Docket: 2016-1017(IT)G

BETWEEN:

WILLIAM DAVIS,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on March 16, 2018, at Toronto, Ontario

Before: The Honourable Mr. Justice Randall S. Bocock

Appearances:

Counsel for the Appellant:	Al Tharani
Counsel for the Respondent:	Sebastien Budd

JUDGMENT

IN ACCORDANCE with the Reasons for Judgment attached, the appeal in respect of the 2013 taxation year is allowed on the basis that the Appellant was not a resident of Canada at the material time, namely May 6, 2013, by virtue of the application of subsection 2(b) of Article IV of the Convention between Canada and the United States of America with Respect to Taxes on Income and on capital, being schedule 1 to the *Canada-United States Tax Convention Act*, 1984, S.C. 1984 c. 20, as amended.

The matter is referred back to the Minister of National Revenue for reconsideration and reassessment.

Costs are awarded to the Appellant in accordance with the Tariff subject to either party's right to make submissions otherwise within 30 days hereof.

Signed at Ottawa, Canada, this 14th day of June 2018.

"R.S. Bocock"

Bocock J.

Citation: 2018 TCC 110
Date: 20180614
Docket: 2016-1017(IT)G

BETWEEN:

WILLIAM DAVIS,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Bocock J.

I. Introduction

[1] Generally, residents of a country pay income tax to and receive benefits from the treasury of that country. The issue of residency is central in this appeal. At the time of a large withdrawal from a U.S. retirement savings account the Appellant, Mr. Davis, says he was a resident of the United States of America (the "U.S.") and not of Canada. The Minister of National Revenue (the "Minister") says that at the material time Mr. Davis was a newly returned resident of Canada and subject to pay income tax in this country on the retirement account proceeds. This is the root of the dispute in this appeal.

II. Undisputed Facts

[2] At the outset of the hearing, the parties handed up a partial agreed statement of facts. Certain other facts went unchallenged during testimony. Mr. Davis was employed in the state of Massachusetts until December 2012. To this day, he still owns a house there, but has not maintained it since July 2013. Presently, Mr. Davis holds a U.S. Permanent Resident Card ("Green Card") which expires in 2020.

[3] From and after October 31, 2009, Mr. Davis also owned a house near Yarmouth, Nova Scotia jointly with his girlfriend.

[4] Further, both parties agree that Mr. Davis was resident in the U.S. at least until April 9, 2013. However, Mr. Davis submits such residency was lengthier: until at least May 9, 2013 and possibly October of that same year.

[5] North of the border, Mr. Davis received a Nova Scotia health card on June 1, 2013, retroactively effective to January 1, 2013. A Nova Scotia driver's license was issued on October 1, 2013.

[6] Sometime after April 9, 2013, Mr. Davis requested a withdrawal of $696,309.38 (USD) from his U.S. 401(k) retirement fund. In the U.S., Federal and state income taxes were withheld in the amounts of $139,261.88 (USD) and $36,556.24 (USD), respectively. After deduction of an owing unrelated loan, Mr. Davis received the sum of $495,325.03 (the "401(k) proceeds") sometime immediately following May 6, 2013 and before his subsequent exit from the U.S. on May 9.

[7] In his 2013 T1 tax return, Mr. Davis reported "net foreign business income" of $727,136.44 and claimed a $265,026.30 non-business income foreign tax credit. He also claimed "other deductions" of $338,831.18. There is no dispute the tax return, notwithstanding its candor in disclosure, was not correctly completed. Originally, the Minister denied these credits and deductions, but subsequently reassessed to allow foreign tax credits of $176,609.30, but maintained that the balance of the 401(k) proceeds received by Mr. Davis were subject to Canadian income tax. The Minister did so by asserting that Mr. Davis was a Canadian resident at the time of receipt, May 6, 2013 (the "receipt date"). The Minister did so in her confirmation after objection and by virtue of assumption in the reply which both assert Mr. Davis became a Canadian resident on April 9, 2013. Elementally, if Mr. Davis was not a resident of Canada on the receipt date, he need not have included the 401(k) proceeds in income. If he was, he must.

III. The Parties' Positions and Certain Observations

(a) The Appellant

[8] Mr. Davis takes alternative positions. First, he asserts that he was not a resident of Canada on the receipt date. Instead, he returned to Canada and became a resident no earlier than May 9, 2013, the date he re-entered and 3 days after receipt of the 401(k) proceeds.

[9] In the alternative, Mr. Davis submits that if he were a resident of Canada on the receipt date, he became a resident of Canada no earlier than April 9, 2013. Even so, on that date and until at least May 9, 2013, he also remained a resident of the U.S. and was, therefore, a resident of both countries. He asserts that he was fully taxed in the U.S. on the 401(k) receipts as a U.S. resident. In turn, Mr. Davis argues that reference to Article IV of the U.S. Canada Tax Treaty[1] (the "Treaty") tie-breaker rules renders him a resident of the U.S. and not of Canada on the receipt date. He asserts that the applicability of one of the following tie-breaker rules in the Treaty determine this: (i) centre of vital interests; or (ii) habitual abode.

(b) The Respondent

[10] In submissions after evidence, and after questioning for clarification from the bench, Respondent's counsel submitted that the Minister's basis for assessment is the reverse to the Appellant's. Firstly, Mr. Davis was a Canadian resident on the receipt date. Further, if he were also a U.S. resident, he received tax credits for the amount of the U.S. tax paid. Moreover, any needed reference to the tie breaker rules in Article IV of the Treaty makes Mr. Davis a resident of Canada because, upon the receipt date, both his centre of vital interests and habitual abode were in and/or had shifted to Canada.

(c) Other factual observations concerning Residency in the potentially Competing Countries:

(i) In the U.S.

[11] Mr. Davis moved to Massachusetts in 2003, ten years before his return to Canada. He worked for a large investment company as an IT systems engineer. On December 31, 2012, Mr. Davis left that job because his department was closed and moved elsewhere in the U.S. He never worked again in the U.S. Over the course of his employment, he saved and invested in his 401(k) retirement account.

[12] His banking was conducted in the U.S. He maintained health insurance coverage in the U.S. until June 30, 2013. During that period Mr. Davis attempted to sell his house in the U.S. At one time, Mr. Davis owned two properties in the U.S.: one in Marlborough and the other in Hudson, both in the State of Massachusetts. The Marlborough property was auctioned for sale in December 2012, although it was unclear when that transaction was completed with finality.

[1] Schedule 1 to the *Canada-United States Tax Convention Act*, 1984, S.C. 1984 c. 20, as amended.

[13] Mr. Davis retains the Hudson property to this day. He lived there until he returned to Canada in May, 2013. His U.S. address for U.S. dealings remains at the Hudson address. Mr. Davis received his 401(k) proceeds by courier delivered to his home in Hudson sometime after May 6, 2013 and before May 9, 2013. There were deductions withheld for U.S. federal tax, state tax and outstanding loans. Mr. Davis asserts that, after receiving the 401(k) proceeds, he commenced his final departure from the U.S., culminating with his final re-entry into Canada on May 9, 2013. Upon crossing the border, he filed customs forms relating to transporting negotiable instruments in excess of $10,000.00, as required. These forms were not adduced at the hearing.

(ii) In Canada

[14] Mr. Davis bought the rural property near Yarmouth, Nova Scotia in October 2009. Mr. Davis' girlfriend funded the down payment. Between that time and Mr. Davis' return in May, 2013, Mr. Davis visited the property frequently. He lives there today, albeit alone for the past several years. During the relevant period, it was uncontested evidence that Mr. Davis and his girlfriend were in a platonic relationship.

[15] From 2009 to 2013, Mr. Davis brought various goods from the Hudson property to Yarmouth. He believably testified that he always intended to return to Canada. It was simply a question of what "tipped the scales" for his final return. The early morning of April 9, 2013 was a particularly important crossing. At 4:00 am at the border crossing, Mr. Davis completed a customs declaration form relating to a "personal effects accounting document" which indicated "I returned to Canada to resume residence on April 9, 2013". The form also indicates that other goods would follow.

[16] When Mr. Davis filed his 2013 tax return, he did so using the software package "Turbo Tax". He also indicated on that return that his commencement date for residency in Canada was April 9, 2013. That same date was used to indicate "the date you became or ceased to be resident of Canada for income tax purposes in 2013, enter the date". Mr. Davis was not familiar with tax laws or accountancy. He followed the software program, knew he should disclose his income and completed the tax return as best he could. He also candidly disclosed receipt of his 401(k) proceeds, but also claimed the off-setting entry described above: other deductions. If he was not a resident of Canada on the receipt date, he need not have done the first. In any circumstance, the second was an error.

IV. The Law

(a) Residency in Canada Generally

[17] An individual taxpayer will be resident in Canada if she or he is either deemed resident by section 250 of the *Income Tax Act* (the "*Act*") to be so, or is ordinarily resident in Canada. The "counter deeming" provisions of subsection 250(5) are potentially applicable to the outcome of this appeal and provide as follows:

> Person deemed resident
>
> 250(1) For the purposes of this Act, a person shall, subject to subsection 250(2), be deemed to have been resident in Canada throughout a taxation year if the person […]
>
> Deemed non-resident
>
> 250(5) Notwithstanding any other provision of this Act […] a person is deemed not to be resident in Canada at a time if, at that time, the person would, but for this subsection and any tax treaty, be resident in Canada for the purposes of this Act but is, under a tax treaty with another country, resident in the other country and not resident in Canada.

[18] As such, it is relevant as to whether Mr. Davis in the first instance was ordinarily resident in Canada. There is no question and counsel agree that for the purposes of income received after his return, he was a Canadian resident. The operative issue is when that occurred. To that point, a taxpayer is ordinarily resident in the place where, in the settled routine of life, the taxpayer regularly, normally, or customarily lives. Relevant factors in determining a taxpayer's residence are well established in *R v Reeder*[2].

(b) Applicability of the Treaty and Tie-breaker Rules

[19] Certain rules exist as tie-breakers within the *Canada-US Tax Treaty* concerning residency[3]. The tie-breaker rules for residence are expressed in Article IV(2):

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[2] *R v Reeder* , 75 DTC 5160 (FCTD).

[3] *Convention Between Canada and the United States of America with Respect to Taxes on Income and on Capital*, being schedule I to *Canada-United States Tax Convention Act, 1984*, S.C. 1984 c. 20 (as amended) [*Canada-US Treaty*].

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

V. Analysis and Findings

[20] For the *US-Canada Treaty* residence tie-breaker rules to be engaged, Mr. Davis must have paid tax in the U.S. based upon residency. To that end, at trial, a statement of deductions was produced to indicate substantial taxes were deducted at the source from the 401(k) proceeds by federal and state authorities in the U.S. This is similar to how such taxes would have been initially collected in Canada if the disbursement had occurred here and Mr. Davis had been a resident. Mr. Davis also testified to deduction of taxes in the U.S. from the 401(k) proceeds. Moreover, at audit, the Minister allowed Mr. Davis foreign tax credits for such amounts paid, having concluded he was exclusively a resident of Canada as of April 9, 2013.

[21] What conclusion can be drawn concerning Mr. Davis' basis for taxation in both countries? The Respondent led no contrary evidence to suggest Mr. Davis was taxed as anything other than a resident of the U.S. Mr. Davis certainly asserted that he was. As stated, his tax deduction slip concerning his 401(k) proceeds patently suggest just such a case. On the Canadian side, there is no dispute that the Minister seeks to tax Mr. Davis as a resident in Canada. A protracted discussion of onus is not required. The Court is satisfied Mr. Davis has established he paid tax as a U.S.

resident in 2013 on the 401(k) proceeds. He has discharged his burden[4] related to that assertion. No rebuttal evidence was proffered. The Respondent's ultimate submissions are also based upon such a situation of taxation as a resident in both countries. Therefore, the Court concludes, as a matter of unrefuted fact, that Mr. Davis paid income tax, *qua* resident of the U.S. rather than on the basis non-resident withholdings taxes.

(a) Was Mr. Davis a resident of both Canada and the U.S. to engage the Treaty?

[22] Based upon the factual evidence before the Court, Mr. Davis was otherwise a resident of both the U.S. and Canada. Co-existing facts confirm the Court's view that he had taken up residency in Canada on April 9, 2013, but had not irrevocably departed from the U.S. at the receipt date, and, on balance, not before May 9, 2013. Dual or competing residency is the very thing the Treaty anticipates and seeks to resolve through its tie-breaker rules. The findings supporting this double residency are:

(i) his two "lives" were co-existent during the material period, albeit one in start-up and the other in wind-up mode;

(ii) the issue of a spouse was not relevant to either state;

(iii) a fiscal presence exists in both states and requires further analysis;

(iv) Mr. Davis had a permanent home available in both countries during the material period.

(b) Treaty Application

[23] Where dual residency exists and forms the basis of taxation, the tie-breaker rules are engaged to resolve the impasse. Ultimately assuming Mr. Davis was a dual treaty resident, each party argued that the tie-breaker rules resolve the impasse in their respective favour. Since the Treaty is engaged, the Court moves to consider its provisions. The first prong of the test is whether a permanent home is available

[4] *Hickman Motors* v *R.* [1997] 2 SCR 336 at paragraph 92. And section 10 of the Partial Agreed Statement of Facts states: "the entirely of the Appellant's retirement funds were taxable in the USA."

in both countries. Factually, as stated, it was the situation factually within this appeal and was not disputed.

(i) First Tier Tie-breaker beyond dual Permanent home - - centre of vital interests

[24] In the second prong of the first tier rule, the question of centre of vital interests relates to a close examination of the taxpayer's personal and economic relations with each country in question. This is done to determine with which country an economic nexus is closer[5].

[25] In the U.S., Mr. Davis had certain connections of a personal and economic nature. The largest value of Mr. Davis' collected assets remained in the U.S. until May 9, 2013. Mr. Davis continued to own a house and have bank accounts in the U.S. Mr. Davis' family lived in Canada, but in Alberta just as far from Nova Scotia as such province is from Massachusetts. His job had ended, but the residual assets derived from employment remained stateside. Lastly, his effective health insurance and driver's licence remained at least during the material time in the U.S.

[26] In Canada, Mr. Davis did not maintain a conjugal relationship, gain employment or return to his previous home province and family. He did not receive a health card until June 30, 2013 or a driver's licence until October of that year.

[27] Similarly, Mr. Davis had clearly made up his mind to leave the U.S. as a resident; the question remains, when did he? Certainly as of the receipt date, his centre of vital interest is not measurably resolvable, but leans slightly towards the U.S. Therefore, the Court will pursue the next tier within the tie-breaker rules: the country of habitual abode.

(ii) Second Tier Tie-breaker - - Habitual abode

[28] To determine habitual abode, one must identify the period for measure. The parties agree the critical income date is the receipt date. Residency for this dual treaty resident on that date is the determinative date. To reiterate, this is May 6, 2013. Before April 9, 2013, Mr. Davis was not a resident of Canada. After May 9, 2013, he was not a resident of the U.S.; the period in issue is the period surrounding May 6, 2013.

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[5] *Trieste* v *HMQ*, 2012 TCC 91 at paragraph 23.

[29] Justice Campbell in *Lingle*[6] provided the following synopsis:

> [19] The Appellant argues that even if the conclusion of Bell J. respecting the Commentary in *Allchin* is wrong and the Commentary is relevant, it contains nothing that would define an habitual abode as the place where the taxpayer "stays more frequently". The Commentary on Article IV(2) does not contain a test requiring a comparison between the frequency of stays in Canada and the United States.
>
> [20] The relevant paragraphs, 16 to 20 from the Commentary on Article IV(2) of the OECD Model, provide:
>
> > 16. Subparagraph *b*) establishes a secondary criterion for two quite distinct and different situations:
> >
> > *a)* the case where the individual has a permanent home available to him in both Contracting States and it is not possible to determine in which one he has his centre of vital interests;
> > *b)* the case where the individual has a permanent home available to him in neither Contracting State.
> >
> > Preference is given to the Contracting State where the individual has an habitual abode.
> >
> > 17. In the first situation, the case where the individual has a permanent home available to him in both States, the fact of having an habitual abode in one State rather than in the other appears therefore as the circumstance which, in case of doubt as to where the individual has his centre of vital interests, tips the balance towards the State where he stays more frequently. For this purpose regard must be had to stays made by the individual not only at the permanent home in the State in question but also at any other place in the same State.
>
> […]
>
> > 19. In stipulating that in the two situations which it contemplates preference is given to the Contracting State where the individual has an habitual abode, subparagraph *b)* does not specify over what length of time the comparison must be made. The comparison must cover a sufficient length of time for it to be possible to determine whether the residence in each of the two States is habitual and to determine also the intervals at which the stays take place.

[6] *Lingle* v *The Queen*, 2009 TCC 435, at paragraphs 19 and 20.

[30] *Lingle* was referenced by Respondent's counsel. The Court questioned counsel extensively on the reference. Some consensus surrounded the view that frequency of stays would quantitatively establish the habitual abode. The Federal Court of Appeal, in referencing a different paragraph in *Lingle*, upheld the decision of Justice Campbell and refined and expanded the test as follows[7]:

> [12] To the extent that the sentence *per se* could be found to be ambiguous, it is, however, clear from a reading of the reasons as a whole and paragraph 30 that, at the point where the sentence occurs, the judge had already concluded that the appellant did not have an "habitual abode" in the United States "because he did not regularly, customarily or normally live in the United States": see paragraph 30.
>
> [13] The appellant argued that the proper test to be applied for determining where a taxpayer has his "habitual abode" is to look at where he or she "is habitually present". He relies upon a tentative conclusion of Dr. J.F. Avery Jones who, … , is currently a judge on the United Kingdom First Tier Tax Tribunal.
>
> [14] The Tax Court found that the appellant "regularly, normally and customarily lived in Canada": see paragraph 30 of the reasons for judgment. By the appellant's proposed test, the Tax Court found that he was habitually present in Canada, but not in the United States.

[31] On balance, given all the facts as stated throughout and upon applying these quantitative and qualitative measures, the Court determines that Mr. Davis' habitual abode was in the U.S. on or before May 9, 2013. He regularly, customarily or normally lived there prior to and immediately after the receipt date. This may not have been true after May 9, 2013, but the critical date framing the material time was the receipt date, May 6, 2013, three days before. Prior to that time, the contrary completion in boxes on forms and returns of the date April 9, 2013 merely reinforces taxpayer misunderstanding and, at most, establishes dual residency begging the very question for this Court. Mr. Davis' residency in Canada before May 9, 2013 was prepatory to disengaging from the U.S. and permanently ceasing to be a resident after May 9, 2013. Before May 9, 2013, Mr. Davis, based upon the factual circumstances before the Court, habitually lived in the U.S. based upon frequently, duration and regularity[8].

VI. Conclusion and Costs

[7] *Lingle* v *R.*, 2010 FCA 152 at paragraphs 12, 13 and 14.
[8] *Lingle*, 210 FCA at paragraph 6.

[32] In this factually unique appeal, the Court determines that Mr. Davis's habitual abode was in the U.S. on May 6, 2013, the date he received the 401(k) proceeds and was taxed in the U.S as a resident. As a dual treaty resident, he was a resident of the U.S. and not Canada by virtue of the application of the tie-breaker rule in section 2(b) of Article IV of the Treaty. As such, the income from the 401(k) proceeds was not taxable in Canada under the *Act.*

[33] For these reasons the appeal is allowed. Mr. Davis shall have his costs in accordance with the Tariff subject to either party's right to make submissions otherwise within 30 days hereof.

Signed at Ottawa, Canada, this 14th day of June 2018.

"R.S. Bocock"

Bocock J.

CITATION:	2018 TCC 110
COURT FILE NO.:	2016-1017(IT)G
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