Live and Invest Overeas

Taxes for Canadians Going Offshore by George C Gonzalez, PhD

Outline

I. Residency v. Non-residency
II. Taxation of Residents
III. Taxation of Non-residents
IV. Tax Treaties
V. The Departure Tax

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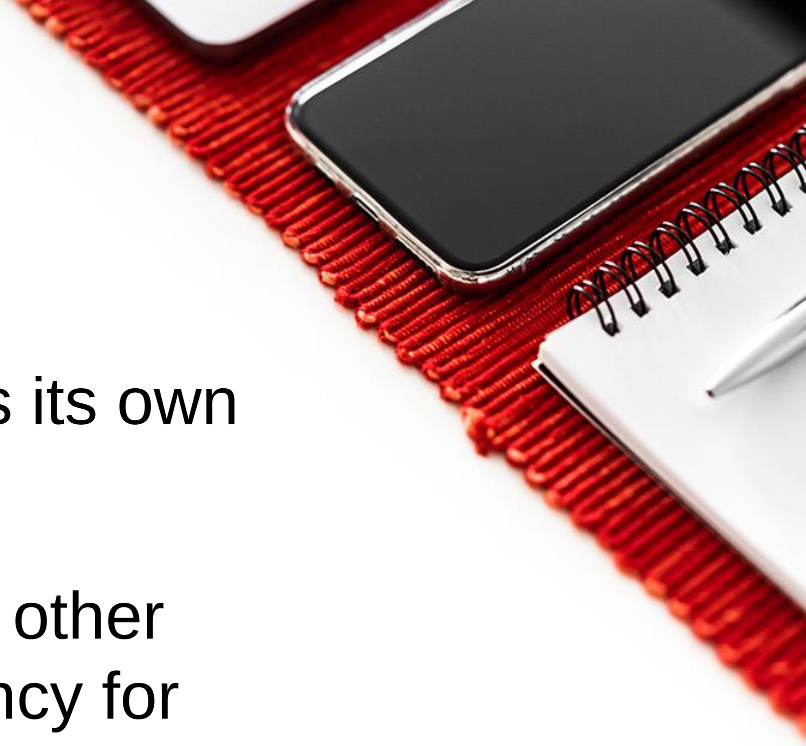
Tax Residency



- Residency for tax purposes has its own set of definitions.
- It is different from residency for other purposes. For example: residency for provincial health plans.

Residency v. Non-residency

Canadian tax residency means:

- You pay tax on your world income, i.e., income from all sources, both Canadian and foreign.

Canadian tax non-residency means:

- You pay tax on Canadian source income only.

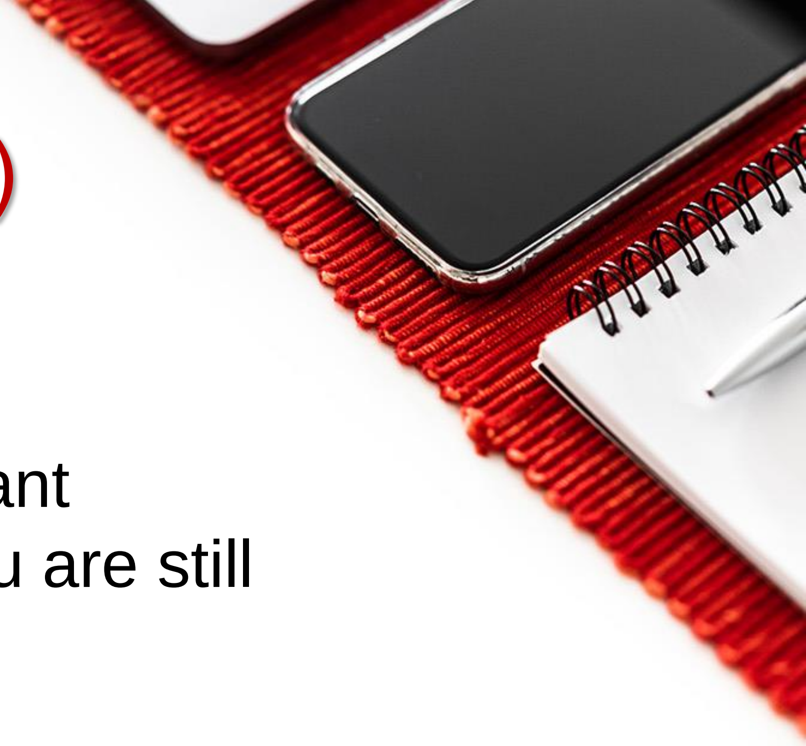
Residency: Tests

- Many different tests.
- It is not as simple as the “six-month” rule.
- It is possible to spend less than six months of the year in Canada yet be considered a tax resident.

Residency: Tests (cont'd)

- One test, for example, falls under the "significant residential ties" test.
- It says that if you maintain a dwelling place in Canada after you expatriate, you are still considered a resident.

Residency: Tests (cont'd)



- … or if your spouse or dependant continues to live in Canada, you are still considered a resident yourself.

Residency: Tests (cont'd)

- It is recommended that you become familiar with the different tests.

- Read the CRA's Tax Folio on residency https://www.canada.ca/en/revenue-agency/services/tax/technical-information/income-tax/income-tax-folios-index/series-5-international-residency/folio-1-residency/income-tax-folio-s5-f1-c1-determining-individual-s-residence-status.html.

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Taxation of Residents

- Some foreign income has special rules. Examples:
  - Foreign dividend income
  - Foreign tax credits
  - Foreign Accrual Property Income (FAPI) earned by a foreign corporation

Foreign Dividend Income

- No gross-up (like for eligible or non-eligible dividends from Canadian corporations)
- No dividend tax credit, either.

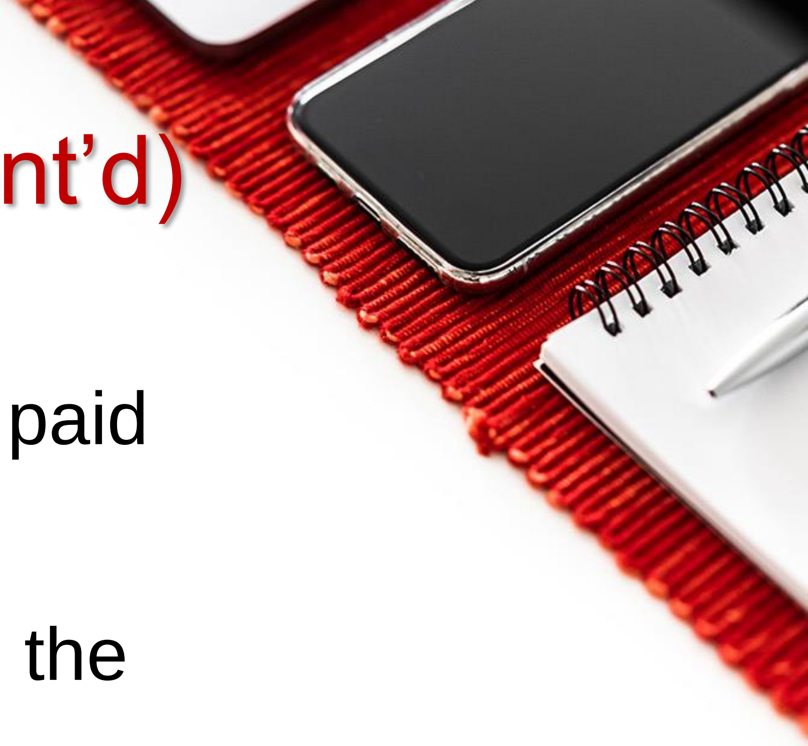
Foreign Dividend Income (cont’d)

- Foreign tax credit for any foreign taxes paid on foreign dividend income.

Foreign Tax Credits

- A credit may be taken for foreign taxes paid on foreign source income.
- Examples of foreign source income that may have foreign taxes:
  - Dividends
  - Rental property income

Foreign Tax Credits (cont’d)

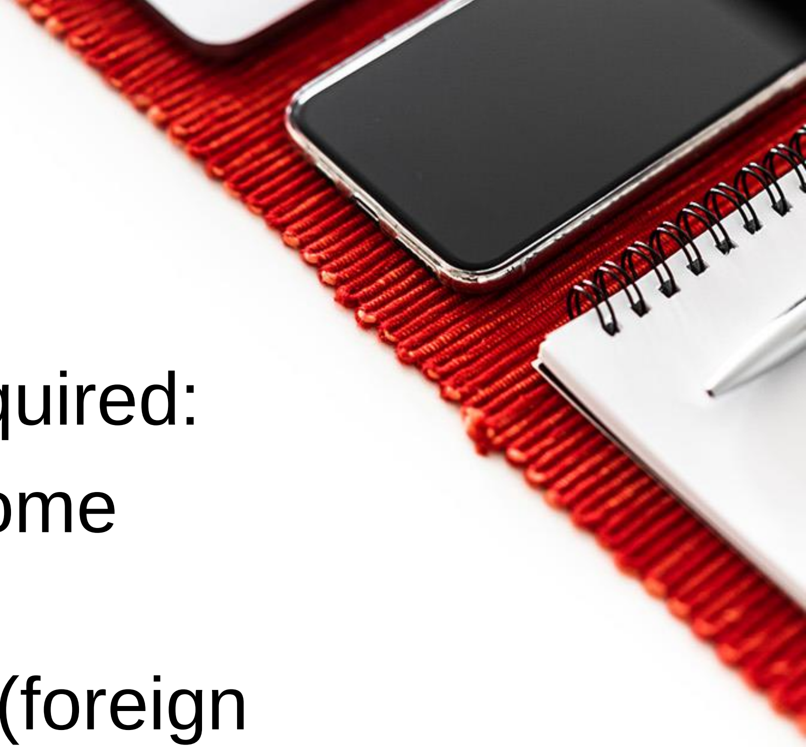


- Foreign tax may have to be paid through tax withholding.
- Withholding tax depends on the country of origin

Foreign Activity Reporting

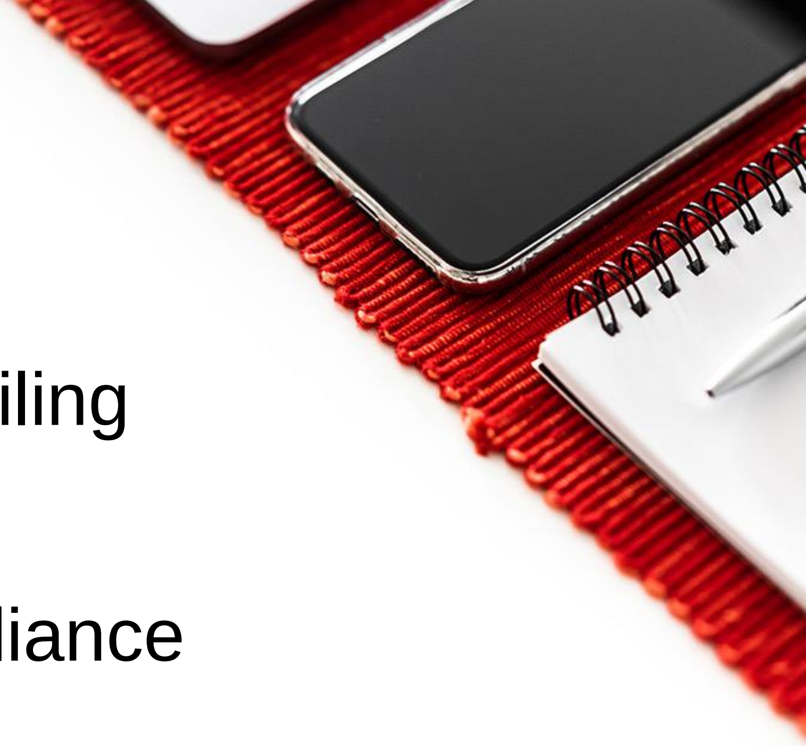
- There are various annual foreign reporting forms that may be required.
- A well-known one is Form T1135 (Foreign Income Verification Form)

Foreign Activity Reporting (cont'd)



- Other forms that may be required:
  - Form T1134 (shares in some foreign corporations)
  - Forms T1141 and T1142 (foreign trusts)

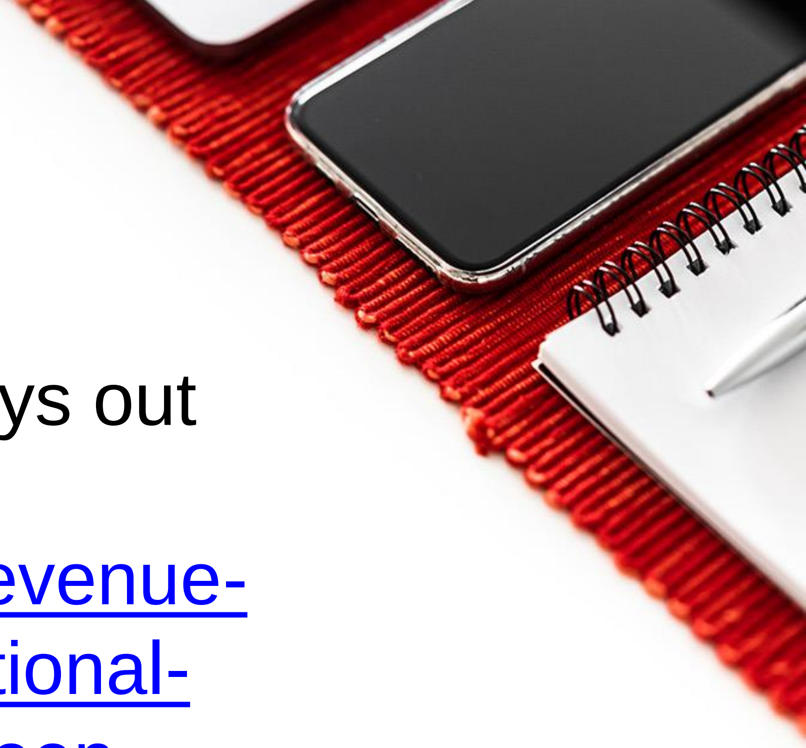
Foreign Activity Reporting (cont'd)



- Be sure to comply with the filing requirements!
- The penalties for non-compliance can be severe.

Foreign Activity Reporting (cont’d)

- This CRA reference page lays out the penalties: https://www.canada.ca/en/revenue-agency/services/tax/international-non-residents/information-been-moved/foreign-reporting/table-penalties.html



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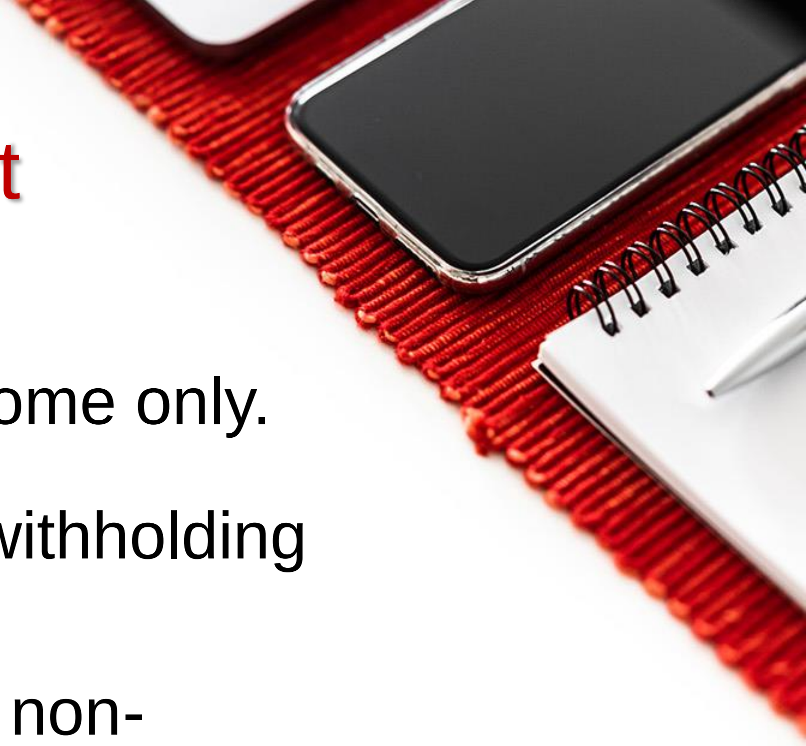
Taxation as a Non-Resident



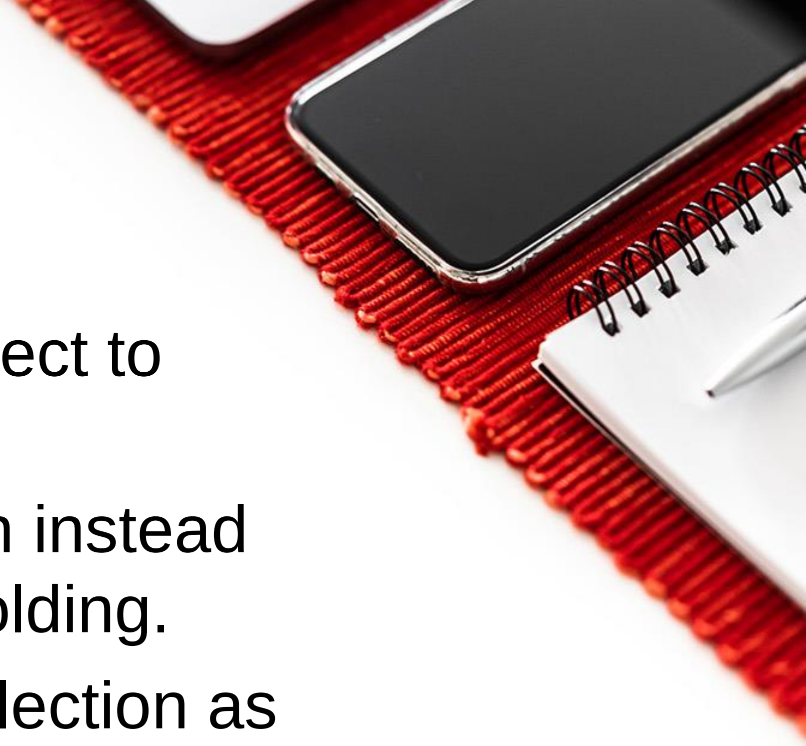
- Taxed on Canadian source income only.
- On most types of income, tax withholding applies.
- For others, must file an annual non-resident income tax return (Form 5013-R).

Common Types of Income Subject to Tax Withholding

- CPP and OAS
- Private pension income
- Registered plan withdrawals (RRSP, RRIF, etc.)
- Rental property income

Tax Withholding Rate

- The default rate for tax withholding is 25%.
- The rate may be lower if a tax treaty applies (more on this later).



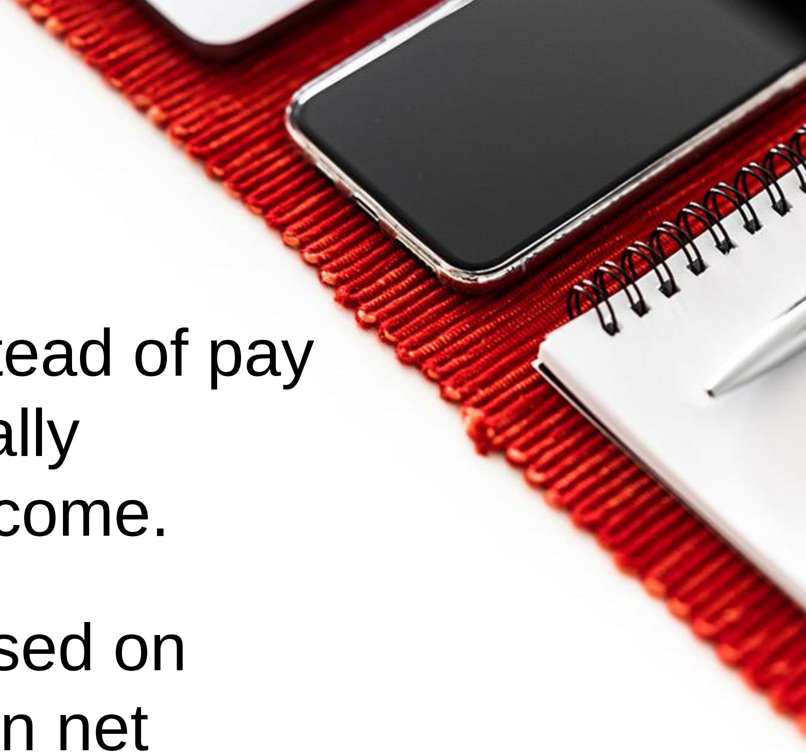
Election to File in Lieu of Withholding

- For some types of income subject to withholding:
  - you may elect to file a return instead of paying tax through withholding.
  - It is worth looking into this election as it may save on your tax bill.

Election to File in Lieu of Withholding (cont'd)

- Types of income for which election is possible included:
  - Pension (CPP, OAS and private)
  - Rental property income

Election to File in Lieu of Withholding (cont’d)



- The election to file a return instead of pay withholding tax may be especially beneficial for rental property income.
- Main reason: withholding is based on gross rental income (rather than net income after deductions).

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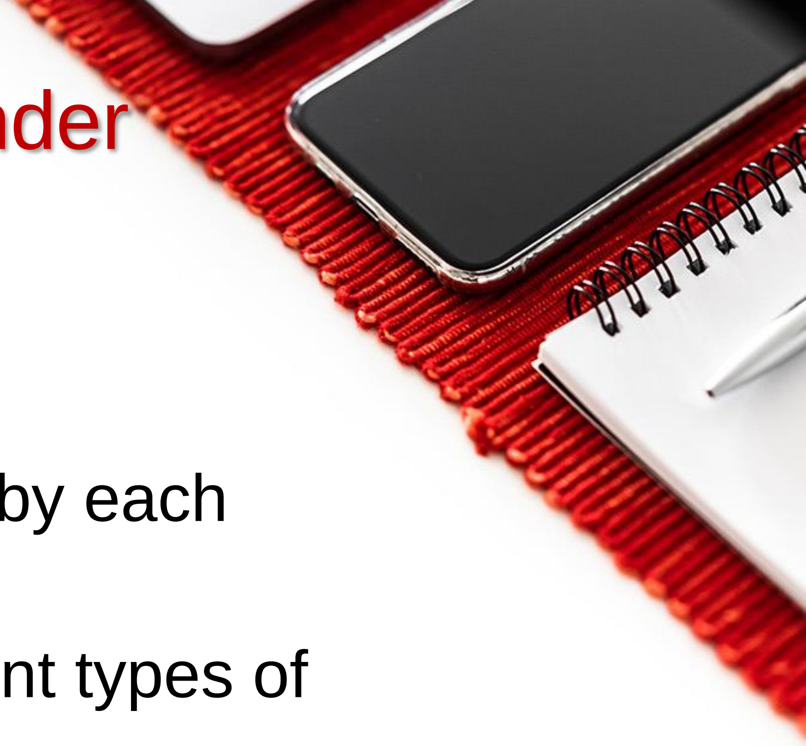
Tax Treaties

- Canada has tax treaties in force with about 94 countries.
- A tax treaty overrides Canada’s, and the other country’s, general tax laws.

Items Typically Covered Under a Tax Treaty



- Definition of residency
- Types of income subject to tax by each country
- Tax withholding rates for different types of income paid out of country (e.g., dividends, rent, royalties, etc.)

Tax Treaties

- Very important to find out if there is a treaty between Canada and your new country of residence.
- … and find out how it may affect your taxes.

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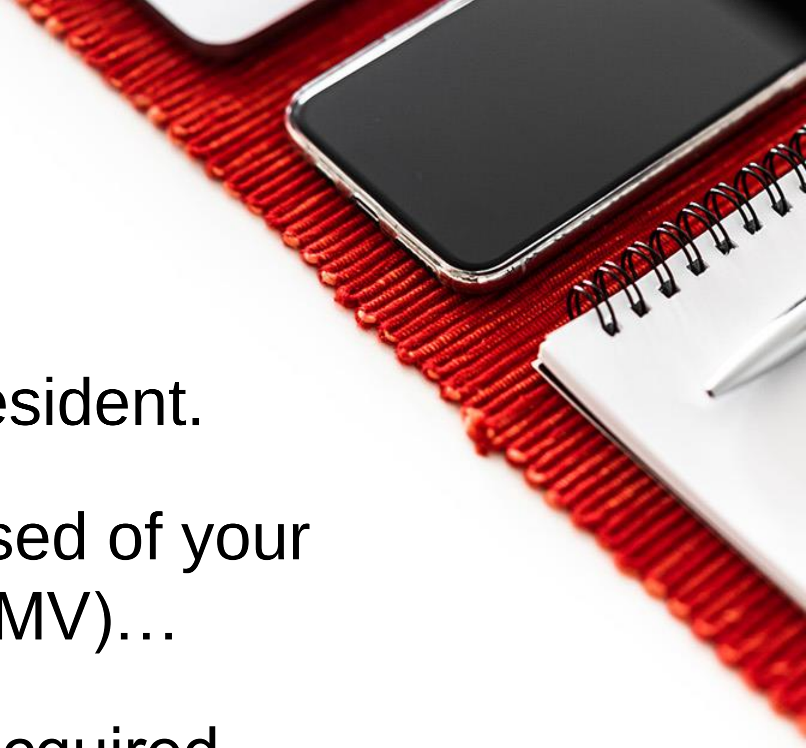
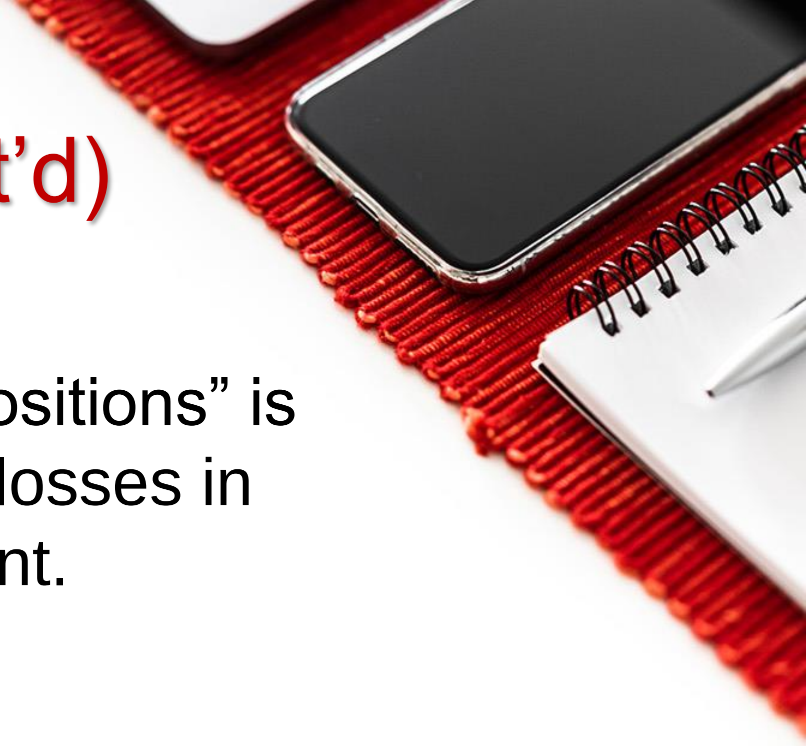
Departure Tax



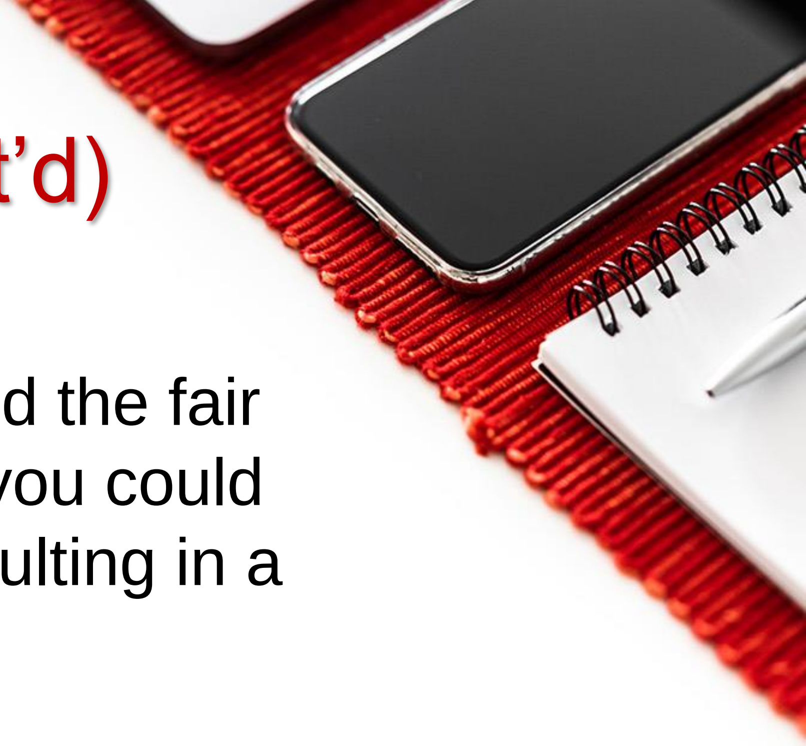
- Applies on your last day as a resident.
- You are deemed to have disposed of your property at fair market value (FMV)…
- … and to have immediately reacquired the property for the same amount.

Departure Tax (cont’d)



- The effect of the “deemed dispositions” is that you will have gains and/or losses in your final tax return as a resident.

Departure Tax (cont’d)

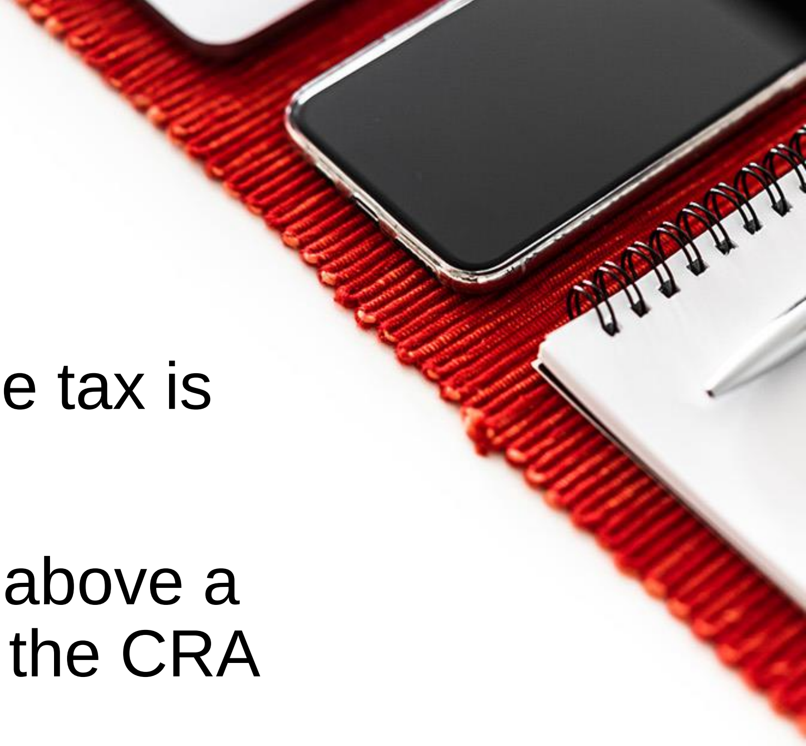


- Depending on the cost base and the fair market value of your property, you could potentially have large gains resulting in a high tax bill.

Departure Tax (cont'd)

- Not all property is subject to the departure tax.
- Examples of exempt property:
  - Canadian real estate
  - Registered plans (RRSP, RRIFs, etc.)

Departure Tax (cont’d)



- An election to defer payment the tax is available.
- If the deferred amount of tax is above a threshold (about $16,000) then the CRA will require a security deposit.
- A collateral security agreement may be arranged with CRA.

Departure Tax Planning

- If you are planning to expatriate, it highly recommended to project what the departure tax will be.
- With advance planning, you may be able to minimise the impact of the departure tax.

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