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IMMIGRATING TO CANADA:

Tax Issues To Consider

Beside the new challenge of settling into a new home and new culture, immigrants to Canada sooner or later will have to face the Canadian income tax system.

When moving to a new country, it is better to know from the outset what the tax issues are so proper steps can be taken to benefit from some of the rules.

I moved to Canada 25 years ago as a newlywed young man excited to embark on a new life experience. When I stepped onto Canadian soil, I had no idea of the tax system; I only knew that in my home country Italy, the tax regime was very strict and people were devising all sort of tricks to "minimize" taxes.

For Canadian tax purposes, individuals moving to Canada will generally be considered residents. Canada's *Income Tax Act* does not make reference to citizenship or immigration status. It simply states that Canadian tax "residents" are bound annually to pay tax on their worldwide income and to declare the existence of substantial foreign assets located outside Canada. The latter obligation is called "foreign asset disclosure."

Residency is determined on the facts of each case. Here are some examples.

- The nature of the stay in Canada
- The length of the stay
- Whether or not the individual is accompanied by his or her family
- The individual's centre of economic interests
- The individual's intentions
- Whether or not the individual is registered in a municipal register to vote
- The place where bank accounts are held
- The place where the person's assets are located
- The terms of employment
- Entitlement to subsidized healthcare

It is possible for an individual to be considered resident of more than one country under the domestic laws of each country. In that case, the individual could be subject to double taxation; there are, however, relief provisions in place such as tax treaties and conventions that Canada has signed with other countries. Those conventions will provide for determination of residency between the two countries that will override the domestic law.

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For the most part, an individual moving to Canada with his or her family to start a new life generally will be considered a resident of Canada for tax purposes.

As mentioned earlier, all Canadian tax residents must report their annual income and pay tax on it. The annual income includes any worldwide income from employment, interest, rent, dividends, capital gains, and pension. If any tax is paid in the foreign country, the Canadian tax system provides for a foreign tax credit to reduce or minimize the burden of double taxation.

Some tax concessions are available to new immigrants.

Deemed Acquisition Rule

Prior to establishing residency in Canada, an individual is deemed to have disposed of all his or her assets—other than taxable Canadian property—and to have re-acquired the same assets at fair market value. Accordingly, gains or losses accrued prior to becoming a Canadian resident are irrelevant when calculating Canadian tax liability at the time the property is sold. The immigrant will calculate the capital gain or loss based on the fair market value at the date of immigration.

Thus, if an individual has highly appreciated assets and establishes residency in Canada prior to selling the asset and if the gain is not subject to tax in another country, he or she may not be taxed on a portion of capital gain. On the other hand, if assets have declined in value prior to moving to Canada, the loss is not available to offset other capital gains earned while in Canada.

As mentioned above, taxable Canadian properties owned by the immigrant prior to moving to Canada are not subject to the tax concession and their cost basis will be the original cost at the time of purchase. Taxable Canadian properties include real property situated in Canada, property used to carry on a business in Canada, certain shares of public corporations, shares of private corporations resident in Canada, and Canadian resource property.

It is recommended that an individual moving to Canada prepare an inventory of the assets owned and establish the market value at the time of entry in Canada. That documentation will be valuable when the assets are sold at a later date.

Immigration Trust

If an individual immigrating to Canada has significant non-Canadian investments that will be subject to Canada's high tax rates once the individual has established Canadian residency, the individual can set up a foreign trust before moving to Canada.

The income from the investment can be sheltered from Canadian taxation for a period of up to 60 months, provided the income earned in the trust is not distributed to a Canadian resident who was the settlor.

That strategy may be advantageous if the trust can be established in a low tax-rate jurisdiction. For the trust to be considered a nonresident trust, it must be established and settled prior to the settlor and beneficiaries establishing residency in Canada. In addition, the majority of the trustees must be nonresident of Canada.

An immigrant individual can contribute his or her foreign investment to the trust for his or her own or family benefit prior to immigrating and avoid Canadian tax for 60 months, provided the income is not paid to the beneficiaries. If after the 60-month period the settlor remains resident of Canada, the income from the trust will be subject to Canadian income tax.

That is a particularly complex matter where expert advice should be obtained before making any decisions as to whether to establish the trust.

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Employment Income

Employment income is taxed when received.

- If an individual earns employment income abroad while nonresident but is not paid until moving to Canada, the income will be taxable in Canada.
- The individual will receive a foreign tax credit.
- There is, however, the risk that higher tax will be paid because the income will be taxed at the individual's marginal tax rate but the foreign tax credit is calculated at the average rate.
- It is therefore a good tax planning strategy to receive all the employment income earned abroad prior to moving to Canada.

Rental Income

When individuals immigrate to Canada, they will often rent-out their property in their home country until they sell it or until they return. Rental income on a foreign property, net of the rental expenses, is included in the resident's Canadian taxable income.

Moving Expenses

Moving expenses to immigrate to Canada are generally not deductible. In planning the move for employment purposes into Canada, it is advisable that the employer reimburse the new employee for moving expenses. Moving expense reimbursements are not taxable to an employee, provided they are reasonable in the circumstances.

Personal Tax Credits

Every taxpayer is entitled to personal exemptions. For example, in 2011 the first $10,382 of income was not taxable. The basic personal exemption, however, is calculated and pro-rated based on the period of residence. If the new immigrant moved to Canada in December, the immigrant would be entitled only to $1/12^{th}$ of the exemption. It is therefore important to choose a moving date that will maximize the benefit of the exemption. There is one exception to this rule—if the individual immigrant has earned more than 90 percent of the income in Canada, the individual is entitled to the full personal exemption.

The tax consequences of moving to Canada and establishing Canadian residency may result in additional tax costs for the individual. The costs may be reduced with adequate tax planning prior to the move and, keeping in consideration the immigrant's individual circumstances, he or she should seek the advice of a tax professional while planning the move. ▲

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Correction from the Summer *Scrivener*, page 72:

"The value of the building will not be taxable but the land will qualify only for the principal residence exemption if it can be considered as contributing to the use and enjoyment of the property and the land does not exceed a half hectare in size or ~~2.47~~ **1.235** acres."