



## Income Tax Issues Associated with Emigrating from Canada

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*Our goal is to provide updates on topical tax issues. Information contained in the newsletters is not meant to be a comprehensive summary of the issues raised. Rather, we wish to bring what we believe to be important issues to the attention of our valued clients. We would be pleased to discuss any questions that you, the reader, might have in greater detail.*

An individual who is resident in Canada during a tax year is subject to Canadian income tax on his or her worldwide income from all sources. A non-resident individual, on the other hand, is generally only subject to Canadian income tax on income from sources inside Canada. Therefore, the determination of a taxpayer's residency status and the date of a change in their residency status, if applicable, is important.

The term "resident" is not defined in the Income Tax Act, however, its meaning has been considered by the Courts. The Canada Revenue Agency's ("CRA") Income Tax Folio S5-F1-C1 – Determining an Individual's Residency Status summarizes the key factors to be considered in determining a taxpayer's residency status. These key factors are referred to as residential ties. For taxpayers who have historically been residents of Canada to become non-residents of Canada for income tax purposes, it is necessary to break these residential ties with Canada.

Residential ties are divided into two categories: (1) significant, those that could determine residency status on their own, and (2) secondary, those that would not individually be determinative.

### SIGNIFICANT RESIDENTIAL TIES

There are three significant residential ties:

1. Dwelling place – The existence of a dwelling place in Canada available for the taxpayer to return to is a significant tie. CRA has said that the renting of the dwelling on arm's length terms and conditions may render the dwelling a secondary tie.
2. Spouse – If they remain in Canada while the taxpayer is abroad, they would be considered to be a significant residential tie.
3. Dependents – similar to a spouse, if they remain in Canada while the taxpayer is abroad, they would be considered to be a significant residential tie.

If any of the above residential ties apply, the taxpayer will likely be considered a Canadian resident for tax purposes.

### SECONDARY RESIDENTIAL TIES

Generally, secondary residential ties must be looked at collectively in order to evaluate the significance of any one such tie. For this reason, it would be unusual for a single secondary residential tie with Canada to be sufficient on its own to lead to a determination that an individual is factually resident in Canada while abroad. The most common secondary ties are:

- Personal property situated in Canada (furniture, clothing, automobiles)
- Social ties with Canada (recreational or religious memberships in Canadian organizations)
- Economic ties to Canada (employment with Canadian employer, Canadian bank accounts, RRSP, credit cards, securities accounts)
- Hospitalization and medical insurance coverage from a Canadian province
- A driver's license from a Canadian province
- A vehicle registered in a Canadian province
- A seasonal dwelling or leased dwelling in Canada (cottage)
- A Canadian passport
- Membership in Canadian unions or professional organizations

For people emigrating from Canada, as many of these secondary ties as possible should be broken to ensure a "clean break" is made from Canada for income tax purposes.

### DATE OF CEASING CANADIAN RESIDENCE

The date upon which a Canadian resident individual leaving Canada will become a non-resident for tax purposes is a question of fact that can only be determined after reviewing all of the relevant facts and circumstances of a particular case. CRA will generally consider that the date at which a taxpayer has severed his or her residential ties to Canada to be the latest of the dates:

1. The individual leaves Canada,
2. The individual's spouse and dependents leave Canada, or
3. The individual becomes a resident of the country to which he/she is immigrating.

It is often advisable for taxpayers who are leaving Canada to complete form NR73 – Determination of Residency Status (Leaving Canada) and file it with the CRA. The form asks a number of questions related to the residential ties outlined to allow the CRA to make a determination of when the taxpayer ceases to be a Canadian resident. This provides certainty as to the date the taxpayer ceased to be resident of Canada for income tax purposes.

## FILING CANADIAN TAX RETURNS

As indicated, an individual who is resident in Canada during a tax year is subject to Canadian income tax on his or her worldwide income from all sources. Generally, a non-resident individual is only subject to Canadian income tax on income from sources inside Canada. Taxpayers must indicate a date of emigration on their final Canadian tax return. From this date to the end of the year they will be taxed as a non-resident of Canada and will be subject to the income tax provisions of their new country of residence.

There are some special forms which must be filed with the final Canadian personal tax return upon emigration. Form T1243 – Deemed Disposition of Property by an Emigrant of Canada and Form T1161 – List of Properties by an Emigrant of Canada must be filed by the taxpayer's filing due date (generally April 30). These forms provide information about significant assets of the taxpayer to the CRA to help them assess the completeness of the reporting on the final Canadian tax return. It is important to note that each form is subject to a maximum penalty of \$2,500 if they are not filed by the deadline.

## DEPARTURE TAX

Upon ceasing to be resident in Canada, taxpayers are required to pay Canadian income tax with respect to capital gains arising from the deemed disposition of all of their capital property. This is commonly referred to as "departure tax". Capital property includes real estate, investments in non-registered accounts and shares of privately held corporations. To the extent that there are accrued gains on any of these items, this will result in Canadian income tax on the final Canadian personal tax return. Departure tax can be significant, and so it is always advisable to speak with a tax advisor prior to leaving Canada.

It is important to note that penalties apply if a taxpayer knowingly, or under circumstances amounting to gross negligence, makes a false statement or omission on their personal tax return or the T1243 and T1161 forms. The penalty is equal to 50% of the understated tax and/or the overstated credits related to the false statement or omission. Therefore, it is important to include all assets and provide best estimates regarding fair market value for the purposes of this reporting.

## CONCLUSION

Residency status can often be a complicated determination. For the reasons outlined, the required reporting can vary greatly depending on whether someone is resident of Canada, non-resident of Canada, or if their residency status changes during the year. Ongoing Canadian tax requirements once a person is a non-resident of Canada is beyond the scope of this newsletter. However, it is important to note that there are often special reporting and withholding requirements in these cases. We recommend seeking professional advice if you are considering leaving Canada for a significant amount of time to ensure you understand all of the income tax implications.