

Foreign Beneficiaries

Foreign beneficiaries: It's complicated

By **Margaret O'Sullivan**



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(April 29, 2019, 8:56 AM EDT) -- With increased mobility of people and their assets, increasingly estates have a multijurisdictional dimension. A multitude of special considerations come into play which must be identified and dealt with if an estate has foreign beneficiaries or executors or other legal representatives which increase the complexity of the estate administration. This is the first of a four-part series of articles highlighting a number of them and is written from the perspective of Canadian and Ontario law.

Foreign beneficiaries

Various tax and non-tax related issues arise during the administration of an estate which has foreign beneficiaries, including:

- withholding tax on payments made to a foreign beneficiary;
- the characterization of distributions made to non-resident beneficiaries, including whether capital distributions can be made tax-free to a non-resident beneficiary or are subject to tax on capital gains;
- requirements to obtain a tax certificate from Canada Revenue Agency (CRA) prior to making distributions to a non-resident beneficiary;
- multiple taxation on death;
- foreign currency and exchange;
- transfers of interests in domestic corporations; and
- payment of a deceased beneficiary's share to a non-resident legal representative.

Withholding tax issues

Under Canadian tax legislation, income which is paid or payable to a non-resident beneficiary does not generally retain its character in the hands of the non-resident beneficiary and is subject to non-resident withholding tax.

The estate is liable to withhold the appropriate rate of tax of 25 per cent (unless reduced by treaty). This tax has to be received by CRA or by a Canadian financial institution on or before the 15th day of the month following the month during which the tax was withheld. The trustee must complete an NR4B Summary and Supplementary Slips reporting the income paid or credited to non-resident beneficiaries and remit the tax withheld. Withholding tax on interest income paid to non-residents was eliminated as of Jan. 1, 2008.

No rollover

Under Canadian tax rules, there is generally no rollover on a distribution of capital property by an estate to a non-resident beneficiary in satisfaction of all or any part of a capital interest. The estate will be deemed to have disposed of the property at proceeds equal to fair market value and the beneficiary acquires the property at that amount. The beneficiary is deemed to have disposed of the capital interest for proceeds equal to its cost amount.

A rollover will apply for a distribution of certain types of property including real property situated in

Canada, property of a business carried on in Canada through a permanent establishment and shares of a non-resident owned investment corporation. These types of property remain subject to Canadian taxation rules.

Section 116 certificate requirements

Section 116 of the *Income Tax Act* (Canada) (ITA) imposes an obligation to obtain a clearance certificate on a non-resident person who disposes of certain taxable Canadian property.

The obligation will apply to a non-resident with respect to a disposition of a capital interest in an estate that occurs because of a distribution of capital by the trust to the non-resident, but with the exception of a cash distribution, unless more than 50 per cent of the fair market value of the estate is derived from Canadian real property.

Under s. 116, the estate is considered a "purchaser" of taxable Canadian property — i.e., the capital interest in the estate — and the non-resident beneficiary is considered the vendor.

If a non-resident beneficiary does not obtain a clearance certificate, the estate must withhold and remit tax equal to 25 per cent of the deemed proceeds to CRA, as well as report the distribution to CRA within 10 days of making the distribution and within 30 days after the end of the month in which the distribution is made. Failure to do so could result in personal liability to the executors or other legal representatives for any unpaid tax. No withholding is necessary in certain situations where the vendor and purchaser are related and certain other provisions are met.

This is part one of a four-part series.

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