THE GLOBE AND MAIL

TAX MATTERS

Consider these four tax manoeuvres before moving to the United States

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SPECIAL TO THE GLOBE AND MAIL
PUBLISHED JUNE 20, 2019UPDATED JUNE 20, 2019
3 COMMENTS

A friend of mine moved to Colorado last summer. I recently asked him: “Jack, what’s life like in Colorado?” “Tim, there are a lot of people here, like me, who have moved from some other place. But you can always tell a native-born Coloradan.”

“How’s that?" I asked. “He has a $6,000 bicycle mounted to his $500 car,” Jack replied.

Jack is like many Canadians who have made a move to the United States for a great employment opportunity. Last week, I compared taxes and the cost of living in eight different Canadian and U.S. cities. The conclusion? Your financial life isn’t always better south of the border. And perhaps you’re like Kawhi Leonard, with millions of friends and neighbours trying to persuade you to stay here in Canada.

Nevertheless, if you’re making a move southward, there are a few tax manoeuvres to consider before you leave. Consider these four:

1. PLAN FOR THE DEPARTURE TAX

If you leave Canada and give up residency here for tax purposes, you’ll be deemed to have sold most assets when you leave, which could give rise to taxes on capital gains if those assets have appreciated in value. Certain assets are exempt from this “departure tax," including Canadian real estate, your registered plans (RRSP, TFSA, RESP, etc.), employee benefit or pension plans and stock option rights, and certain trust interests. You can file a special election to defer the tax owing when you leave (using Form T1244) but you may have to post security for the amount owing. You’ll also need to file forms T1161 (a listing of assets owned upon emigration) and T1243 (reflecting the deemed disposition) when you depart. Finally, when moving to the United States, it’s possible to avoid tax there on the same capital gain you realize on departure from Canada (avoiding double-taxation) by making a special election under Article XIII(7) of the Canada-U.S. tax treaty. You should visit a tax pro to talk about your departure because the rules are more complicated than quantum theory.

2. MINIMIZE TAX ON YOUR RRSP

Make sure you leave your registered retirement savings plan intact when you leave Canada. Collapsing your plan before you leave will only give rise to a big tax bill. Instead, make withdrawals from your RRSP after you take up residency in the United States. You'll pay a simple withholding tax to the Canada Revenue Agency (the tax is 25 per cent, but this can be reduced to 15 per cent under the Canada-U.S. tax treaty on periodic withdrawals, as opposed to lump-sum withdrawals from your plan). South of the border, you'll be able to withdraw, free of U.S. tax, the cost amount of your investments inside your RRSP (any gains on your RRSP assets will be taxable in the United States). So, here's an idea: Maximize your cost amount before moving to the U.S. by selling the investments in your RRSP and reinvesting the proceeds. The result? No tax in Canada since the assets are inside an RRSP, but greater tax-free withdrawals in the U.S. later.

3. DEAL WITH YOUR TFSA PROPERLY

If you have a tax-free savings account, you can continue to hold that TFSA once you're in the United States. The problem? While you won't face tax in Canada on income and growth inside the TFSA, you'll face tax in the U.S. on any income and realized capital gains each year since our tax treaty with the United States doesn't provide protection here. So, before you leave Canada, consider liquidating your TFSA investments and withdraw the proceeds. There will be no tax in Canada, but you'll increase your TFSA contribution room by the amount of the withdrawal, so that if you return to Canada later, you'll be able to recontribute that amount to a TFSA.

4. NAME A NEW SUBSCRIBER FOR AN RESP

What if you're a subscriber to a registered education savings plan? While you could continue to be the subscriber on an RESP after you move to the United States (the RESP would continue to be exempt from tax in Canada), the annual income earned in the RESP each year, plus any government grant or bond money received annually, would be taxable to you in the U.S., since an RESP is considered to be a foreign trust. That's a bad deal. When the children or grandchildren make withdrawals from the RESP later, they'll face tax in Canada at that time on the accumulated income, and grants, in the plan. The result? Double-taxation (taxed in your hands in the U.S., and again in their hands in Canada). So, consider naming a Canadian resident – perhaps a family member or friend – as the subscriber of the RESP before you leave.

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