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CESTNICK

TAX MATTERS

Thinking of leaving Canada? Deal with your RRSP properly

Yesterday I took my youngest son, Michael, who will be turning five in one week, for a walk along our street. Our neighbour Lloyd was also out for a walk.

"I'm going to be five!" Michael exclaimed as we approached Lloyd. "Five years old," Lloyd replied. "Imagine that. You're not even as tall as my umbrella!" "How old is your umbrella?" Michael asked.

As we were chatting with Lloyd about birthdays and umbrellas, he shared with me that he's moving to the sunny south – permanently. I'm going to miss Lloyd. He's lived on our street for more years than I know – certainly longer than we've lived here. As we talked, I shared with him some facts about his registered retirement savings plan that should save him thousands in tax. Let me share the idea with you.

THREE STEPS

If you're tired of the long winters and are thinking of moving to the United States, be sure to leave your RRSP intact when you go. You see, you're going to be better off by making RRSP withdrawals after you've given up Canadian residency, and not before. But there are three steps you should consider.

Step 1. Leave the RRSP intact. If you were to collapse your RRSP before leaving Canada, you'd face a significant tax hit because that withdrawal would be fully taxable in the year of your withdrawals. Lloyd and his wife, Margaret, are going to avoid this by leaving their RRSPs intact until they have given up residency.

If you wait until you're a resident of the United States (or any country for that matter), the only tax you'll pay to the Canada Revenue Agency will be a 25-per-cent withholding tax on any withdrawals from your RRSP. Further, the 25-per-cent rate will generally be reduced to just 15 per cent on periodic withdrawals, as opposed to lump-sum withdrawals from your plan, provided Canada has a tax treaty with your new country of residence.

Step 2: Step-up the cost base. If you've taken up residency in the United States, any withdrawals from your RRSP will be taxed by the U.S. (in addition to the Canadian withholding tax), but Uncle Sam won't tax the full amount of your withdrawals. Rather, you'll be entitled to withdraw from your plan, tax-free, the cost base of your RRSP investments as calculated on the day you took up residency in the U.S. So, if you can maximize that cost base, you'll be entitled to greater tax-free withdrawals in the United States. Lloyd and Margaret are going to accomplish this by selling and repurchasing, before they leave Canada, their RRSP assets that have appreciated in value.

You see, if you have investments in your RRSP worth \$300,000 but you only paid \$100,000 for them, your cost base is \$100,000. If you sell those investments and reinvest the proceeds, your new cost base will be \$300,000. This is a step-up in your cost base. You won't face a tax bill in Canada on the sales since it all takes place inside your RRSP where gains are sheltered.

Step 3: Give up residency properly. Lloyd and Margaret are going to take great pains to make sure they give up Canadian residency properly. If the CRA considers you to still be a resident of Canada, even after you've left the country, you'll face tax on your RRSP withdrawals at full Canadian tax rates, not the lower withholding rates.

Be sure to follow all three steps outlined here. Why? Because in this game, it's not three strikes and you're out. If you swing and miss on even one of these steps, you could cost yourself significant tax dollars.

At a glance

Although no single factor will determine whether you've truly given up Canadian residency for tax purposes, the tax collector will consider a number of things, and in particular:

- The permanence and purpose of your stay abroad (if you return to Canada to live, the Canada Revenue Agency may presume that you were a resident of Canada the whole time unless you can demonstrate otherwise).
- Your residential ties within Canada (your primary ties include your home, spouse and dependents, personal property and social ties).

- Your residential ties elsewhere (the courts have said that you must be a resident somewhere, and you can be resident in more than one country at the same time).
- The regularity and length of your visits to Canada after you've left.

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