

TAX WITHHOLDING OBLIGATIONS OF NON-RESIDENT EMPLOYERS: FURTHER EXEMPTION DETAILS RELEASED

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In its 2015 Budget, the Canadian federal government announced its intention to exempt "certified" non-resident employers from the obligation to withhold and remit income tax in respect of certain employees that perform duties in Canada. The Canada Revenue Agency (the "**CRA**") recently released the application form that a non-resident employer must use to secure relief under the new exemption regime. **However, if non-residents wish to rely on the new exemption from the beginning of 2016, they must act fast as relief retroactive to the beginning of the year must be requested by March 1st.**^[1]

Background

In the past, non-resident employers have been required to withhold a portion of the remuneration paid to a non-resident employee in respect of services performed in Canada and remit such amounts to the CRA. While the non-resident employee might not have been subject to Canadian income tax by virtue of a tax treaty, the employer was nevertheless required to withhold and remit tax, and the employee was thereafter required to file a Canadian tax return to obtain a refund of the tax withheld.

As an administrative matter, the CRA permits non-resident employees to apply for a waiver that suspends the obligation to withhold under certain circumstances. Unfortunately, requests for such waivers are time consuming and require the submission of a significant amount of information. In addition, such waivers only apply in respect of a single employee, are narrow in scope, and need to be sought well in advance of a non-resident employee performing duties in Canada. As a consequence, the waiver process is widely regarded as cumbersome and impractical in most cases.

New Relieving Measures

In July 2015, the government introduced statutory amendments in support of its promise to ease the withholding and reporting burdens placed on non-resident employers (the "**Relieving Measures**")^[2].

The Relieving Measures provide that an employer will not be required to make income tax withholdings if (i) the employer is a "qualifying non-resident employer", and (ii) the employee is a "qualifying non-resident

employee".

"Qualifying Non-Resident Employers"

To be a "qualifying non-resident employer", an employer must satisfy two conditions.

First, the employer must be resident in a country with which Canada has a tax treaty.^[3]

Second, the employer must be "certified" by the Minister of National Revenue (Canada) ("**Minister**"). The Relieving Measures provide that the Minister *may* certify an employer for a specified period of time if the employer has applied in prescribed form, and the Minister is satisfied that the employer meets both (i) the treaty residence requirement described above, and (ii) any other conditions established by the Minister.

It is ultimately in the discretion of the Minister whether to "certify" a non-resident employer, and the Minister may impose any conditions on certification that she deems appropriate, which may change over time.

At the time of the release of the Relieving Measures, the prescribed form to be used to apply for certification, and the list of the qualifying conditions to be imposed by the Minister governing certification, were not released.

"Qualifying Non-Resident Employees"

To be a "qualifying non-resident employee", an employee must (i) be resident in a country with which Canada has a tax treaty, (ii) not be liable to pay general Canadian income tax in respect of payments received from the qualifying non-resident employer because of that treaty, and (iii) work in Canada for less than 45 days in the calendar year that includes the time of a payment *or* be present in Canada for less than 90 days in any 12-month period that includes the time of a payment.

Employers may encounter difficulties in applying the foregoing tests. For instance, determining the residence of an employee can be difficult where facts relating to the employee's personal circumstances are not readily available, or the employee maintains homes in multiple jurisdictions. In addition, to be a "qualifying non-resident employee", an employee must be able to claim the benefits afforded by a tax treaty. Where a treaty imposes conditions on the ability to claim treaty relief, determining whether an employee is entitled to the benefits of the treaty may be challenging. Finally, an employee's status as a "qualifying non-resident employee" is dependent on the employee working or being present in Canada for less than a specified number of days. Where work schedules are varied, or the employee may be present in Canada for personal reasons or in respect of employment by others, the ability to determine whether the "days in Canada" test is satisfied may again be limited.

Employer Certification

In the middle of January 2016, the CRA released the list of conditions that must be satisfied for the CRA to certify a particular non-resident employer as a "qualifying non-resident employer", along with the prescribed form to be used to apply for certification.

To obtain certification as a "qualifying non-resident employer", a non-resident must submit new Form RC473 to the CRA (the "**Application Form**"). (A copy of the Application Form can be accessed [here](#).)

A non-resident must have a CRA Business Number in order to apply for certification. (If a non-resident employer does not have a Business Number, the non-resident is required to register for a Business Number when submitting its Application Form.)

The Application Form requires a non-resident to submit detailed information regarding the applicant's business and activities in Canada, including the following:

1. whether the non-resident provides services in Canada pursuant to a contract;
2. the estimated date that the non-resident's first employee will arrive in Canada;
3. the estimated number of employees of the non-resident that will come to Canada during the certification period;
4. the employer's industry (including additional details if the non-resident is involved in the entertainment industry); and
5. the types of services that the non-resident's employee(s) will be providing in Canada.

The Application Form also requires a non-resident employer to provide certain covenants to the CRA, including covenants that the employer will:

1. comply with "all obligations and requirements" imposed on a "qualifying non-resident employer";
2. inform the CRA immediately of any changes to the information presented in the Application Form, or if the employer no longer meets the conditions of a "qualifying non-resident employer"; and
3. only exempt payments from withholding upon receipt of an approval letter from the CRA certifying that the employer is a "qualifying non-resident employer".

The CRA has indicated that the "obligations and requirements" of a qualifying non-resident employer require the employer to:

- evaluate and document how a particular employee meets the definition of a "qualifying non-resident employee" at the time the employer pays any employment income to the particular employee. (The CRA has stated that, in performing such an evaluation, the employer must (a) make sure the employee meets the definition of a "qualifying non-resident employee" on an ongoing basis, (b) obtain documents to

support the employee's country of residence, and (c) have in its possession the information/documentation necessary to demonstrate how the employee is expected to be exempt from tax in Canada because of a tax treaty.);

- track and document, on an ongoing basis, the number of days a qualifying non-resident employee is working or is present in Canada, and the employment income that corresponds to those days;
- prepare and file information returns in respect of each non-resident employee (including T4 slips and T4 summaries) unless such reporting is excluded under the applicable income tax regulations (as discussed in greater detail below).
- complete and file Canadian income tax returns for those calendar years covered by the certification period; and
- make its books and records available in Canada for the CRA to inspect so that it can verify that the employer is meeting (a) the covenants made in the Application Form, and (b) its withholding requirements under the *Income Tax Act* (Canada) (the "**Tax Act**").

Exemptions from withholdings under the Relieving Measures will not apply to a particular non-resident employer until the employer has been notified in writing that they have been certified. The CRA has indicated that an Application Form must be submitted at least 30 days prior to the commencement of a non-resident employee providing services in Canada for the non-resident applicant.

Certifications will not be granted by the CRA on a retroactive basis. ***However, as a transitional measure, the CRA has indicated that, if a completed Application Form is submitted by the end of the day on March 1, 2016, the CRA may retroactively certify a non-resident employer as of January 1, 2016.***

Once granted, certifications may remain valid for up to two calendar years. Employers are permitted to subsequently request the extension of the two-year certification period.

Advantages of Certification

A qualifying non-resident employer will be relieved of the obligation to make income tax source withholdings from remuneration paid to qualifying non-resident employees.

If a qualifying non-resident employer does not withhold and remit income tax in respect of a particular employee that the employer thought was a qualifying non-resident employee, and it is subsequently demonstrated that the employee was not a qualifying non-resident employee, the employer will not be subject to a penalty if, after "reasonable inquiry", the employer had no reason to believe, at the time of each payment of remuneration, that the employee was not a qualifying non-resident employee. (What constitutes a "reasonable inquiry" is not defined in the Tax Act; however, the CRA has indicated that a "reasonable inquiry" requires an employer to "take prudent measures to proactively monitor and confirm" that its employee is not a qualifying

non-resident employee.)

The Relieving Measures further provide that a non-resident employer is not required to file Canadian information returns and reporting slips (i.e., T4 reporting documentation) in respect of a qualifying non-resident employee if the employer, after reasonable inquiry, has no reason to believe that the employee's total taxable income earned in Canada during the relevant calendar year is more than CAD\$10,000.

In considering whether the exemption from information reporting requirements applies, it is critical to note that the applicable test differs from the test used to determine whether source withholdings and remittances are required. Most significantly, the test focuses on the employee's taxable income earned in Canada during the year and is not governed by the number of days the employee spent in Canada. The test looks to all sources of taxable income, not just amounts received from the non-resident employer, and is based on the gross amount of taxable income earned in Canada by the employee, without regard to the portion of such income that may not ultimately be subject to Canadian taxation by virtue of a tax treaty.

Other Implications of Certification

The CRA has expressly indicated that it will not consider an applicant's compliance history with respect to its past withholding, remittance and reporting obligations when reviewing an application for certification. However, the CRA has stressed that certification does not cancel any past tax, penalty or interest liability, and encourages applicants to consider making a voluntary disclosure to address past compliance deficiencies in advance of submitting an Application Form.

The covenants made under the Application Form require a non-resident employer to maintain detailed records of the activities and presence of an employee in Canada, and undertake meaningful due diligence in respect of the residency of the employee and his/her entitlement to claim the benefits of a particular tax treaty.

Exemption from Canadian income tax source withholding obligations also does not relieve the employer of the potential obligation to withhold and remit amounts from remuneration in respect of Canada Pension Plan and Canadian Employment Insurance obligations.

Finally, the obligation to make books and records available in Canada for CRA review may signal an enhanced likelihood that the non-resident employer may be subject to a CRA audit review in the future.

Revocation of Certification

The CRA reserves the right to revoke a certification if it believes that the non-resident employer fails to satisfy its covenants in the Application Form, or if the facts presented in the Application Form prove to be inaccurate. If certification is revoked, the CRA has indicated that the employer may become liable to withhold and remit

tax to the CRA and may be subject to any related penalties and interest for the entire period that the employer was certified.

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While the Relieving Measures represent welcome relief to certain non-resident employers that dispatch employees to Canada for limited purposes, non-residents will need to carefully consider the obligations imposed on "qualifying non-resident employers" prior to seeking certification.

[1] On January 28th, the CRA announced that the deadline to request retroactive relief would be extended from February 1st to March 1st.[ps2id id='1' target=""]

[2] It is expected that the Relieving Measures will be enacted into law at some point this year. The CRA has indicated that it will administer the Relieving Measures as if they have already been enacted into law.[ps2id id='2' target=""]

[3] If the employer is a partnership, members of the partnership that are entitled to not less than 90% of the income or loss of the partnership must generally be resident in a country with which Canada has a tax treaty.[ps2id id='3' target=""]

A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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