

Thinking about leaving Canada?

TAX-SMART INVESTING®

In a country like Canada, where taxes can be almost 50% of your taxable income, saving taxes should always be a priority.

At AIC, our investment approach incorporates tax planning to minimize your investment tax bill each year. This approach to maximize your after-tax returns is evidenced by our commitment to tax-smart education, a strong corporate philosophy grounded in tax minimization and our tax-smart investment products.

A tax-smart portfolio is a portfolio that focuses on maximizing after-tax investment returns. After all, it's not how much you earn, but how much you keep that matters most.

AIC believes in maximizing after-tax wealth (i.e. your bottom-line cash flow). We are proud of being Canada's tax-smart investment manager and a committed educator of Canadians in matters of investing, tax planning and an integrated tax-smart investment approach.

This brief is one in a series on tax-smart investing. We believe you will find this brief, along with our tax-smart investment products, helpful in maximizing the value of your taxable investment portfolio.

Whether you are leaving Canada to retire under sunnier skies, moving to a new job, or simply spending time outside of Canada, there are some things you need to know before you pack your bags. This bulletin will help you answer some of the more commonly asked questions such as: Who is considered to be a resident of Canada? Will I still be liable for Canadian income taxes? What happens to my assets when I leave Canada?

Who is liable for Canadian income tax?

Canada levies taxes based on residency, not on citizenship the way that some other countries do. Therefore if you are considered to be a resident of Canada for tax purposes, you will pay tax to Canada on all your worldwide income. The problem is that determining residency is not just a question of looking up your mailing address. Some people who leave Canada do not sever their ties with Canada properly and end up still being considered a resident here, despite the fact that they don't live here.

There are a number of factors considered when determining whether or not you are a resident of Canada. According to Interpretation Bulletin IT-221R3- *Determination of an Individual's Residence Status*, the Canada Revenue Agency (CRA) will look at four factors when determining if a taxpayer has given up residence in Canada. If it is found that the person has in fact given up residence, a Canadian tax return does not have to be filed for income earned after the date of departure. If the person is found to still be a Canadian resident (for tax purposes) this person is still liable for Canadian tax on his/her worldwide income and must file a Canadian tax return each year.

The four factors that the CRA considers are:

- 1) Residential ties with Canada;
- 2) Evidence of intention to permanently sever residential ties with Canada;
- 3) Residential ties elsewhere; and
- 4) Regularity and length of visits to Canada.

Residential ties with Canada

Significant Residential Ties – A person’s residential ties with Canada are the most important factor that the CRA will look at to determine whether or not someone is a resident. While a number of factors are looked at to determine an individual’s residential status, if a person does not sever all significant residential ties with Canada prior to leaving, that person will generally be considered to be a resident of Canada. Significant residential ties include the location of a person’s dwelling place, spouse or common-law partner and dependants.

If an individual leaves Canada but keeps a home in Canada (whether owned or rented) available for his or her own use, the home will be considered to be a significant residential tie with Canada during the individual’s stay abroad. However, if an individual rents his or her home to a third party on arm’s length terms and conditions, the CRA will take into account all of the circumstances of the situation and may not consider the home to be a significant residential tie with Canada.

As you would suspect, if an individual who is married or cohabiting with a common-law partner leaves Canada, but his or her spouse remains in Canada, then that spouse will usually be a significant residential tie with Canada during the individual’s absence from Canada. However, where an individual was living separate and apart from his or her spouse prior to leaving Canada, by reason of a breakdown of their marriage or common-law partnership, that spouse or common-law partner will not be considered to be a significant tie with Canada. If an individual with dependants under the age of 18 leaves Canada, but his or her dependants remain behind, then those dependants will usually be considered to be a significant residential tie with Canada while the individual is abroad.

Secondary Residential Ties – The CRA will also look at a person’s secondary residential ties to Canada. Usually these secondary ties are looked at collectively, which means just because a person still holds on to one or two of these ties, does not necessarily mean he or she will automatically be considered a resident of Canada.

Secondary ties include:

- Personal property in Canada (such as furniture, clothing, automobiles and recreational vehicles);
- Social ties with Canada (such as memberships in Canadian recreational and religious organizations);
- Economic ties with Canada (such as employment with a Canadian employer and active involvement in a Canadian business, Canadian bank accounts, retirement savings plans, credit cards and securities accounts);
- Landed immigrant status or appropriate work permits in Canada;
- Hospitalization and medical insurance coverage from a province or territory of Canada;
- A driver’s licence from a province or territory of Canada;
- A vehicle registered in a province or territory of Canada;
- A seasonal dwelling place in Canada or a leased dwelling place;
- A Canadian passport; and
- Memberships in Canadian unions or professional organizations.

Evidence of intention to permanently sever residential ties with Canada

Whether an individual is permanently severing his or her ties with Canada will depend in part on his or her intentions at the time of departure. In the past, a person’s length of stay abroad was used to determine this intention. In fact, a rule of thumb used to be if a person was planning to be absent from Canada for at least two years, that person would generally be considered to be a non-resident. Although length of absence from Canada is still one factor that is considered, there is no longer a set

amount of time that a person should stay away in order to be considered a non-resident. Instead, if there is evidence at the time a person leaves that he or she is planning on returning, then the CRA will look to see if strong residential ties remained here as well. For example, if a person leaves Canada on a non-renewable contract for one year, the CRA will use this as evidence that the person did not intend to permanently sever ties with Canada, if and when the person returns to Canada.

Another factor that the CRA will look at to determine whether there is an intention to permanently sever ties with Canada is how the taxpayer filed his or her tax return in the year that he or she left Canada. Individuals who are leaving Canada permanently and are in fact becoming non-residents of Canada, are deemed to dispose of the majority of their assets for fair market value proceeds at the time of departure. These individuals must either pay or post acceptable security for tax liability arising from this deemed disposition. The CRA will look to see whether this requirement is met as an indication of an individual's intention to permanently sever ties with Canada. You will find more on the topic of departure tax and security below.

Residential ties elsewhere

Similar to severing ties with Canada, the CRA will also look to ensure that an individual develops residential ties with the other country. Therefore, an individual should develop as many secondary residential ties as described above as possible (i.e. buy or rent a home, get a driver's licence, join clubs and memberships, etc.) in the other country.

Regularity and length of visits to Canada

If a person is present in Canada for 183 days or more in a year, the person is deemed to be a Canadian resident for tax purposes. However, even with fewer days than this, the CRA may still consider you to be resident if these visits are more than just occasional and the person has maintained some secondary residential ties with Canada.

As you can see, the way you structure your affairs prior to leaving Canada can speak volumes about

whether or not you will be considered a resident here, so be sure to speak to a tax professional who can help you before you leave.

Leaving Canada

If you are leaving Canada and all factors indicate that you will be considered a non-resident, there are a few things you should keep in mind. In the year you leave Canada, you will be taxed on all your worldwide income (the same as you always were) up to the time when you leave Canada and become a non-resident. You may also be subject to departure tax. On the date of departure, a person is deemed to have disposed of most capital assets for fair market value proceeds. If the assets have appreciated in value, a capital gain and tax liability will result. These capital gains are reported on your personal tax return for the year of departure. Pensions and other retirement savings plans (including RRSPs, RRIFs and RESPs), business properties and real property located in Canada are not subject to departure tax. Be sure to speak to a tax professional prior to leaving Canada in order to prepare an estimate of the tax liability resulting from this deemed disposition.

Due to the large potential tax liabilities in the year of departure, with no corresponding cash inflows (as you are not really selling all of your assets for proceeds), a person may post acceptable security with the CRA, in lieu of paying tax in the year of departure. For example, a letter of credit, a mortgage, a bank guarantee, or even the assets subject to the deemed disposition could be considered acceptable security. When the asset is actually sold, the security will be returned and the departure tax is due at that time. The maximum amount of tax that can be deferred by posting security is the tax arising from \$100,000 of gains.

A person giving up residency does not have to file any special forms with the CRA. The individual should simply enter the date of departure on page 1 of their personal tax return. There is no requirement to file form NR73 *Determination of Residency Status (Leaving Canada)*. This form is basically a questionnaire pertaining to the individual and his or her ties and intentions when leaving Canada. Sometimes individuals will fill out this form thinking

it is a CRA requirement and send it to the CRA. It is generally not recommended to file this form since the information could be used against the taxpayer. That is, the CRA uses the information you provided to argue against your claim as to whether or not you are a resident of Canada.

Investment accounts in Canada

If you are ceasing Canadian residency, you can still keep your investment accounts (including registered accounts) in Canada. However, you must inform your financial institutions that you are a non-resident so that your accounts can be coded accordingly. You should also speak with your investment advisor, as there may be securities laws in the other country that would restrict your ability to deal with, and give instructions on your different investment accounts.

If payments are made to non-residents, withholding taxes will be taken off at source. The general withholding tax rate is 25 per cent for most payments such as withdrawals from an RRSP or RRIE, dividends or interest. Capital gains are taxable only in the country of residence (unless “taxable Canadian property” such as Canadian land is being sold). The 25 per cent withholding rate is usually reduced if there is a tax treaty between Canada and the other country of residence. Current tax treaties in force can be found at: http://www.fin.gc.ca/treaties/treatystatus_e.html

Even as a non-resident, you should still focus on tax-smart investing – and that’s where AIC can help. Keeping all of your AIC Fund investments intact prior to leaving Canada makes sense. Why? By holding investments, such as AIC Funds, that minimize taxable distributions annually and instead concentrate on long-term appreciation, you’ll minimize any withholding taxes payable to Canada. This should always be a focus, but especially if you’re moving to a tax-haven country or a country with very low tax rates. If you invest in funds that have annual distributions, you will have to pay withholding tax to Canada. The problem is, if your country of residence has lower tax rates than the amount of withholding tax you pay, you will not be able to claim a full foreign tax credit for the amount

of tax paid to Canada. This means you’re paying more tax than you have to. That’s why holding AIC Funds as a non-resident makes sense – by minimizing distributions, you minimize your tax liability, leaving more money in your hands to grow for the future.

RRSPs and RRIFs in Canada

RRSPs are one of the few assets that escape departure tax and since an RRSP is likely one of your largest assets, it’s important that you are aware of some tax planning strategies for RRSPs before you leave Canada.

First, in the majority of cases it makes sense not to collapse your RRSP prior to leaving Canada. The reason is because if you collapse the plan, the full amount of the proceeds will be included in your Canadian income and taxed at your marginal tax rate – which may be almost 50 per cent. If you decide after you leave Canada that you need the money, you will only pay a 25 per cent withholding tax to Canada. There may also be tax to pay in the country you move to, but chances are it will be less than the amount you would have paid in Canada.

If you’re moving to the U.S., there are some special tax-planning strategies of which you should take advantage. First, you should bump up the cost amount of the assets that have grown in value inside your RRSP. When money is taken out of the registered plan once you are a resident of the U.S., you will then only pay tax on the growth inside the plan since leaving Canada – not on the cost amount. Therefore, if you sell and repurchase all the assets inside your plan that have grown in value prior to becoming a resident of the U.S., you will bump up your cost amount inside your RRSP and will have a greater tax-free withdrawal in the U.S. once you are a resident there.

Another idea is to ensure that if you need to take money out of the plan while in the U.S, that these withdrawals are considered to be periodic withdrawals, not lump-sum withdrawals. In this way, the withholding tax owing to Canada will be reduced from 25 per cent to 15 per cent under the Canada-U.S. tax treaty. You can ensure that your

withdrawals will be considered periodic payments by converting your RRSP to a RRIF before making withdrawals, and withdrawing no more than twice the required minimum withdrawal each year, or 10 per cent of the fair market value of the plan annually, whichever is greater.

Conclusion

Leaving Canada is not as simple as packing your bags and heading to the airport. There are many factors you need to consider – tax being a major one. Be sure not to get caught by simply assuming

that you will or will not be considered a resident in Canada. If your situation is unique, it's important to visit a tax professional before you get on that plane so you can rest assured that your tax planning has been taken care of properly.

Canadian provinces and territories impose their own tax rates in addition to the federal tax rates. Therefore, depending on where an investor lives, that individual's tax rate may differ from any examples shown. The content of this bulletin is for informational purposes only and in no way should be construed as tax or investment advice. Please consult a professional advisor for advice related to your specific situation.

AIC's STRATEGY FOR SUCCESS:

BUY.

A simple summary of our approach to mutual funds at AIC is this: choose the right heroes and keep the faith. We buy into excellent companies — the best of the best — in strong, long-term growth industries and we hold these investments for the long run. The goal is a better rate of return for our clients.

HOLD.

Stand for nothing and you are likely to fall for everything. The truth is, bears, bulls and other unpredictable market influences eventually disappoint short-term investors who focus on share prices rather than a company's true worth. At AIC, we stick with the quality businesses in which we invest.

AND PROSPER.

Prosperity to us means meeting the three objectives of investing. It means preserving your principal over the long term. It means growing your money at a good rate. And it means protecting your investment from the ravages of taxes. It's really quite simple. And the results over the long term are something to behold. Of course, what you do with your prosperity in the end is up to you.

Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated. Commissions, trailing commissions, management fees and expenses may be associated with mutual fund investments. Please read the prospectus before investing.

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