

# Tax Topics

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## CRA AUDIT SAYS IT HAS A JUSTICE OPINION CONFIRMING ITS POSITION: DO YOU HOLD OR FOLD?

—Jonathan Éthier and David H. Sohmer, *Spiegel Sohmer Inc.*, Montreal

In an article entitled “The Role of the Attorney General in Tax Litigation”,<sup>1</sup> Wilfrid Lefebvre stated that “the role of [Department of Justice (DOJ)] counsel is somewhat different than that of practitioners representing the interest of a private litigation. DOJ counsel have a duty, of course, vis-à-vis the court, but also vis-à-vis the community at large” and that “[. . .] distinctions can and should be drawn between the professional obligations of DOJ counsel and those imposed on a member of the private bar.” He argues that this distinction translates “at a minimum” into the application of certain guidelines.

DOJ counsel should always act in the interest of justice and the research of the truth.

If DOJ counsel is aware of facts or documentation that favours the position of the taxpayer (who may not have knowledge of or access to such information), he or she should produce it without hesitation.

A subset of the “interest of justice” rule is that DOJ counsel should seek to do all that he or she can to achieve a result that is fair and right.

DOJ counsel should assess the evidence at hand in terms of what he or she perceives would be a court’s reaction. CRA auditors are often not familiar with the rules of evidence, and it is therefore incumbent on DOJ counsel to ensure that assumed facts are not, in appropriate circumstances, based on an erroneous or incomplete understanding of the rules.<sup>2</sup>

While the guidelines are proposed in a civil litigation context, it is our contention that they should also apply in the context of the administrative dispute resolution process. In particular, they should apply in determining the role of DOJ counsel when a CRA auditor represents that his or her opinion has been confirmed by DOJ counsel. The position of the DOJ is that privilege effectively exempts counsel from complying with the guidelines in a non-litigation context. The guidelines should not compromise the entitlement of the CRA to seek and obtain legal advice without the apprehension of being prejudiced by subsequent disclosure of confidential communication. However, the disclosure of factors which imply that the contents of confidential communication may have been misrepresented is not the same as the disclosure of such communication. A CRA auditor declaring that Justice agrees should not be a declaration that he or she is no longer persuadable. As importantly, DOJ counsel should not permit a CRA auditor to use an opinion as a tactical weapon unless counsel is satisfied that both he or she as well as the CRA auditor are in compliance with the guidelines and their spirit.

<sup>1</sup> Wilfrid Lefebvre, “The Role of the Attorney General in Tax Litigation”, (2013) 61, *supp. Canadian Tax Journal*, 231-239.

<sup>2</sup> *Id.*

If DOJ counsel can be convinced that the guidelines are applicable during the administrative dispute resolution process, a taxpayer faced with a representation that DOJ counsel agrees with the auditor's position may consider taking the following steps:

- (1) Ask the CRA auditor what assumptions of fact support his or her position. The CRA expressly acknowledges that taxpayers are entitled to know the facts and assumptions on which assessments are based.<sup>3</sup>
- (2) Ask the DOJ counsel if the assumptions of fact disclosed to the taxpayer differ from the assumptions of fact contained in the auditor's request for an opinion and whether he or she has assessed the evidence of the assumed facts or merely assumed their veracity.
- (3) Ask the CRA auditor to provide a *List of Documents* equivalent to what Rule 81 of the *Tax Court of Canada Rules (General Procedure)*<sup>4</sup> would require to be filed and served if the taxpayer was appealing to the Tax Court of Canada.
- (4) Ask the DOJ counsel if the documents in the list were disclosed to her or him.
- (5) Ask the DOJ counsel if he or she is aware of facts or documentation that favours the position of the taxpayer which were not disclosed in the assumptions of fact or included in the *List of Documents*.
- (6) Ask the CRA auditor to paraphrase the DOJ counsel's opinion. CRA auditors are expressly permitted to do so in *Investigations Manual IM-01*.<sup>5</sup>
- (7) Ask the DOJ counsel if the paraphrased version misrepresents DOJ counsel's opinion.
- (8) Ask the DOJ counsel to consider whether the spirit of the guidelines suggest that he or she should disclose unfavourable case law to the taxpayer as is the duty to do so to the court.

[c]ounsel before the courts have a positive duty to make full disclosure of all the binding authorities relevant to a case, including all authorities on point whether they support or undermine the position being urged upon the court, even if opposing counsel has not cited such authority<sup>6</sup> [emphasis added]

It is also arguable that a representation that DOJ counsel agrees with the auditor's position constitutes an implied waiver of privilege. In the case of *Mann v. Carnell*,<sup>7</sup> the High Court of Australia appeared to have supported this argument.

At common law, a person who would otherwise be entitled to the benefit of legal professional privilege may waive the privilege. It has been observed that "waiver" is a vague term, used in many senses, and that it often requires further definition according to the context. Legal professional privilege exists to protect the confidentiality of communications between lawyer and client. It is the client who is entitled to the benefit of such confidentiality, and who may relinquish that entitlement. It is inconsistency between the conduct of the client and maintenance of the confidentiality which effects a waiver of the privilege. **Examples include disclosure by a client of the client's version of a communication with a lawyer, which entitles the lawyer to give his or her account of the communication** or the institution of proceedings for professional negligence against a lawyer, in which the lawyer's evidence as to advice given to the client will be received<sup>8</sup> [emphasis added]

A representation that DOJ counsel agrees with the audit is effectively the auditor's version of his or her communication with counsel, even if the auditor refuses to paraphrase counsel's opinion. However, whether or not privilege has been waived is a question that may only be answered by the courts. Appealing to a DOJ counsel's sense of duty by raising the guidelines may be the preferred alternative. Should counsel refuse, a complaint may be filed with the Office of the Taxpayers' Ombudsman who has a direct line of communication to the Minister. It is the Minister who is effectively entitled to the privilege and who has the power to waive it.

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<sup>3</sup> Cf. Canada Revenue Agency, TPM-04 Document, "Third-Party Information", October 27, 2003 (modified on April 24, 2020).

<sup>4</sup> *Tax Court of Canada Rules (General Procedure)*, SOR/90-688a.

<sup>5</sup> Cf. Canada Revenue Agency, IM-01 Investigations Manual IM-01 Part-2 Tax, section 1.13 "Legal opinions from Department of Justice", October 17, 2007; Cf. Canada Revenue Agency, Manuel de la vérification, 2008, pages 15-16.

<sup>6</sup> *Blake v. Blake*, 2019 ONSC 4062, para. 30 (motion for leave to appeal granted: *Blake v. Blake*, 2020 ONSC 2203); Cf. *Likhi c. Canada (Citizenship and Immigration)*, 2020 CF 171, para. 39.

<sup>7</sup> *Mann v. Carnell*, (1999) 201 CLR 1.

<sup>8</sup> *Id.* [references omitted].

## RECENT INCOME TAX INTERPRETATIONS

### TOSI — “Excluded Shares”— Clarification of 2019-081943E5

The Canada Revenue Agency (“CRA”) provided clarification on some comments made previously in technical interpretation 2019-0819431E5, dated January 10, 2020. The scenario addressed was set out in detail in the previous interpretation and involved a corporation that initially both carried on a medical services business and earned income from a significant portfolio of investments which had been acquired with the earnings of the medical services business (“PC1”). The physician held all of the voting shares and the spouse and physician each held 50% of the non-voting shares. PC1 ceased carrying on the medical services business and a new corporation (“PC2”) was incorporated for this purpose at the end of year 1, with the spouse acquiring 50% of the voting shares of PC1 from the physician for fair market value consideration.

The question addressed in 2019-0819431E5 was whether the shares of PC1 held by the spouse would qualify as “excluded shares” for years 1, 2, 3, and subsequent years. In respect of years 1 and 2, no clarification was required. However, the CRA’s comments on the application of the “excluded share” definition as it may apply for year 3 and subsequent years (which were that the shares of PC1 held by the spouse would not qualify as “excluded shares”, such that dividends paid on the shares to the spouse would be subject to TOSI, in part because they would be considered to be derived directly or indirectly from a “related business” carried on by PC2 (and not PC1) in year 2 and subsequent years) did require clarification since, in respect of those years, the CRA’s published comments on “second generation” income as set out in 2018-0779981C6 and 2018-0768801C6 should have been specifically addressed.

Specifically, if the income of PC1 for year 2 and any subsequent year is income earned solely from its investment business (a question of fact), such income would not be considered to be derived directly or indirectly from the medical services business now carried on by PC2. This would be the case even though the historical retained earnings of PC1 that are used in PC1’s investment business were originally derived from its former medical services business. Accordingly, in those circumstances, the CRA would consider all the conditions of the “excluded share” definition to be technically met for those years.

A caution was added that if it is determined that any transaction, either alone or as part of a series, has been undertaken primarily to obtain the “excluded amount” exemption under subsection 120.4(1) of the *Income Tax Act* in a manner that would frustrate the object, spirit, and purpose of section 120.4, the CRA would seek to apply the general anti-avoidance rule.

— *External Technical Interpretation, Reorganizations Division, April 8, 2020, 2020-0839581E5*

### Exemption of Prescribed Prizes

The Canada Revenue Agency (“CRA”) was asked if certain prizes met the definition of “prescribed prizes” in section 7700 of the *Income Tax Regulations* (the “Regulations”), and if the entity giving them was justified to issue T4A forms to the recipients. Unfortunately, the information concerning the name of the prizes, the entity giving the prizes, the number of prizes given, and the potential recipients was stricken from the technical interpretation. The CRA offered some general information and confirmed that the prizes would qualify as prescribed prizes under section 7700 of the Regulations. The CRA confirmed that the prize was awarded for meritorious achievement in the arts (a field of endeavour ordinarily carried on by the prize recipient) and did not appear to be for services rendered or to be rendered. Additionally, it is reasonable to conclude that the prize was recognized by the general public. Therefore, the prize qualified as a prescribed prize under section 7700 of the Regulations and would not be included in the income of the recipient under paragraph 56(1)(n) of the *Income Tax Act*. The payer of the prize did not have to report the prize on T4A forms to the recipients and was to cancel them regardless of whether they were asked to do so by the recipients. For more details on how to proceed for the cancellation of T4A forms, see CRA Guide RC4157.

— *External Technical Interpretation, Business and Employment Division, February 5, 2020, 2019-0811441E5*

### Donation of Shares

The Canada Revenue Agency (“CRA”) was asked if the transfer of all the issued shares of the capital stock of a corporation by an individual to a “qualified donee” for the sum of \$1 per share would be considered a gift for the purpose of claiming a charitable donation tax credit under section 118.1 of the *Income Tax Act* (the “Act”). The individual was also considering giving the assets instead of the shares of the corporation. After noting that the taxpayer’s question was more in the nature of a request for general tax planning or tax advice, the CRA confirmed that this was well beyond its mandate and suggested that the taxpayer seek independent professional tax advice. A gift of shares or corporate assets by the shareholder can result in complex income tax implications that should be taken into consideration.

However, the CRA provided the following general information:

- To qualify for a charitable donation tax credit, the gift must be supported by an official donation receipt issued by a "qualified donee" (as defined in subsection 149.1(1) of the Act).
- The term "gift" is not defined in the Act, but is normally considered a voluntary transfer of property by a donor who freely disposes of it to a donee who receives it without any right, privilege, material benefit, or advantage conferred on the donor or any person designated by the donor in exchange for the gift. The question of whether there is a gift is one of fact to be determined after a careful review of all the circumstances.
- The receipt of an advantage (i.e., a benefit or other consideration) by a donor from a donee would not by itself disqualify a property transfer from being a gift to a qualified donee for tax purposes (see subsection 248(30) of the Act).
- The "eligible amount" of the gift used to claim the charitable donation tax credit would be the excess of the fair market value ("FMV") of the property transferred to a "qualified donee" over the FMV of the advantage (see Income Tax Folio S7-F1-C1 and CRA Policy Statement P-113).
- For dispositions of capital properties (including shares and corporate assets) by way of gift, see subparagraph 69(1)(b)(ii) and subsections 118.1(6) and 248(35) of the Act and Income Tax Folio S7-F1-C1 for rules to determine the deemed proceeds of disposition of those capital properties. In those situations, the designated amount is treated as both the disposition proceeds to calculate the donor's capital gain and the FMV of the gifted property to determine the eligible amount of the gift to calculate the charitable donation tax credit.
- An individual giving a property considered to be a "non-qualifying security" ("NQS") to a "qualified donee" is considered under subsection 118.1(13) of the Act as having not made that gift and not to qualify for a charitable donation tax credit in respect of that gift. An NQS is defined in subsection 118.1(18) of the Act as a share of the capital stock of a corporation if the individual or his/her estate does not deal at arm's length with the corporation. An NQS does not include a share of a corporation listed on a designated stock exchange.

— *External Technical Interpretation, Financial Industries and Trusts Division, February 13, 2020, 2019-0825501E5*

## Death of RRSP or RRIF Annuitant

The Canada Revenue Agency ("CRA") was asked to consider

- (1) whether the deduction provided in subsection 146(8.9) or 146.3(6.2) of the *Income Tax Act* (the "Act"), as the case may be, is discretionary when the surviving spouse is named the sole beneficiary in an unmatured registered retirement savings plan ("RRSP") or a registered retirement income fund ("RRIF") contract;
- (2) whether an amount may be deducted under subsection 146(8.9) or 146.3(6.2) when the surviving spouse is designated in the contract as the successor annuitant of a matured RRSP or an RRIF;
- (3) when the annuitant of an unmatured RRSP or an RRIF dies and the surviving spouse is named as the sole beneficiary in the contract, whether the exception to issue T4RSP and T4RIF slips in the name of the surviving spouse, instead of in the name of the deceased, is applicable only when all of the property of the unmatured RRSP or RRIF is transferred directly to an RRSP or RRIF under which the spouse is the annuitant;
- (4) what is the time limit applicable for the issuer of an RRSP or RRIF to file the T4RSP or T4RIF slip when the annuitant died in December 20X1 and the issuer is notified of the death in March 20X2; and
- (5) whether the deduction of an amount pursuant to subsection 146(8.9) or 146.3(6.2) of the Act is possible even if the estate did not receive in the prescribed delay a T4RSP or a T4RIF slip in the deceased annuitant's name.

The CRA responded as follows:

- (1) Yes, subsections 146(8.9) and 146.3(6.2) both provide for a discretionary deduction.
- (2) No. For subsection 146(8.9) to apply, an amount must otherwise be deemed received pursuant to subsection 146(8.8), and an amount must qualify as a refund of premium which is not possible in the case where the annuitant dies after the maturity of the RRSP. Similarly, for subsection 146.3(6.2) to apply, there must be an amount that would otherwise be included under subsection 146.3(6). Subsection 146.3(6) of the Act applies only when the last annuitant of an RRIF dies.

(3) The exception only applies when all the conditions are met. As explained in RC4177, RC4178, and T4079, unless all the conditions are met, T4RSP and T4RIF slips must be issued in the name of the deceased.

(4) Subsection 205(1) of the *Income Tax Regulations* provide that T4RSP or T4RIF information returns shall be filed on or before the last day of February in each year and shall be in respect of the preceding calendar year. However, when an issuer or a carrier is only notified of the death of an annuitant of an RRSP or an RRIF after its information return has been filed, the issuer or the carrier must file an additional slip for the deceased individual as stated in Chapter 5 of the T4079 Guide.

(5) Yes. The fact that the estate did not receive in the prescribed delay a T4RSP or a T4RIF slip does not change the responsibility of the deceased annuitant's legal representatives to properly include in the final return the amount deemed received by the last annuitant under subsection 146(8.8) or 146.3(6), as the case may be. Such amount will be dependent on any reduction under subsection 146(8.9) or 146.3(6.2), as applicable, provided all the conditions set out in the applicable provision are met.

— *External Technical Interpretation, Financial Industries and Trusts Division, April 8, 2020, 2016-0668991E5*

## Car Share Expenses

The Canada Revenue Agency ("CRA") was asked whether car share expenses are deductible by a salaried employee in computing income from employment under section 8 of the *Income Tax Act* (the "Act").

The CRA responded likely yes. While paragraph 8(1)(h.1) of the Act does not outline the specific motor vehicle expenses that may be deducted thereunder, Guide T4044, *Employment Expenses 2018*, describes the types of expenses that may generally be deducted by an employee earning a salary, and clarifies that motor vehicle expenses include fuel, maintenance and repairs, insurance, license and registration fees, and eligible leasing costs. Notwithstanding that a Member does not incur the cost of specific motor vehicle expenses (i.e., fuel, maintenance and repairs, insurance, etc.), it is the CRA's view that the fixed amount (per-minute, per-hour, per-kilometre, or daily) paid by a Member is an amount expended in respect of motor vehicle expenses provided the employer has provided a T2200, there are no benefits provided to the member that are unrelated to the use or operation of the automobile, and the amount is reasonable and is supported by receipts.

— *External Technical Interpretation, Business and Employment Division, March 9, 2020, 2019-0812581E5*

## Deferred Salary Leave Plans

The Canada Revenue Agency ("CRA") was asked whether it could extend the six-year maximum deferral period for deferred salary leave plans ("DSLPS"). The individual asking the question works in the public health sector and is concerned about taking a leave of absence at a time when those services are needed most. The individual asked the CRA to extend the maximum deferral period for their DSLP since if the leave is not taken as scheduled, the person's DSLP will have to be terminated, resulting in all deferred salary being paid to them and included in their income.

The CRA responded, stating that it has no discretion to extend the maximum deferral period for DSLPs; this would require an amendment to the *Income Tax Regulations*.

CRA officials have discussed this concern with officials of the Department of Finance who are presently considering several submissions on issues relating to the DSLP rules that have arisen due to COVID-19. They have agreed to consider this issue as part of their review.

Pending completion of the Department of Finance review, the CRA will not require an employer to terminate an individual's DSLP in the event that the individual defers their leave of absence beyond the six-year maximum deferral period. This administrative position will apply regardless of the reason for deferring the leave.

— *External Technical Interpretation, Financial Industries and Trusts Division, May 14, 2020, 2020-0848641E5*

## Eligible Dependent Credit — Shared Custody Situations

The Canada Revenue Agency ("CRA") Rulings Directorate was asked by a staff member to comment on the application of subsection 118(5.1) of the *Income Tax Act* (the "Act") in shared custody situations where child support payments are made under a "set-off" arrangement. Specifically, it was asked how such arrangements could impact the taxpayer's ability to claim an eligible dependent tax credit under paragraph 118(1)(b) of the Act. In this particular situation, the support amounts and set-off amounts were calculated under the Federal Child Support Guidelines.



Relying on CRA Guide P102, on Income Tax Folios S1-F3-C3 and S1-F4-C2, and on the current case law, the CRA provided the following general comments:

- Subsection 118(5) of the Act prevents an individual from claiming a personal tax credit under subsection 118(1) for a person for a taxation year if he or she pays a "support amount" (as this term is defined in subsection 56.1(4)) for that person to his or her spouse or common-law partner. This applies only if the individual is separated from his or her spouse or common-law partner during the whole year, or if he or she claims a deduction for the year under section 60 of the Act for support paid to that spouse or common-law partner.
- However, subsection 118(5.1) of the Act ensures that one individual can still claim the personal tax credit (i.e., eligible dependent tax credit or Canada caregiver tax credit) for an infirm child in a case involving a shared custody situation or a change of custody in the year. In this situation, more than one person may be required to pay support for the same child in a taxation year. Note that the two individuals must agree on who may claim the credits for the child, or the credits will be lost for both of them.
- Where parents live separately and share custody of two children, one parent can claim the credit for one child and the other parent can claim the credit for the other child.
- To benefit from subsection 118(5.1) of the Act, both parents (not only one) must be prevented from claiming the credit under subsection 118(5) and must be required to pay some "support amounts" (as this term is defined in subsection 56.1(4)). For example, the payments must be made under an order of a competent tribunal or under a written agreement.
- The requirement under the child support guidelines to use the income of both parents in determining the single support payment to be paid by one spouse or common-law partner is not equivalent to the requirement for two distinct legal obligations to pay such support. Only the second requirement would result in the application of subsection 118(5.1) of the Act.
- Subsection 118(5.1) of the Act will not apply if there is only legal obligation for one parent and one set-off payment made by that parent, but it will apply where:
  - (1) there is a court order or written agreement supporting the legal obligation of both parents to pay child support; and
  - (2) the parents agree to use a set-off arrangement (i.e., the parents must pay support to each other, but only one of them will make a child support payment for the difference).

In other words, a court order or written agreement calculating the child support obligations based on a statutory scheme like the Federal Child Support Guidelines does not necessarily establish a requirement for both parents to make child support payments under the Act. Even if the income of both is used to calculate child support, it is not sufficient to establish the requirement that both of them make child support payments. Unless the order or written agreement establishes that both parents must pay child support, only one of them is considered to be making child support payments. In this case, the payer cannot claim the personal tax credit, and the recipient may claim it only if he or she is otherwise eligible to claim the amount. Whether the written agreement or court order imposes a legal obligation on both parents to pay child support is a question of fact.

— *Internal Technical Interpretation, Business and Employment Division, December 9, 2019, 2019-08181017*

## Supplementary Employee Retirement Plan and Group RRSP

The Canada Revenue Agency ("CRA") was asked to rule on whether the supplementary employee retirement plan (the "Supplemental Plan", a "SERP"), as described below, was a salary deferral arrangement ("SDA"), as defined in subsection 248(1) of the *Income Tax Act* (the "Act"). The CRA confirmed that the Supplemental Plan was not an SDA because it would provide reasonable pension benefits and none of its main purposes were to postpone the payment of tax. More specifically, the CRA ruled that:

- (1) the plan was not an SDA;
- (2) the plan was not a retirement compensation arrangement ("RCA"), as defined in subsection 248(1) of the Act;
- (3) no amount would be included in the member's income under subsection 5(1) or paragraph 6(1)(a) as a result of the member's participation in the plan;
- (4) the payments made under the plan by the employer to a member, former member, or beneficiary under the plan would be included in the recipient's income in the taxation year the amount is received as a superannuation or pension benefit under subparagraph 56(1)(a)(i);
- (5) subject to subsection 18(1) and sections 67 and 78, subsection 9(1) will allow the employer to deduct from its income any of the amounts paid to a member, former member, or beneficiary of the plan in the taxation year the employer is required to pay those amounts; and

(6) subsection 12(4) would not apply to a plan member to require any amount to be included in his income as interest for his entitlements under the plan.

The purpose of the transactions for which the ruling was issued was to establish a supplemental plan to provide the employees and executive employees of the above employer with additional post-termination employment benefits beyond those earned from contributions to the company's group RRSP since such contributions were subject to certain limits under the Act.

— *Tax Ruling, Financial Industries and Trusts Division, 2019, 2019-0817751R3*

## COVID-19 — Expiry of Unused Credits in Health Care Spending Account

The situation the Canada Revenue Agency ("CRA") was asked to consider involved credits allocated to an employee's health care spending account ("HCSA") which could not be used by the employee before their expiration because of the COVID-19 pandemic preventing the health care service providers from rendering their services. More specifically, the CRA was asked if those HCSA credits could be carried forward without affecting the private health services plan ("PHSP") status of the HCSA. The CRA confirmed that, because of the COVID-19 pandemic, an HCSA that already qualified as a PHSP and that had unused credits expiring between March 15, 2020 and December 31, 2020, could be carried forward for a reasonable period of time to enable the employee to access health care services otherwise restricted during the COVID-19 outbreak. The CRA added that a period of up to six months would be considered reasonable and would not disqualify the HCSA as a PHSP.

Note that the above interpretation would apply to the following three models of HCSAs:

- Use it or lose it model — HCSA does not permit the carry-forward of unreimbursed eligible medical expenses or unused credits.
- Carry-forward of credits — HCSA permits the carry-forward of unused credits to the next plan year (i.e., a period not exceeding 12 months).
- Carry-forward of expenses — HCSA permits the carry-forward of unreimbursed eligible medical expenses to the next plan year (i.e., a period not exceeding 12 months).

— *External Technical Interpretation, Business and Employment Division, May 25, 2020, 2020-0846751E5*

## Canada Emergency Wage Subsidy — Meaning of Public Institution

The Canada Revenue Agency ("CRA") was asked for comments on the definition of "public institution" for the purposes of the recently enacted section 125.7 of the *Income Tax Act* (the "Act"). Section 125.7 implements the new Canada Emergency Wage Subsidy ("CEWS") for Canadians who have lost their jobs due to the COVID-19 pandemic. Specifically, the CRA was asked what criteria would be considered when determining if an entity is a public institution. It was also asked if the question of eligibility depends on whether the entity's enabling legislation states that it is a Crown agent. If this is the case, the agency is a public institution not eligible for the CEWS.

The CRA first noted that whether an entity was one described in paragraphs 149(1)(d) to (d.6) of the Act was determined with reference to the ownership of the shares or capital of the corporation and the existence of any right by a person other than Her Majesty in right of Canada, a province, or a Canadian municipality to acquire the shares. In the context of a corporation with no share capital, the determination of ownership requires a review of all relevant documents, including articles of incorporation, by-laws, and agreements relating to the operation and control of the corporation and its assets. The following factors are relevant in making such a determination:

- the structure of the corporation;
- the identity of its members;
- who exercises control over the financing, operation, and direction of the corporation;
- who has the right to elect or change the board of directors or to reverse its decision;
- who can contribute capital and receive a distribution of capital;
- details regarding asset distribution on winding-up or dissolution; and
- whether a person other than Her Majesty in right of Canada, a province, or a Canadian municipality has any right to acquire any of the corporation's capital.

— *External Technical Interpretation, Financial Industries and Trusts Division, May 1, 2020, 2020-0846931E5*

## COVID-19 — Deferred Salary Leave Plan

The situation the Canada Revenue Agency ("CRA") was asked to consider involved a deferred salary leave plan ("DSLPL"), which allowed employees to defer their salary for funding a leave of absence from their employment, but only if they met certain conditions. One condition was that the deferral period could not exceed six years, with the leave period beginning immediately after the deferral period. Another condition was that the leave period had to be a continuous one of at least six consecutive months (or three months for certain educational leaves).

The COVID-19 pandemic has prevented, as follows, employees providing essential services and covered by a DSLPL from meeting the above DSLPL conditions:

- They were recalled from their leave period before having met the minimum leave period condition, but would resume their leave of absence following the end of the pandemic.
- They were unable to begin their leave of absence as scheduled, and would therefore contravene the maximum deferral period condition.

Under normal conditions, the DSLPL would be terminated and all deferred salary would be paid to the employees and included in their income. However, the CRA confirmed that, because of the COVID-19 outbreak, the employers would not have to terminate the DSLPLs for any failure to meet one of the above conditions. The administrative position will remain applicable regardless of the reason for deferring the leave or returning to work. This administrative position will also accommodate employees who had planned to travel during their leave of absence, but could not do it or had to return early because of travel restrictions caused by the COVID-19 pandemic.

The above situation is currently under review by the Department of Finance.

— *External Technical Interpretation, Financial Industries and Trusts Division, May 28, 2020, 2020-0849681E5*

## COVID-19 UPDATE

Given the rapidly changing information related to COVID-19 we are providing continuously updated information at <https://blog.intelliconnect.ca/>.

### Federal

#### Government Announces Extension of Rent Relief for Small Businesses (September 8, 2020)

The Canada Emergency Commercial Rent Assistance ("CECRA") for small businesses will be extended by one month to help eligible small businesses pay rent for September. All provinces and territories continue to participate in this initiative and collaborate with the federal government to provide rent supports to those small businesses most in need. Current CECRA application deadlines will also be extended to accommodate this extension. The government announced this will be the final extension of this program as the government explores options to support small businesses as they face the ongoing challenges of the COVID-19 pandemic.

#### Extended SR&ED Reporting Deadlines (September 4, 2020)

Under the *Time Limits and Other Periods Act (COVID-19)*, the Canada Revenue Agency has received a ministerial order to extend certain deadlines imposed under the *Income Tax Act*.

Corporations with tax year ends from September 13, 2018 to December 31, 2018, that had an SR&ED reporting deadline from March 13, 2020 to June 30, 2020, are extended by six months. Corporations with tax year-ends from January 1, 2019, and to June 29, 2019, that would usually have an SR&ED reporting deadline from July 1, 2020 to December 29, 2020, are extended to December 31, 2020.

For individuals who operated a sole proprietorship with a December 31, 2018, tax year end and who had an SR&ED reporting deadline of June 15, 2020, the deadline is extended by six months to December 15, 2020.

Trusts with tax year ends from December 13, 2018 to April 1, 2019, that would usually have an SR&ED reporting deadline from March 13, 2020 to June 30, 2020, are extended by six months. Trusts with tax year ends of April 2, 2019 to October 1, 2019, that would usually have an SR&ED reporting deadline of July 1, 2020 to December 30, 2020, are extended to December 31, 2020.

#### Guidance on International Income Tax Issues Raised by the COVID-19 Crisis (September 2, 2020)

The application of the guidance, which began on March 16, 2020, was extended from June 29, 2020, to September 30, 2020. Section I.-B. (income tax residency of corporations) has been updated to address a possible issue with corporate residency requirements as it relates to the surplus calculations of a foreign affiliate of a Canadian-resident corporation. Section VI, *Non-resident employer certification*, has been



added to address a possible issue for non-resident employers whose non-resident employees may have had to remain in Canada for an extended period as the result of the travel restrictions. The guidance has also been updated generally to make it more readable and consistent with existing government writing style. None of these changes indicate a change in policy or approach of the CRA in applying the guidance.

## Provincial

### British Columbia

#### Deadlines Extended for Tax Credits

As part of BC's COVID-19 supports, the deadline to apply for some provincial income tax credits — Training Tax Credit for Employers, Book Publishing Tax Credit, Film and Television Tax Credit, Mining Exploration Tax Credit for Corporate/Personal Income Tax, Production Services Tax Credit, Interactive Digital Media Tax Credit, and Scientific Research & Experimental Development Tax Credit — for claims required to be made March 13, 2020 or later is extended to six months from the original due date or to December 31, 2020, whichever is earlier.

The BC mining flow-through share ("MFTS") tax credit eligibility period is being extended from 24 months to 36 months for 2019 and 2020 flow-through share purchases. This is the eligibility period during which an expenditure must be incurred by the issuer in order to be renounced in favour of flow-through shares. This extension aligns the eligibility period for the BC MFTS tax credit with the temporary federal timelines for flow-through shares.

#### Province Confirms Tax Measure Implementation Dates, Deferral Deadlines for Businesses (September 2, 2020)

BC is delaying implementation dates to April 2021 for changes to provincial sales tax ("PST") and the province's carbon tax. A scheduled increase in April 2020 from \$40 to \$45 per tonne of carbon dioxide equivalent ("tCO<sub>2</sub>e") had been paused until at least October as part of the COVID-19 Action Plan. Upon review, the BC government has decided the carbon tax rate will remain at its current level of \$40 per tCO<sub>2</sub>e until April 2021, when it will increase from \$40 to \$45 per tCO<sub>2</sub>e. The carbon tax will increase to \$50 per tCO<sub>2</sub>e in April 2022.

The implementation of two other planned tax changes is also being delayed until April 2021. This includes the elimination of the PST exemption for carbonated beverages that contain sugar, natural sweeteners, or artificial sweeteners, and the addition of new PST registration and collection requirements for e-commerce businesses located outside BC. In addition, the employer health tax ("EHT") 2020 quarterly instalment dates are being extended as follows:

- December 31, 2020 (original instalment date was June 15, 2020);
- January 31, 2021 (original instalment date was September 15, 2020); and
- February 28, 2021 (original instalment date was December 15, 2020).

The 2020 EHT filing and balance due date will remain March 31, 2021.

Effective March 23, 2020, as part of BC's COVID-19 Action Plan, the filing and payment due dates for the following sales taxes were extended to September 30, 2020, along with the 2019 EHT filing and balance due date:

- PST;
- hotel tax, also known as municipal and regional district tax;
- tobacco tax;
- motor fuel tax; and
- carbon tax.

The provincial government announced that these administrative deferrals are not being extended further.

### Saskatchewan

#### Provincial Training Allowance and Skills Training Benefit Programs Repayment To Resume (September 10, 2020)

The Provincial Training Allowance and Skills Training Benefit Programs overpayment moratorium is scheduled to end September 30, with repayments anticipated to resume in October 2020.

## International

### US IRS Clarifies Interest Deduction Limitation (September 9, 2020)

The US Internal Revenue Service has released for publication in the Federal Register final regulations on the limits introduced in the Tax Cuts and Jobs Act ("TCJA") on deductions for business interest expenses, following amendments in the Coronavirus Aid, Relief, and Economic Security ("CARES") Act.

Under the TCJA, for tax years beginning after December 31, 2017, business interest expense deductions are generally limited to the sum of: the taxpayer's business interest income; 30 per cent of the taxpayer's adjusted taxable income; and the taxpayer's floor plan financing interest expense.

The CARES Act temporarily increased the amount of interest expense businesses are allowed to deduct to 50 per cent of adjusted taxable income for 2019 and 2020.

The regulations (TD 9905) provide guidance to taxpayers on how to calculate the limitation, what constitutes interest for purposes of the limitation, which taxpayers and trades or businesses are subject to the limitation, and how the limitation applies in consolidated group, partnership, international, and other contexts.

### OECD Releases 2020 Tax Trends Report (September 4, 2020)

The OECD has released its annual report on global tax policy reform trends, noting that while governments have taken unprecedented fiscal action in response to the COVID-19 crisis, more fiscal stimulus measures will be necessary to support the economic recovery, despite rising costs.

The report, "Tax Policy Reforms 2020", describes the latest tax reforms across OECD countries, as well as in Argentina, China, Indonesia, and South Africa. The report identifies major tax policy trends adopted before the COVID-19 crisis and takes stock of the tax and broader fiscal measures introduced by countries in response to the pandemic, from its outbreak to June 2020.

The report shows that while the size of fiscal packages in response to the COVID-19 crisis has varied across countries, most have been significant, and many countries have taken unprecedented action. It also points out that most countries have adopted a phased approach to COVID-19, gradually adapting their fiscal packages as the crisis has unfolded.

Initial government responses focused on providing income support to households and liquidity to businesses to help them stay afloat. As the crisis has continued, many countries expanded their initial response packages. The most recent measures and discussions suggest that the recovery phase will be supported by expansionary fiscal policy in a number of countries, the report says.

With countries facing such high levels of uncertainty, policy agility will be key and targeted support measures should be maintained as long as needed to avoid scarring effects, says the report. Once recovery is well underway, governments should then shift from crisis management to more structural tax reforms. However, the OECD said they must be careful not to act prematurely as this could jeopardize recovery.

"Right now, the focus should be on the economic recovery. Once the recovery is firmly in place, rather than simply returning to business as usual, governments should seize the opportunity to build a greener, more inclusive, and more resilient economy," said Pascal Saint-Amans, Director of the OECD Centre for Tax Policy and Administration. "One path that should be urgently prioritized is environmental tax reform and tax policies to tackle inequalities."

Rising pressure on public finances as well as increased demands for fairer burden-sharing should also provide new impetus to reach an agreement on digital taxation, he said, adding: "Tax co-operation will be even more important to prevent tax disputes from turning into trade wars, which would harm recovery at a time when the global economy can least afford it."

Tax Policy Reforms 2020 also provides an overview of the reforms introduced before the COVID-19 crisis. It highlights continuation of a number of trends identified in previous years, including personal income tax reductions for low- and middle-income households and the stabilization of standard value-added tax ("VAT") rates observed across many countries. Corporate tax rates have continued to decline, but at a faster pace than in 2019, the report says.

The report also notes that "clear progress" has been made in areas covered by the OECD's base erosion and profit shifting Action Plan. These include reforms to ensure the effective collection of VAT on online sales of goods, services, and intangibles, and the adoption of measures to protect corporate tax bases against international tax avoidance. On the other hand, progress on environmentally related taxes has been slow, with reforms being concentrated in a small number of countries and limited in scope, the report says.

The report also notes that there has been a marked change in property taxation compared with previous years, with an increase in the number of reforms in that area, generally aimed at raising taxes.

## RECENT CASES

### Expenses incurred by taxpayer in winding up his pension plan during course of marital dispute not deductible as business expenses

At all material times, the taxpayer operated a management consulting service as a sole proprietorship. His marital relationship broke down, and he subsequently made an assignment into bankruptcy. This resulted in an order by the Superior Court of Justice Family Branch requiring, among other things, that one half of the amount accrued in his Individual Pension Plan ("IPP") be transferred to his spouse. In order to comply with this order, the taxpayer incurred legal, accounting, and other professional fees in the amount of \$33,653, which the Minister disallowed as a business expense deduction subsequently claimed by the taxpayer. The taxpayer appealed to the Tax Court of Canada.

The appeal was dismissed. Fees involved in the winding up of an IPP could not be considered as having been incurred in the normal course of income-earning operations. In this case, the legal, accounting, and other professional fees were incurred by the taxpayer to comply with the terms of a court order to wind up the taxpayer's IPP, and to transfer 50% of its value to the taxpayer's spouse. These fees were not incurred for the purpose of earning income for the taxpayer's IPP, or for the taxpayer himself. Hence they were not deductible as a business expense, and the Minister's assessment was affirmed accordingly.

¶150,531, *Burley v. The Queen*, 2020 DTC 1049

### In transferor-transferee tax liability proceedings, Minister correctly calculated tax liability of transferor

L was the sole shareholder, director, and officer of the corporate taxpayer 257, and of 661. In 2003, when it owed tax for 2000, 661 transferred an amount in excess of \$900,000 to 257 for no consideration. The Minister assessed 257 under the transferor-transferee tax liability provisions of section 160 of the *Income Tax Act*. Accordingly, 257 appealed to the Tax Court of Canada, alleging that: (a) non-capital losses incurred in 661's 2001 and 2002 taxation years ought to have been carried back to its 2000 taxation year, which would have reduced its taxable income for 2000; and (b) as a result it did not have a tax liability for 2000 in the amount that led to the Minister's assessment.

The appeal was dismissed. The core issue was whether 661 had a tax liability when it transferred the funds in question to 257, and whether the Minister had correctly calculated interest on that liability. 661 did have a tax liability when it effected the transfer in issue, and the Minister correctly calculated that interest. Also, it was 661's right to choose how to allocate its 2002 losses and the Minister had no legal basis to impose on 661 an obligation to apply its 2002 unused losses to its 2000 taxation year in this case, despite 257's argument to the contrary.

¶150,530, *1455257 Ontario Inc. v. The Queen*, 2020 DTC 1048

## INTERNATIONAL NEWS

### IRS Keeps Tax-Related Interest Rates on Hold

The US Internal Revenue Service ("IRS") has announced that tax-related interest rates will remain the same for the calendar quarter beginning October 1, 2020. The rate of interest is determined on a quarterly basis. For taxpayers other than corporations, the overpayment and underpayment rate is the federal short-term rate plus three percentage points.

For the quarter beginning October 1, 2020 the interest rates will be:

- three per cent for overpayments (two per cent in the case of a corporation);
- 0.5 per cent for the portion of a corporate overpayment exceeding US\$10,000;
- three per cent for underpayments; and
- five per cent for large corporate underpayments.

The interest rates are contained in Revenue Ruling 2020-18, which will appear in Internal Revenue Bulletin 2020-39, dated September 21, 2020.

## IRS Reviewing Double Tax Dispute Resolution Processes

The IRS is undertaking a review of its procedures for taxpayers seeking competent authority assistance, to reduce the compliance burden on taxpayers and their agents.

US taxpayers can seek assistance from the US competent authority if they think that the actions of the United States, a treaty country, or both, cause or will cause double taxation or taxation otherwise inconsistent with the treaty. Instructions are set out in Revenue Procedure 2015-40. Typically, provisions to resolve double tax issues involving a treaty country are included in the Mutual Agreement Procedure article of the relevant tax treaty.

Written comments on the burden on taxpayers of requesting assistance under Revenue Procedure 2015-40 should be sent to the IRS by November 2, 2020.

### TAX TOPICS

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