

CANADIAN RESIDENTS LEAVING CANADA

Recent Jurisprudence and Lessons to be Learned

Introduction

The current administrative position of the Canada Revenue Agency (“CRA”) with respect to the residence of an individual may be found in Interpretation Bulletin IT-221R3 (Consolidated) “Determination of an Individual’s Residence Status”. It may also be inferred from the questions in CRA Form NR73 “Determination of Residency Status (Leaving Canada)”.

While the CRA’s administrative position is important, the final arbiter, when residence is in dispute, is the Court.

Several recent decisions of the Tax Court of Canada indicate increasing attempts by the CRA to claim that residents who have left Canada remain resident for tax purposes. I shall discuss several cases in reverse chronological order and derive lessons from each of them.

Gaudreau

A tax case decided on December 22, 2004, *Gaudreau v. The Queen* (so far unreported) provides some useful pointers to departing residents.

Mr. Gaudreau, a Canadian resident, accepted an offer from his Canadian employer to work on a contract in Egypt. He spent four months working on the contract in Canada and then left for Egypt in September 1996, returning to Canada in April 2000, at the end of the contract.

His employment agreement was expressed to be for an indefinite period, but the name of his employer was left blank. Under the signature of the employer’s representative was an indication that Mr. Gaudreau’s return date would be in approximately four years.

Mr. Gaudreau and his wife moved to Egypt. They kept their home and furniture in Canada and did not rent out their home. People in Canada looked after the house in their absence, paying bills, etc. Mrs. Gaudreau returned to Canada at least twice while living in Egypt and stayed in their house.

In Egypt, the couple rented a semi-furnished apartment on an annual lease. Mr. Gaudreau worked “almost seven days a week” and “did not really have a social life”. Their three adult children remained in Canada; one visited them in Egypt during their stay.

Mr. Gaudreau kept two bank accounts in Canada. His salary from his Canadian employer was deposited in one of them. His wife owned a car in Canada, stored at their house. In Canada, Mr. Gaudreau had a Registered Retirement Savings Plan (“RRSP”), credit cards and a safety deposit box.

He completed tax form NR73 for each year he was abroad and filed it with his Canadian tax return, even though there is no requirement to do so. On the form, he indicated that he would retire in Canada after completion of his assignment. In the first year that he filed the form, he stated that he would maintain his eligibility for (Canadian) provincial medical insurance cover. From information in the NR73 forms, it seems that he returned to Canada at least once, for 20/30 days, during his stay in Egypt.

The Court distinguished the Nicholson case (discussed below) in its judgement, based on the perceived intent of the taxpayer. In contrast to Mr. Gaudreau, Mr. Nicholson had no intention of returning to Canada at the end of his assignment.

The Court held that Mr. Gaudreau was a dual resident of Canada and Egypt during his assignment, and so turned to the provisions of the Canada/Egypt Income Tax Convention, Article 4(2), reproduced in Appendix A. The Court concluded that Mr. Gaudreau had a permanent home in both countries, and consequently turned to the next test. Under that test, he is deemed to have been a resident of the state with which his personal and economic relations (centre of vital interests) were closer during the period.

The Court looked to the Commentary to the OECD Model Convention Article 4, paragraph 15 and quoted from the condensed version, dated January 28, 2003. The quotation is reproduced in Appendix B.

The decision of the Tax Court was that the applicant’s centre of vital interests was closer to Canada than to Egypt during the years under appeal. The tie was broken in favour of Canada, so Mr. Gaudreau was subject to Canadian tax on his worldwide income during the years he was living in Egypt.

This case provides a useful checklist, based on the Court’s indication of where Mr. Gaudreau went wrong. I suggest below what he could have done to improve his chances of being held to be a non-resident of Canada during his stay in Egypt.

His first mistake (a major one) was to submit Form NR73 with his Canadian tax returns. This form may be submitted on a voluntary basis to the CRA by a Canadian taxpayer, to request the CRA to determine his residency status after he leaves Canada. My view is that a voluntary form should never be submitted to tax authorities anywhere, absent compelling circumstances. It certainly should not be attached to a tax return.

Now for my other suggestions:

- Mr. & Mrs. Gaudreau did not want to dispose of their home for valid personal reasons (a promise to Mrs. Gaudreau's parents to pass the house along to their children). They did not want to rent it either. They should have closed it up (e.g. boarded up the windows, turned off utilities as far as possible) and left it vacant. When they visited Canada, they should not have stayed there. Another possibility would have been to transfer title of their house to their children, retaining the right to live there for their joint lives – but subject to taking professional advice on any Canadian income tax complications. Disposal of the house would probably have resulted in a decision in favour of the taxpayer. Under Article 4(2) of the Canada/Egypt Income Tax Convention, if Mr. Gaudreau had a permanent home in Egypt and none in Canada, that should have concluded the matter.

Other action would have been helpful in determining where Mr. Gaudreau's centre of vital interests was located, for example:

- Mrs. Gaudreau should have disposed of her car when she left Canada.
- Mr. Gaudreau should have opened a bank account outside Canada (not necessarily in Egypt) to deposit his salary and any other income. He should have cancelled his Canadian credit cards and replaced them by credit cards from the non-Canadian bank.
- Mr. Gaudreau might have cancelled his Canadian driver's license, closed his safe deposit box (perhaps asking one of his adult children to take charge of his valuables).
- The Court made reference to the fact that Mr. Gaudreau did not ask for an Egyptian passport. It seems unlikely that he could have obtained one during a comparatively short stay in Egypt, but it would have been helpful had he applied, and been able to produce an official letter of refusal.
- A significant point was Mr. Gaudreau's continued provincial (Ontario) hospitalisation and medical insurance cover, which he specifically advised to the CRA on Form NR73. Cover is normally restricted to residents of the province. By continuing his cover, he is effectively suggesting that he considers himself still to be a resident of Ontario. In any event, why tell the CRA about it? Wait for them to ask!
- The Court noted that, when his employer closed the office in Egypt, Mr. Gaudreau "did not look for another job in that country...". His chances may have improved had he contacted other local companies and enquired about job availability.
- There was no need for him to have advised the CRA annually on Forms NR73 that he planned to retire in Canada after his assignment. Did he really make a final decision about his retirement before he left for Egypt? Had the question been raised by the CRA, he could probably have answered honestly: "It all depends". His Canadian home

is in Northern Ontario. For example, a subsequent health problem (either husband or wife) could have resulted in a final decision to retire somewhere warmer, outside Canada.

- Mr. & Mrs. Gaudreau should have made some effort to show that their lifestyle in Egypt indicated ties with that country. The Court made a particular point of this. Such activities as joining social clubs and a church and having friends in Egypt might have made a difference.

My conclusion is that the Court reached the right decision. Whether it would have been different had the taxpayer followed most or all of the suggestions above is a matter of opinion. My guess is that Mr. Gaudreau would have had a better chance of success had he taken, and acted upon, professional advice.

Snow

Judgement was brought down by the Tax Court on May 19, 2004 in the case of *Snow v. The Queen*,¹. The taxpayer lost her case.

Ms. Snow, a Canadian resident with dual Canadian/US citizenship, accepted an offer from Volunteers Service Overseas (“VSO”) for an assignment in Belize. After training courses in Canada and the UK, she left Canada in February 1998. A VSO posting is usually for two years, but her stay was extended to three years.

She testified that “she knew in ‘my head’ she would not return to Canada, since she wanted a different life”. Before leaving Canada, she closed a small business she was operating, surrendered her provincial health insurance benefits and resigned from her professional organisation and a local club.

Ms. Snow did not want to sell her townhouse in Vancouver, because the local real estate market was depressed, so she let her son and his family live in it rent free. Most of her belongings were stored in Vancouver. She said that she could not live in Belize and there was “no way” she would take her furniture to a developing country.

She considered Vancouver as the place where she could ‘reconnect’, and visited Vancouver while living in Belize, staying at her townhouse. She maintained her Canadian driver’s license and her RRSP, as well as her Canadian bank accounts (in which her Canadian pension cheques were deposited) and credit cards. She left her car in Vancouver and allowed her son to use it. She used the car when visiting Vancouver.

She gave evidence that she intended to accept a second posting overseas, but apparently was not successful in finding one.

The Court held that she was ordinarily resident in Canada during 1998 and 1999. A key part of the judgement was:

¹ [2004] 5 CTC 2085

“Mrs. Snow considered Vancouver as the place where she could ‘reconnect’ and where, if she needed a place to stay, she could stay. Mrs. Snow sojourned in Belize, that is, her stay in Belize was temporary. Vancouver was her home; ...”

The Court made reference to the fact that all her banking and other financial interests were in Canada, and that her mail continued to be sent to Vancouver. She “...had no intention to reside on any permanent basis in Belize”.

Ms. Snow may have had a better chance of success had she sold her townhouse, closed her Canadian bank accounts and cancelled her credit cards, but even then, in my view, her chances would be slim, since her evidence implied that she looked to Vancouver as her “home”.

There is no double tax treaty between Canada and Belize, so dual residence under a tax treaty was not an issue.

What can we learn from this case which, I suggest, was correctly decided?

- Sell your Canadian residence if you claim non-residency. It is an open point whether it would have made any difference had she sold her townhouse to her son, and had stayed at a hotel when visiting Canada.
- Close your Canadian bank accounts and cancel Canadian credit cards.
- Dispose of your car before leaving Canada and rent a car when visiting.
- Show an intention either to remain in the foreign country for an extended period, or at least to remain out of Canada indefinitely. It was clearly not good enough for Ms. Snow just to know “in my head” that she would not return to Canada.

Revah

The taxpayer in this case, *Revah v. The Queen*,² was successful in his claim that he became a non-resident of Canada when he moved to the United States in September 1992. The CRA had assessed Mr. Revah for 1993 and 1994 as a resident of Canada. Judgement was handed down on May 17, 2004.

Mr. Revah sold his Canadian residence in September 1992. He lived in a leased apartment in Florida with his daughter for six months, while his Florida house was completed.

² [2004] 5 CTC 2067

Before leaving Canada, he sold his car, cancelled his Canadian driver's license, his provincial health insurance card and his Canadian credit cards. In the US, he leased cars, obtained a Florida driver's license, took out US health insurance, and obtained US credit cards.

Mr. Revah kept two Canadian bank accounts, used to receive his Canadian government pension cheques and payments from his RRSP. After leaving Canada, he made charitable contributions to Canadian organisations.

He obtained a US three year temporary work permit in September 1992 and applied for a US "green card" in the same month. He received it in January 1995 and became a US citizen in 2003, retaining his Canadian citizenship.

He visited his family in Canada "maybe once a year".

He filed Canadian personal income tax returns for 1993 and 1994, reporting only his Canadian source income. These returns contained confusing, and apparently erroneous, information about his address and his province of residence. The reasons for the errors were explained to the Court, who described the situation as "... sloppy reporting on behalf of the tax preparer", and said that his accountant's explanations for the errors were "not unreasonable".

Copies of Mr. Revah's US personal tax returns (1040K) filed for 1993 and 1994 were submitted to the Court. These returns included only his US source income, which the Court found to be disturbing, but noted that this "... is a matter for the Internal Revenue Service and not for me or the CRA".

The Court allowed Mr. Revah's appeal with costs, which was, in my view, the correct decision. The following quotation from the judgement is of particular interest:

"The fact that the appellant had several links with Canada did not make the appellant a Canadian resident indefinitely. The links that Mr. Revah had with the United States were even more substantial than those he had with Canada. He usually lived in the United States, which is where most of his property was located. In 1992, the appellant intended to leave Canada permanently and he actually left the country. The appellant was not therefore resident in Canada during the 1993 and 1994 taxation years."

Counsel for the appellant argued that, if Mr. Revah was found to have been a resident of both Canada and the United States, the tie-breaker rules in Article 4 of the Canada/US tax Convention made Mr. Revah a US resident during the years in dispute. The Court mentioned this argument, making it clear that Mr. Revah was judged to be a US resident and not a Canadian resident during the years under appeal. Since there was no dual residence, it was unnecessary to refer to the Canada/US Tax Convention. Article IV(2) of that Convention is very similar to Article 4(2) of the Canada/Egypt tax treaty, reproduced in Appendix A.

Mr. Revah did almost everything right and won his appeal accordingly. Minor errors in his Canadian tax returns could have been a problem, but the explanations were accepted by the Court.

Nicholson

This case, *Nicholson v. The Queen*,³ was won by the taxpayer. The Court handed down its decision on November 25, 2003.

The facts are a little complicated.

Mr. Nicholson, a Canadian resident, was working for a US company in Canada. In August 1994, he was asked to move to the UK to take charge of the US company's European business operations. He accepted, and moved to the UK in January 1995, with a 36-month UK work permit. He lived in the UK in rented accommodation, with a car provided by his employer. He opened a bank account in the UK. He did not apply for UK residence status, but did apply for an "insurance number". It was understood that his next move, after three years in the UK, would be to Chicago. There would have been no position available in Canada once his three year term in Europe expired.

His employer continued his Canadian benefits while he was in the UK, including Canada Pension Plan contributions and medical plans, which covered his family.

In January 1996, he was told that his US employer company had been sold to a UK competitor. His job changed to integrating the European business with the business of the purchaser. He relocated to the north of England, where the acquiring company was headquartered.

Mr. Nicholson realised that the European business would disappear, and the acquiring company offered him a position based in Canada. He left the UK at the end of August 1996, having been resident in the UK for only about 20 months. He had visited Canada once while living in the UK, at Christmas 1995.

He was reassessed by the CRA, on the basis that he remained a Canadian resident while living in the UK. He appealed, claiming to have been a non-resident of Canada for that period.

Mr. Nicholson was separated from his wife, who had custody of their two children. Before moving to the UK, he lived in a rental apartment in Canada, while his wife and children lived in the matrimonial home. He was awarded a \$30,000 equalisation payment on separation in 1993, and kept joint title to the home until 2001 as security for the payment.

³ [2004] 2 CTC 2310

He maintained two bank accounts in Canada, and his explanation for so doing was accepted by the Court. He collapsed his RRSP in 1995. He continued to participate in the Ontario Health Insurance Plan while living in the UK.

Mr. Nicholson had what he described as a “girlfriend” resident in Canada, who visited him “quite regularly” in the UK. They lived together as husband and wife in the UK, and were married in 1999. Her child attended school in the UK.

The Court held that Mr. Nicholson was a non-resident of Canada while he was living in the UK. The Court mentioned several factors which were important in arriving at their decision:

- The Court was satisfied that, when Mr. Nicholson left Canada in January 1995, he had no intention to return, except for visits to his family.
- He gave credible reasons for maintaining two bank accounts in Canada, for remaining in the provincial health program and for his continued part ownership of the matrimonial home.
- The Court indicated that the existence of family ties in Canada did not affect his intent to reside outside Canada.
- Mr. Nicholson’s presence in the UK was not “casual and uncertain”. His “mode of life was in the United Kingdom during the period in issue”.

There was no reference by the Court to the Income Tax Convention between Canada and the United Kingdom. Article 4(2) of that Convention is quite similar to Article 4(2) of the Canada/Egypt Income Tax Convention reproduced in Appendix A, referred to in the Gaudreau case, above.

Presumably the Court decided that, since Mr. Nicholson was not a dual resident, reference to the Convention was not necessary. He was deemed by the Court to be a resident of the UK, and not a resident of Canada. Had he been deemed a dual resident, a decision in his favour may have resulted in any event, since he had a permanent home (rented) available to him in the UK, while the house in Canada was occupied by his (separated) spouse and children, so perhaps it was not available to him.

What can we learn from this decision? I suggest that there are three key points:

- Intent when leaving Canada is most important. The individual who states that he plans to return to Canada at the end of an overseas assignment runs a serious risk of being considered to remain a Canadian resident for tax purposes. The future is always clouded in doubt, and circumstances change. The departing resident should keep an open mind as to his or her future residence, and avoid categorical statements concerning his or her future. However, action which clearly demonstrates an intent to

return (such as keeping a Canadian residence, as did Mr. Gaudreau and Ms. Snow) may create a presumption that the individual has made a temporary move.

- Behaviour of the individual while in the foreign country is another important factor. Mr. Nicholson apparently settled into his life in the UK, while Mr. Gaudreau did not do so while living in Egypt. The Court made much of this fact, which presumably arose from the evidence given by Mr. Nicholson.
- Not cutting certain ties with Canada, e.g. maintaining Canadian medical insurance and bank accounts, while not advisable, may be acceptable if the Court deems the reasons for so doing to be justifiable.

Conclusion

When a Canadian resident moves to another country and claims to be a non-resident of Canada thereafter, the key points are:

- The CRA are looking very carefully at departing Canadian residents, as evidenced by the number of court proceedings in recent years, and by the experience of many international tax practitioners.
- If the reason for the move is to work in a foreign country, if the assignment is for a fixed term and the taxpayer plans to return to Canada when it terminates, he or she will probably not be successful in claiming non-residency. Intent, when leaving Canada is the key.
- A permanent move from Canada must be accompanied by action to cut most or all Canadian ties. Disposing of the taxpayer's Canadian residence appears to be important evidence of intent. To the extent that ties remain, there should be good reasons to present to the Court.
- If the move is to a country with which Canada has a comprehensive income tax treaty, this must be taken into account in planning the move. However, the tax treaty will not be invoked unless there is dual residence. If residence in the foreign country is not established, or if evidence confirms that the taxpayer was not a Canadian resident (as in Mr. Nicholson's case), there will be no reference to a tax treaty.

Canada/Egypt Income Tax Convention
Article 4(2)

2. Where by reason of the provisions of paragraph 1 an individual is a resident of both Contracting States, then his status shall be determined as follows:

- (a) he shall be deemed to be a resident of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident of the State with which his personal and economic relations are closer (centre of vital interests);
- (b) if the State in which he has his centre of vital interests cannot be determined, or if he has not a permanent home available to him in either State, he shall be deemed to be a resident of the State in which he has an habitual abode;
- (c) if he has an habitual abode in both States or in neither of them, he shall be deemed to be a resident of the State of which he is a national;
- (d) if he is a national of both States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.

OECD Model Convention
Commentary to Article 4 – Paragraph 15
(Quoted by the Court)

15. If the individual has a permanent home in both Contracting States, it is necessary to look at the facts in order to ascertain with which of the two States his personal and economic relations are closer. Thus, regard will be had to his family and social relations, his occupations, his political, cultural or other activities, his place of business, the place from which he administers his property, etc. The circumstances must be examined as a whole, but it is nevertheless obvious that considerations based on the personal acts of the individual must receive special attention. If a person who has a home in one State sets up a second in the other State while retaining the first, the fact that he retains the first in the environment where he has always lived, where he has worked, and where he has his family and possessions, can, together with other elements, go to demonstrate that he has retained his centre of vital interests in the first State.