

TAX ALERT



TAX ALERT is a commentary on topics of current interest – usually topics relating to recent changes in tax law, new CRA administrative practices or current interpretations arising from tax cases. Professional advice should be obtained before acting on any of this information.

EMIGRATING FROM CANADA – TAX PLANNING AND YOUR DEPARTURE

We live in a mobile society these days. People come and go and move from country to country regularly. Here in Waterloo our itinerant population is as big as it gets. With a significant hi-tech and academic population mix from all over the world, borders just become sign posts. In Canada and indeed in most countries of the world, this coming and going has tax consequences.

Many forms are required to be filed with the Canada Revenue Agency (CRA) when you emigrate from Canada. The situation is more complicated if you plan to retain your home in Canada after you leave and convert it to a rental property.

There are significant penalties for not filing the appropriate forms on a timely basis so close attention to detail is important. Form NR74 provides a helpful list of questions to determine if you have become a non-resident of Canada but we do not suggest you submit it to CRA – just use it as a personal checklist.

Tax Laws in Play

Rules in the *Income Tax Act* spell out the tax implications and filing procedures when you cease to be a resident of Canada. There is yet another set of rules dealing with the tax issues when you come here. This article concentrates on the departure implications with no comment on the rules relating to the arrival of new Canadians – a topic for another time.

In general, you need to understand the impact of three separate sets of rules and the interplay between them: 1) rules in the Canadian *Income Tax Act*, 2) tax rules of the other country and 3) rules in international tax agreements between Canada and the other country.

To be more specific, you need to identify how each of your various sources of income will be taxed in both countries in the year you change residence and how the income will be divided between them. And then there is the matter of tax on deemed capital gains on the assets you own at departure. And finally, you should understand how you can avoid double taxation and the punitive penalties that apply for overlooking filings or late filing.

As far as Canada is concerned, the good thing is that when you are done with departure tax filings you are done. That's quite different than United States which continues to tax its citizens no matter where they live in the world or whether or not they have US income.

Capital Gains on Departure

The reporting of employment and investment income is a fairly standard issue, but the reporting of capital gains on the disposition of property (actual or deemed) is a bigger concern. It gets more complicated when you factor in the *departure tax* on the deemed sale of assets.

After you leave Canada, you will eventually pay tax on the unrealized appreciation in the value of the assets you owned when you left Canada. The gains on certain assets will be reported at the time of departure (on your final tax return) but other gains (most notably on Canadian real estate) are not reported until the property is actually sold.

Tax Symmetry Between Countries

Obviously, the taxation rules in Canada and the new country will be quite different so it is important to get some help with these rules in advance to avoid the traps, penalties and possibly double taxation. For example, the United States only recognizes the actual cost of your assets in their tax filings after you move there so you may want to sell certain assets and repurchase them before you leave Canada to increase your cost to current values for US tax purposes.

Canada has a tax treaty with virtually all of the developed countries of the world. Tax treaties are designed to eliminate the contradictions between the tax rules in the departing country and the new country of residence. Tax treaty provisions trump domestic tax law. They work reasonably well but not perfectly and therefore you may need some professional help.

Tax Issues to Ponder

If you are about to leave Canada, here are some concerns you should check out well in advance:

- ◆ Are you really becoming a nonresident of Canada?
- ◆ Do the rules change if you have only lived in Canada for five years or less?
- ◆ What are the implications if you do not sell your home until after leaving Canada?
- ◆ What special tax filings and elections does Canada want and what are the filing deadlines?
- ◆ If you rent out property after you leave, how is that handled?
- ◆ If you overlook some of your filings, can you file a voluntary disclosure with CRA and avoid penalties?
- ◆ Maybe, just maybe, you might come back to Canada and does that matter?

Tax planning your departure from Canada is different for almost everyone. I suggest you think carefully about your situation and get some advice if your situation is at all complicated.

CRA Wants to Know

There are many forms to file when you are heading out of Canada but most of them are filed after you leave Canada. Here is a list with filing dates noted:

<i>Forms</i>	<i>When to File</i>	<i>Applicable</i>
<input type="checkbox"/> T1161 – List of Properties by an Emigrant of Canada	File with final tax return	_____
<input type="checkbox"/> T1243 – Deemed Disposition of Property by an Emigrant of Canada	File with final tax return	_____
<input type="checkbox"/> T1244 – Election, Under Subsection 220(4.5) of the <i>Income Tax Act</i> to Defer the Payment of Tax on Income Relating to Deemed Disposition	File with final tax return	_____
<input type="checkbox"/> T1159 – Income Tax Return for Electing Under Section 216	Due by June 30 following the year you emigrated	_____
<input type="checkbox"/> T2091 – Designation of a Property as a Principal Residence by an Individual	Due with return for year of sale	_____
<input type="checkbox"/> T2062 – Request by a Non-Resident of Canada for a Certificate of Compliance related to the Disposition of Taxable Canadian Property	Due within 10 days of property sale	_____
<input type="checkbox"/> T2068 – Certificate – The Disposition of Property by a Non-Resident of Canada (Certificate of Compliance)		_____
<input type="checkbox"/> NR6 – Undertaking to File an Income Tax Return by a Non-Resident Receiving Rent from Real Property or Receiving Timber Royalty	Due annually before first day of tax year	_____
<input type="checkbox"/> Letter – Ignore Change of Use of Principal Residence	Due with tax return for year of sale	_____
<input type="checkbox"/> 5013-R – Income Tax Return for Non-Residents of Canada (final return)	Due April 30 th following year of emigration	_____
<input type="checkbox"/> Letter – Election to Ignore Change of Use of Principal Residence under Subsection 45(2)	File with tax return for the year	_____
<input type="checkbox"/> NR4 – Non-Resident Tax Withholding, Remitting and Reporting	Due by the 15 th of the month after rent receipt (see T4144 – guide for electing under section 216)	_____

Voluntary Disclosure

A client left Canada in 2005 (this and other information are fictional) and retained their Canadian home which they rented out from 2005 to 2012 when it was sold. Unfortunately, no reporting was ever made to CRA.

As a result, withholding of 25% of the proceeds left sitting in their lawyer's office which they wanted back. To do that, they needed to file all of those uncompleted returns – some which carried penalties for being late.

In the end, almost all of the tax was recovered and all penalties were completely avoided by a voluntary disclosure to CRA. Without filing, the results would have been as follows:

- ◆ Form T2062 - penalty for not filing within ten days of sale
- ◆ Form T1161 - penalty for not filing of the value of properties or ceasing to be a Canadian resident
- ◆ NR6 - tax on the gross income instead of net rental income
- ◆ Form T2091 - partial loss of the principal residence exemption
- ◆ Form T2068 - withholding tax equal to 25% of the selling price of property and not graduated tax on the taxable gain

Conclusion

Leaving Canada is a tricky business. Start thinking about the issues as far in advance as you can and get some professional advice. If you don't, your life will take on a considerably grimmer aspect not to mention the cost in taxes and penalties. *This article first appeared in the Exchange magazine.*

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