exclusions to the assets that are deemed disposed of, including Canadian real estate[3], RRSPs (Registered Retirement Savings Plan) and TFSAs (Tax-Free Savings Plan), and life insurance policies, among other things. Importantly, the CRA expects you to have obtained valuations of your assets at or around the date of your exit to support the values you report, and that there will be a cost to having such valuations carried out, so be sure to plan for this.

Once you have successfully become a non-resident of Canada, and become a resident of another country, are you safely outside of the reach of the CRA? In many important ways the answer is yes, but a non-resident remains taxable on certain income and property. Summarised here are some important points to bear in mind as a new or prospective non-resident.

- **RRSPs:** Nothing happens to your RRSP account(s) when you cease to be resident in Canada. In your year of exit, you can still contribute to the account to the full extent of your eligibility for that year (although it might be low if you leave early in the year). The funds in your RRSP are sheltered from Canadian tax while they remain in the RRSP, but this may not be the case in your new country of residence, which may view it simply as any other investment account and may tax it accordingly.[4] You can withdraw some or all of the funds in an RRSP that you had accumulated prior to your exit. As a non-resident, these withdrawals will be subject to the non-resident withholding tax of 25 per cent, but that is a much lower rate than the graduated rate you would otherwise have been subject to had you withdrawn the funds whilst being a Canadian resident (unless you withdrew the funds during a very low-income year). Once the funds are out, you are free to use or invest them and you will not be subject to Canadian tax on the proceeds of such investments going forward. Withdrawal is not always the best option though, as you may wish to simply keep the funds sheltered in the RRSP for a time in the distant future, or to keep as part of your estate and pass on to a spouse on a rollover basis, for example.
- **TFSAs:** Similar to RRSPs, nothing happens to these upon exit and such accounts remain sheltered from Canadian tax, including upon withdrawal (no non-resident withholding tax either). Additionally, like RRSPs, note that other countries may simply view these as regular investment accounts and tax them accordingly to their regular rules of taxation. The same advice therefore applies regarding crystallization of latent gains that may be unrealised, prior to exit.
- **Real estate:** If you continue to own real estate in Canada as a non-resident, you are probably leasing it out (if it is residential, you should absolutely be leasing it out on arm's length terms or your non-resident status will be in jeopardy). Rental income from a Canadian property is Canadian source of income and will be subject to non-resident withholding tax, and may also be subject to preferential treatment under a bilateral tax treaty, if applicable. Canadian source income, whether from real estate, business, investments or otherwise, will result in the requirement to continue to file returns with the CRA.
- **Investments:** Dividends you receive from Canadian sources are subject to non-resident withholding tax, which may be reduced by an applicable treaty. Interest (assuming it is from an arm's length party), is not subject to Canadian tax when paid to a non-resident (not the case if the

[3] Note that a "principal residence" undergoes a "change of use" rather than a deemed disposition, although the effect is similar in that there is a deemed realization of the latent gain, but the principal residence exemption can still apply to shelter the full amount (assuming the property is otherwise eligible for the principal residence exemption for all the years the property was owned).

[4] Consider crystallizing any latent gains within the RRSP account prior to exit, for this reason (i.e., to minimize capital gains that may be realized as a non-resident when they are no longer sheltered). Unless of course your new place of residence is a very low or no tax jurisdiction.

source is not an arm's length party). These income sources also give rise to Canadian filing requirements, even if no tax is actually payable.

- **Foreign trusts:** It may occur to you that setting up an offshore trust is attractive now that you are no longer a tax resident of Canada. It may well be that there are excellent opportunities available to you since you will be clear of many of Canada's aggressive reporting and attribution rules that apply to trusts, but, as with most dealings with trusts, professional advice is critical. Canada's deemed residency rules as they relate to foreign trusts can catch many people off guard. If you establish a trust within 5 years of your departure from Canada, for example, and there are Canadian beneficiaries, that trust will be deemed resident in (i.e., taxable in) Canada even though you established it after you were firmly and clearly non-resident. There are similar considerations that will apply to the years prior to your return to Canada too, so good planning from the outset will be critical to ensure you do not inadvertently lose out on some of the tax advantages of non-residency. Things to consider are the timing of the trusts' establishment, how to structure the initial settlement and future contributions, who will make those contributions, who the beneficiaries will be, whether that will change in the future, and when they will actually receive any funds from the trust and under what conditions (e.g., only if and when they cease to be Canadian resident?), among other things. These decisions will also affect what information the trustee is obligated to keep on file, and may be obligated to report, so bear that in mind if you have privacy concerns.
- **Wills and POAs:** Any wills, powers of attorney, and other estate planning you may have done prior to your exit should be re-assessed in light of your new residency situation, which likely came with a shift in at least some of your assets, and likely more of a shift the longer you remain non-resident. Multiple wills are common among the expatriate community; one (or more) for assets in Canada, and another for assets in your new country of residence, and perhaps more for certain assets elsewhere such as real estate or bank accounts you may own in yet a third country. A local will in each jurisdiction can dramatically ease the estate administration process; it avoids the need to seek resealing of foreign probate, or equivalent, in each jurisdiction, a cumbersome and often non-transparent process. Multiple will preparation requires careful drafting to ensure the documents work seamlessly together and do not conflict, and, of course, to ensure they meet the requirements of the jurisdiction in which each is intended to operate. Similarly, any POAs you may wish to have in place in the event of your incapacity will need to be prepared (or re-prepared) in your new place of residence to ensure they are effective there.

Determining how to break residential ties with Canada (and not accidentally re-establishing them), reporting to the CRA in an effective manner on exit, structuring your assets while non-resident in the context of a broader wealth and estate plan, and knowing your continuing Canadian tax or reporting obligations even as a non-resident, are all key areas to consider in order to ensure your non-residency is both compliant and tax efficient. The issues discussed in this article are only examples intended to provide a general overview of some of the common considerations, but there are often many other factors to consider depending on your specific circumstances, assets, plans, and risk tolerance.

If you are considering non-residency status in Canada and want to make sure you get the most out of your years abroad or are otherwise concerned about the tax implications of the move, please contact us and we will be delighted to provide the guidance you need. ■

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