Global Tax Alert
News from Americas Tax Center

Canadian nonresident trust rules require notice of relieving elections by 31 March or 25 June 2014

Executive summary

Amendments to Canada’s nonresident trust rules, which had been in proposal form for many years, were finally enacted on 26 June 2013, generally with application to taxation years that end after 2006. A nonresident trust to which these rules apply will be deemed to be resident in Canada for certain purposes and taxed on its worldwide income and gains.

Certain relieving elections are available, the filing deadlines for which are either 31 March 2014 or 25 June 2014.

Detailed discussion

Background

Under the old rules, both a Canadian-resident beneficiary and a Canadian-resident contributor to the trust were required. The new rules, however, will apply where there is a Canadian-resident contributor of property to a nonresident trust even if there are no Canadian-resident beneficiaries. The definition of “contributor” is very broad and the rules expand the contribution concept to include indirect and third-party transfers in certain circumstances.

Although a variety of exceptions are provided, the rules may apply in many situations where there are both nonresident and Canadian-resident beneficiaries. For example, global foreign pension and employee benefit plans may be established as trusts in a foreign jurisdiction and may include employees in several countries. The legislative exceptions for these types of plans do not provide exemption for all plans.
**Election to limit Canadian tax to resident portion**

In order to reduce the impact of these rules, and avoid tax on worldwide income/gains, the trust may elect to be taxed only on the income and capital gains generated from the property contributed by Canadian-resident contributors. This election effectively permits the trust to be split into two separate trusts (for Canadian tax purposes) − the “electing trust” in respect of the resident portion (contributed by Canadian contributors) and the “nonresident portion trust.” Only the electing trust will be subject to Canadian tax, although returns must be filed for both trusts. If this election is not made, the trust will be subject to tax on its worldwide income/gains. Late-filed elections are not permitted and so it is critical to meet the filing deadline.

The election is made by the trustees and must be filed with the trust’s tax return for the first year in which the nonresident trust is deemed to be a resident of Canada. For trusts that became initially subject to the nonresident trust rules in any of the years between 2007 and 2012, an extension is provided and the election must be filed no later than 25 June 2014. For trusts that initially became subject to the nonresident trust rules in 2013, if the trust’s year end is 31 December, the election filing deadline is 31 March 2014. There is no prescribed form and the election is made by letter attached to the tax return.

**Election for Canadian contributor to pay the tax**

Another election is available that allows the tax to be paid by the Canadian contributor rather than the electing foreign trust. Where this election is made, the resident contributor will be attributed its share of the trust’s income. The tax rate payable by the contributor may be lower than that of the trust (typically taxed at the top marginal tax rate). This election is available for taxation years ending after 4 March 2010 and must be filed by the contributor by its tax filing due date for the first taxation year for which the contributor wishes the election to be effective. If the filing due date would have been before 24 October 2013, the filing due date is extended to 25 June 2014.

**Election to apply new rules to prior years**

The new rules apply to nonresident trusts starting with taxation years that end after 2006. An election is also available to apply the new rules to taxation years between 2000 and 2006. This election must be filed by 31 March 2014.

**What you should do**

If you have a global employee benefit or pension arrangement that is considered a trust, determine if there are any beneficiaries who are Canadian residents and in respect of whom a contribution of any sort could have been made by or on behalf of the Canadian employer.

Review all the available exemptions to see if any applies to exempt the trust from the new rules.

Consider filing the election to split the trust into the resident and nonresident portions and determine the appropriate election filing date.

Consider whether a Canadian entity should make the “electing contributor” election so that the tax otherwise payable by the trust can be paid at lower rates.

Consider whether it would be beneficial to have the new rules apply to taxation years prior to 2007.
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