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Tax-Driven Changes in Residency for Canadians

By James Bowden | 25 February 2022

For those with sufficient assets, tax-driven relocations and changes in residency have become commonplace. They began to occur in earnest in the 1990s and have increased in popularity ever since. In the past 1-2 years in particular, the popularity of residency changes for tax reasons has seen a marked rise. This has been driven by several factors, which include: the steady reduction in other viable international tax planning strategies as the OECD continues to press aggressive reform, more mobile lifestyles brought about by COVID-19, and the expectation of an increased tax burden especially for the wealthy (also brought about by COVID-19, at least in part). In short, more people have begun to enjoy more mobility, and the comparative tax advantages of relocating have never been greater. As we have stated in prior inBriefs, for Canadians, changing their country of tax residency is almost certainly going to be the single most effective tax planning strategy they can adopt, with both immediate and long-term benefits.

The opportunity to attract such mobile, wealthy people is also very appealing to potential recipient countries, who stand to gain economically from an influx of wealthy immigrants. Competition for economically beneficial immigrants is high. Many countries have established residency programs and tax incentives specifically intended to attract economic immigrants. Some of the most popular destinations in recent years have included the UAE, Portugal, Greece and Italy, among many others including some Caribbean nations. The models adopted by these countries typically require the applicant to make an investment in the country, often in real estate, in exchange for medium- or long-term residency (and sometimes a path to citizenship over time), and access to a favourable tax regime. The amount of the investment varies greatly from country to country (from EUR 200,000 to EUR 3,000,000).[1] The favourable tax regime will be one of two models: the requirement for an annual lump-sum payment of tax

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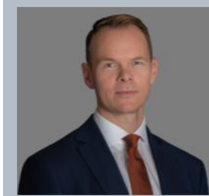

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James is an experienced transactional and corporate and commercial practitioner, having trained in both Ontario and with Afridi & Angell in Dubai for many years. He has developed significant expertise in a number of specialisations, most notably commercial 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.

[1] There are other paths to residency aside from investment in some countries, such as through employment or establishing a business. In the UAE, for example, you may establish a company for significantly less cost than the cost of investing in real estate, and arrange for the company to sponsor your UAE residency.

irrespective of actual income each year (*e.g.*, Italy, Switzerland), or, access to a low or no tax environment without the lump-sum in exchange for having made an initial investment (*e.g.*, Portugal, Greece, UAE).

Deciding where to seek your new residency can be complex and should take into account many factors, not only taxation. There are publicly available resources which help you to evaluate potential destination countries according, breaking down some of the more relevant factors on a country-by-country basis, and even offering rankings of countries by popularity for their tax residency offerings.[2]

The conditions of residency and favourable tax treatment usually do not require significant "days in country", so extensive travel is permitted, but you would need to avoid spending so many days in another country that you are deemed tax resident there as well. The residency status granted normally gives you and your family the ability to live, study, and work in the destination country (and, for EU destinations, these rights would apply anywhere in the Schengen region).

From a tax planning perspective, it is crucial to carefully evaluate your assets and your expected sources of income before settling on a destination for tax residency, and to obtain professional advice as to how your specific assets and income will be taxed there. There are always exceptions to the favourable tax treatment offered by each jurisdiction. For instance, some may provide that only passive income from foreign sources will enjoy low/no tax, and only if there is a double taxation treaty in place with the foreign source country (in which case, income from assets located in offshore jurisdictions may not qualify, nor income you generate if you are working in your new country of residence). Also, assets located in the country you are moving away from may continue to impose tax on income and gains on those assets, despite your non-residency.

As such, the change of residency journey will almost always include a restructuring of your assets, and planning your sources of income, in order to achieve the desired tax-efficient result. As part of the planning, it can often be helpful to make use of trusts in low/no tax jurisdictions as a vehicle in which to hold appreciating or income-producing investments. Distributions from trusts can generally be structured in a manner which attracts little or no tax, depending on whether the distribution is out of trust income or trust capital. International planning using trusts can be complex and requires cooperation among advisors in your new country of residence, your country of origin, the country in which the trust is established, and every country in which there is a beneficiary of the trust. Trust distributions to a beneficiary will be treated differently depending on where each beneficiary resides. However, despite some complexity in the planning phase, trusts remain by far the most popular wealth planning vehicle for good reason, as the benefits of their use can be significant. For example:

- **Tax efficient distributions:** payments from a trust to its beneficiaries can be managed so as to attract less overall taxation, or no taxation, if the trust has been planned and structured properly. This can include tax-free distributions to Canadian resident beneficiaries, if properly planned.
- **Wealth accumulation:** trusts in low/no tax jurisdictions often have very long lifespans, or are permitted to exist indefinitely. As such, they can accumulate investment gains with little or no tax over a long period, and can effectively preserve and grow capital. As such, capital can effectively be sheltered in the offshore trust indefinitely, with distributions made to beneficiaries as and when desired so that only those distributions are subject to tax when received (assuming the recipient is subject to tax).
- **Transition of wealth:** for the above reasons, it is often very advantageous to structure an inheritance through an offshore trust, where the capital can be better preserved, grown and distributed much more efficiently than if the inheritance were given directly to beneficiaries.

[2] For example, see the popular Henley & Partners indices and reports which rank investment immigration programs, and perceived quality of different residencies and citizenships: https://www.henleyglobal.com/publications

- **Creditor protection:** trusts have long been a popular vehicle for asset protection. Since the trust legally owns the assets, the settlor's creditors cannot seize them (subject to some exceptions where there are concerns around defrauding creditors). And, since beneficiaries usually only have discretionary interests which are not vested, the creditors of the beneficiaries have nothing to seize either. Trusts are also a useful tool to keep wealth outside of the net of "family property" or similar definitions which determine what a spouse is entitled to upon separation, divorce or death.

- **Flexibility and control:** trusts are flexible enough to allow you to transfer legal title to assets and grant beneficiaries economic benefits to or from the assets, without transferring control over the assets. This flexibility to retain control can be useful for many reasons, including in situations where beneficiaries may not be ready to responsibly manage the assets, or, in the context of a family business, where you may not yet know which child or children will be involved in the business upon succession. Often of most interest to settlors is the ability to continue to control the management of the trust's investments, rather than handing over control to a trustee and institutional investment manager.

- **Estate planning benefits:** trusts have a great many benefits in the context of an estate plan, including all of those noted above in this list, along with additional benefits such as the ability to place trust assets outside of the scope of a forced heirship regime, and the fact that trust assets will not be made subject to probate and estate administration procedures which are complex, time-consuming and sometimes expensive.

Once you have selected a destination and have considered how to structure your assets and income in order to achieve a tax-efficient result, you may also need to carefully plan your emigration from your current place of residency. For Canadian residents, there are tax consequences of ceasing to be a resident and there may be planning opportunities to reduce the impact upon your exit. Advance planning is especially important if you own shares in one or more private companies.

In light of the above, it is important that you select an experienced advisor who not only has local expertise along with an international network and capabilities, but who can also mobilize other professionals in your country and your new country of residence (and a suitable trust jurisdiction) in order to provide you with cohesive and complete advice. It is typical to require legal counsel and tax accountants in at least two countries, along with valuation experts and professional trustees, in order to provide complete advice on a tax-driven relocation.

If you would like to explore a change in residency and the potential tax advantages, please do not hesitate to contact us. ■

[See also our earlier inBrief dated 4 October 2021, "Planning for Non-residency – Doing it Right"]

Afridi & Angell

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Afridi & Angell Professional Corporation, Afridi & Angell's Toronto office which was established in 2021, takes advantage of the firm's many Canadian ties and brings to our Canadian clients, and those with Canadian interests, the highest standards of advice and client service for which Afridi & Angell is known. Our Toronto office, which operates as a separate legal entity from Afridi & Angell's UAE offices, provides legal and advisory services in the following areas: corporate and commercial; mergers and acquisitions; tax planning and advisory; asset protection; private client and estate planning; anti-money laundering and anti-bribery compliance; IT outsourcing and contracting; consulting on Canada-UAE opportunities and cross-border legal issues.

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