2015 Federal Budget summary

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Well, as predicted, the 2015 Federal Budget (the "Budget") contained significant tax measures. After years and years of boring tax budgets, recent budgets have reversed that trend and the 2015 Budget is certainly no exception.

For those of you who do not have the patience, nor energy, to read this entire summary, below is a recap of the more relevant tax measures that will impact our clients and friends.

Executive summary

1. No announcements were made with respect to the testamentary trust rules that have been the subject of a lot of discussion and controversy.

2. The Tax-Free Savings Accounts ("TFSA") contribution limits will increase from $5,500 to $10,000 effective January 1, 2015 with no indexation.

3. Currently, income that is eligible for the small business deduction is subject to a Federal tax rate of 11% on the first $500,000 of profits (subject to the normal "association" rules and taxable capital restrictions). The Budget proposes to decrease the 11% tax rate to 9%, and phase in such a reduction over 4 years. The dividend tax credit applicable to dividends paid from such after-tax profits will also be amended to compensate for the reduced small business tax rate.

4. The Budget announced its intention to study and consult with interested stakeholders on a review of the circumstances in which income from property should qualify as active business income eligible for the small business deduction.

5. The Budget proposes to increase the capital gains deduction amount for farmers and fisherman from $813,600 to $1M. It is interesting to note that such an increase is not applicable for the disposition of qualified small business corporation shares. Accordingly, the capital gains deduction available to farmers and fisherman will be the greater of $1M and the normal indexed amount for qualified small business corporation shares.

6. New charitable donation rules will exempt certain portions of capital gains from taxation when private corporation shares and/or real estate proceeds are used for a charitable donation.

7. The government is proposing another personal tax credit – the Home Accessibility Tax Credit – which will be available for "qualifying individuals" (people who are 65 years of age or older, or are eligible for the disability tax credit at any time in the particular taxation year). The new credit will also be available to "eligible individuals" (described further below) and will amount to a maximum of $10,000 of "eligible expenditures" per "eligible dwelling."

8. The Budget proposes to simplify the T1135 reporting process for years that begin after 2014. However, there will be no corresponding legislative change and ultimately, the intent is to simplify foreign asset reporting for anyone who has foreign assets less than $250,000 of cost.

9. The RRIF minimum withdrawal calculations are being adjusted so as to enable RRIFs to preserve more of their capital.

10. Specific amendments to Section 55 are being introduced to counter-act the result in *D&D Livestock*.

11. The current "failure to report income" penalty in subsection 163(1) is proposed to be amended to provide relief in limited circumstances.

12. The *Income Tax Act* will be amended to clarify that the Canada Revenue Agency (the "CRA") and the courts may increase or adjust any amount included in an assessment that is under objection or appeal at any time, provided that the total amount of the assessment does not increase.

13. The government announced its intention to implement the OECD's common reporting standard on July 1, 2017, allowing a first exchange of information in 2018.

14. The Budget announced its intention to exempt certain non-resident employers from employment withholdings for qualifying non-resident employees.

15. The Budget announced that its consultation on eligible capital property continues.

16. The captive insurance amendments that were introduced in the 2014 Budget are being amended to cast a wider net to such arrangements. The Department of Finance is inviting comments on these new measures.

17. The multi-national enterprise consultation continues in light of the government's participation in the OECD's BEPS initiative.

18. The tax deferral for patronage dividends that are received by eligible members from an agricultural cooperative will be extended to 2021 (such a tax deferral was scheduled to expire in 2016).

19. The government will introduce "balanced budget legislation". Such legislation "will ensure that the only acceptable deficit would be one that responds to a recession or an extraordinary circumstance – such as a war or natural disaster."

Analysis of tax measures

1. No announcement on testamentary trust measures

As our firm wrote about in a recent blog, there are certain significant technical issues that result in the income of certain "life interest trusts" becoming income of the deceased beneficiary upon the death of such a person. This results in a "misplaced tax liability" as a result of new subsection 104(13.4). There are other technical issues that are troublesome as well. Our firm has been very active, directly and indirectly, in responding to such issues.

We were hopeful that the Budget documents would announce some positive changes. However, the government chose not to make such announcements in the Budget. This is disappointing. However, we

understand that the government has not lost sight of these issues and we are hopeful that further progress will be made soon.

2. TFSA contribution limit changes

On January 1, 2013, the TFSA contribution limits increased to $5,500 subject to indexation. The Budget announced that the TFSA contribution limit will be increased to $10,000 as of January 1, 2015, with no further indexation. For people who can afford to contribute these annual amounts, this is a positive measure.

3. Tax rate reduction for small businesses

Currently, CCPCs that earn income from an active business in Canada are eligible for a reduced federal corporate tax rate of 11% as compared to the higher corporate rate. The lower rate must be shared amongst “associated corporations” and access to such rate is reduced on a straight-line basis for CCPCs having taxable capital employed in Canada between $10M and $15M. For example, in Alberta, the highest combined federal and provincial tax rate for CCPCs eligible for the small business deduction is 14% compared to the general rate of 25%.

The Budget proposes to further reduce the corporate tax rate for CCPCs by another 2%. In addition, the dividend gross-up and dividend tax credits for non-eligible dividends (dividends that are paid by CCPCs out of their retained earnings and that are not paid out of the general rate income pool) will be adjusted so as to preserve tax integration.

To summarize, the amendments to the federal tax rate, dividend gross-up and dividend tax credit will be phased in as follows:

	2015	**2016**	**2017**	**2018**	**2019**
Small business tax rate (%)	11.0	10.5	10.0	9.5	9.0
Gross up (%)	18.0	17.0	17.0	16.0	15.0
Dividend tax credit (%)	11.0	10.5	10.0	9.5	9.0

Obviously, personal tax rates on non-eligible dividends will be affected. From an integrated basis (meaning tax paid both corporately, and ultimately personally, from dividends paid out of corporate retained earnings), the overall tax on dividends paid from retained earnings that have been accumulated from active business income, subject to the small business deduction, should not change by much. However, CCPCs that earn investment income and ultimately pay such after-tax income out to its personal shareholders as non-eligible dividends will face an overall tax increase because of the increased tax rate on non-eligible dividends. Our calculation of the increased non-eligible dividend rates are as follows for Alberta and BC individual shareholders:

	2015	**2016**	**2017**	**2018**	**2019**
Alberta	29.36%	31.04%	32.22%	33.28%	33.15%
BC	37.98%	35.93%	36.52%	36.94%	37.33%

Overall, our firm is pleased with these measures, but ultimately, shareholders of CCPCs will need to monitor dividends paid from retained earnings that have accumulated from the taxation of investment income so as to manage the overall tax increase effectively.

4. A review of the circumstances in which income from property should qualify as active

business income eligible for the small business deduction

Currently, investment income is taxed differently than business income for CCPCs. In general, investment income is subject to the higher corporate tax rate and also subject to the refundable dividend tax on hand (“RDTOH”) regime which, overly simplified, does not enable investment income earned by a CCPC to benefit from tax deferral (unlike business income), since the recovery of the RDTOH requires taxable dividends to be paid to its individual shareholders.

A common question often arises in practice as to whether certain types of income are investment income or business income. For example, is income earned from the rents of a self-storage or campground business of a CCPC business income or investment income? One would automatically think that it is business income. However, most tax geeks, such as me, would suggest that such an activity involves deriving income from property (and thus investment income) and no tax deferral would be available.

The Budget announced that it is entering into a review of the circumstances in which income from a business, the principal purpose of which is to earn income from property, should qualify as active business income. The government is inviting interested parties to submit comments by August 31, 2015.

Overall, we applaud this review and will likely provide comments to the government. There are many circumstances where we believe that the type of business income being generated should not be taxed differently than active business income, and we intend to provide such examples in our submission.

5. Increased capital gains deduction for farmers and fisherman

Currently, the lifetime capital gains deduction is $813,600 for individuals who dispose of qualified small business corporation shares and qualified farm or fishing property (and indexed to inflation for future years). The Budget proposes to increase the lifetime capital gains deduction to apply to up to $1M of capital gains realized by an individual on the disposition of qualified farm or fishing property. Specifically, the capital gains deduction for qualified farm or fishing property will be the greater of:

a) $1M; and

b) the indexed lifetime capital gains deduction applicable on the disposition of qualified small business corporation shares.

This measure will apply to dispositions of qualified farm or fishing property that occur on or after April 21, 2015. In addition, the $1M limit in (a) above is not indexed to inflation.

We have a couple of comments on this measure. First, it is curious as to why the increased capital gains deduction is limited to only farmers and fisherman, and not for persons who own shares of qualified small business corporations. We aren’t exactly sure why the government decided on such a limitation. However, this leads to our second comment. The benefit realized by farmers and fisherman under this proposal is immediate, but other taxpayers will catch up overtime as the indexation of the capital gains deduction for qualified small business corporation shares reach $1M eventually.

Accordingly, farmers and fisherman may want to consider planning to take advantage of this new increased limit.

6. Donations involving private corporation shares or real estate

A number of years ago, the government introduced legislation (under paragraph 38(a.1) of the *Income Tax Act* that exempts from taxation realized capital gains when donations of publicly traded securities are gifted directly to registered charities. Subsequent to the introduction of such rules, there have been many commentators who have suggested that donations of real estate and private corporation shares to registered charities should also be subject to a similar capital gains exception. The government has resisted introducing such measures until now.

The Budget proposes to provide an exemption from capital gains tax in respect of certain dispositions of private corporation shares and real estate. The exemption will be available where:

a) cash proceeds from the disposition of the private corporation shares or real estate are donated to a qualified donee within 30 days after the disposition; and

b) the private corporation shares or real estate are sold to a purchaser that is dealing at arm's length with both the donor and the qualified donee to which cash proceeds are donated.

The exempt portion of the capital gain will be determined by reference to the proportion that the cash proceeds donated is of the total proceeds from the disposition of the shares or real estate. Anti-avoidance rules will ensure that the exemption is not available in circumstances where, within five years after the disposition:

a) the donor (or a person not dealing at arm's length with the donor) directly or indirectly reacquires any property that had been sold;

b) in the case of shares, the donor (or a person not dealing at arm's length with the donor) acquires shares substituted for the shares that had been sold; or

c) in the case of shares, the shares of a corporation that had been sold are redeemed and the donor does not deal at arm's length with the corporation at the time of the redemption.

Where the anti-avoidance rules apply, the exemption will be reversed by including the previously exempted amount in the income of the donor in the year of the re-acquisition by the donor (or the non-arm's length person) or the redemption.

This new rule will apply to donations made in respect of dispositions occurring after 2016. It will be interesting to see, once the proposed legislation is released, whether the exempted capital gain will increase the capital dividend account of a corporate donor.

Overall, we applaud these new proposals. Individuals who are philanthropically inclined should plan to take advantage of these new proposals. The tax savings from the proposed exemption, together with the donation tax credit/deduction and the potential addition to capital dividend account, could be significant.

7. Home Accessibility Tax Credit

The government is introducing yet another personal tax credit. The proposed non-refundable credit will provide tax relief of 15 per cent, on up to $10,000 of eligible expenditures per calendar year, per qualifying individual, to a maximum of $10,000 per eligible dwelling.

The below is a partial copy of the material from the Budget documents:

Seniors and persons with disabilities will be considered qualifying individuals for the purposes of the Home Accessibility Tax Credit and will be able to claim the credit. For the purposes of this credit:

- *seniors are individuals who are 65 years of age or older at the end of the particular taxation year; and*

- *persons with disabilities are individuals who are eligible for the Disability Tax Credit at any time in a particular taxation year.*

Eligible individuals will also be eligible to claim the Home Accessibility Tax Credit. For the purposes of this credit, an eligible individual, in respect of a qualifying individual, will be an individual who has claimed the spouse or common law partner amount, eligible dependant amount, caregiver amount, or infirm dependant amount for the qualifying individual [for the taxation year subject to specific rules beyond the scope of this summary].

Where one or more qualifying individuals or eligible individuals make a claim in respect of an eligible dwelling, the total of all amounts claimed by the qualifying individual(s) and eligible individuals for the year in respect of the eligible dwelling must not exceed $10,000.

An eligible dwelling, which includes the land on which the dwelling is situated, must be the principal residence of the qualifying individual at any time in the taxation year.

In general, a housing unit will be considered to be a qualifying individual's principal residence where it is ordinarily inhabited (or is expected to be ordinarily inhabited within that taxation year) by the qualifying individual, and it is owned (either jointly or otherwise) by the qualifying individual or the qualifying individual's spouse or common-law partner.

For the purposes of the Home Accessibility Tax Credit, a qualifying individual may have only one principal residence at any time, but may have more than one principal residence in a taxation year (e.g., in a situation where an individual moves in the taxation year). In situations where a qualifying individual has more than one principal residence in a taxation year, the total eligible expenditures in respect of all such principal residences of the qualifying individual will be subject to the $10,000 limit.

In the case of condominiums and co-operative housing corporations, the credit will be available for eligible expenditures incurred to renovate the unit that is the qualifying individual's principal residence, as well as for the qualifying individual's share of the cost of eligible expenditures incurred in respect of common areas.

In the case where a qualifying individual does not own a principal residence, a dwelling will also be considered to be an eligible dwelling of the qualifying individual if it is the principal residence of an eligible individual, in respect of the qualifying individual and the qualifying individual ordinarily inhabits that dwelling with the eligible individual.

Qualifying or eligible individuals who earn business or rental income from part of their principal residence will be allowed to claim the credit for the full amount of eligible expenditures made in respect of the qualifying individual's personal-use areas of the residence. For expenditures made in respect of common areas or that benefit the housing unit as a whole, the administrative practices ordinarily followed by the Canada Revenue Agency to determine how business or rental income and expenditures are allocated between personal use and income-earning use will apply in establishing the amount qualifying for the credit.

Expenditures will be eligible for the Home Accessibility Tax Credit if they are made or incurred in relation to a renovation or alteration of an eligible dwelling, provided that the renovation or alteration:

• allows the qualifying individual to gain access to, or to be more mobile or functional within, the dwelling; or

• reduces the risk of harm to the qualifying individual within the dwelling or in gaining access to the dwelling.

The improvements must be of an enduring nature and be integral to the eligible dwelling. Examples of eligible expenditures include expenditures relating to wheelchair ramps, walk-in bathtubs, wheel-in showers, and grab bars. Eligible expenditures will include the cost of labour and professional services, building materials, fixtures, equipment rentals, and permits. Items such as furniture, as well as items which retain a value independent of the renovation (such as construction equipment and tools), would not be integral to the dwelling and expenditures for such items will therefore not qualify for the credit.

The following are examples of other expenditures that will not be eligible for the Home Accessibility Tax Credit;

• expenditures made with the primary intent of improving or maintaining the value of a dwelling;

• the cost of routine repairs and maintenance normally performed on an annual or more frequent basis;

• expenditures for household appliances and devices, such as audio-visual electronics;

• payments for services such as outdoor maintenance and gardening, housekeeping or security; and

• the costs of financing a renovation (e.g., mortgage interest costs).

The Home Accessibility Tax Credit will not be reduced by any other tax credits or grants to which a qualifying or eligible individual is entitled under other government programs. For instance, in the case of an individual who claims an eligible expenditure that also qualifies for the Medical Expense Tax Credit, the individual will be permitted to claim both the Home Accessibility Tax Credit and the Medical Expense Tax Credit in respect of that expenditure. Expenditures that are reimbursed, or are expected to be reimbursed, other than through a government program, will not be eligible.

Expenditures will not be eligible for the Home Accessibility Tax Credit if they are for goods or services provided by a person not dealing at arm's length with the qualifying or eligible individual, unless that person is registered for Goods and Services Tax/Harmonized Sales Tax purposes under the Excise Tax Act.

The Home Accessibility Tax Credit will apply in respect of eligible expenditures for work performed and paid for and/or goods acquired after 2015. Any eligible expenditure claimed for the Home Accessibility Tax Credit must be supported by a receipt.

While the above Budget summary is informative, it illustrates that the introduction and administration of personal tax credits is complex and burdensome. We have written about this before. Notwithstanding, the introduction of this credit, from a policy intent, is admirable and if it can assist seniors or disabled people to live further in their own homes then that is excellent.

8. T1135 reporting simplification

The T1135 reporting issues and challenges have been much discussed and reported on. We have discussed such issues previously in a number of our blog postings.

While there are no legislative amendments being proposed in the Budget to “fix” the issues, the government used the opportunity to announce that the CRA is developing a new T1135 form, which will simplify the reporting of foreign assets for people who have such assets with a cost between $100,000 to $250,000. For people with assets in excess of $250,000, the new “normal” reporting rules will still apply.

Overall, this is a positive move. However, it would have been better if the government introduced a legislative amendment to change the law to increase the foreign reporting requirement for persons who have foreign assets with a specified cost in excess of $250,000. As mentioned, the reporting requirement, although now simplified, still exists for people who have foreign assets with a specified cost of $100,000 or more.

9. Changes to the minimum withdrawal amounts for RRIFs

Current legislation requires RRSPs to be withdrawn or converted to a RRIF in the year that the annuitant turns age 71. Minimum amounts must be withdrawn annually from the RRIF which ultimately exposes such withdrawn amounts to tax.

The Budget documents state as follows:

The existing RRIF factors were determined on the basis of providing a regular stream of payments from age 71 to 100 assuming a seven per cent nominal rate of return on RRIF assets and indexing at one per cent annually. The factors are capped at 20 per cent for ages 94 and above to ensure that the RRIF may continue for the life of the holder (or the holder’s spouse or common-law partner).

Budget 2015 proposes to adjust the RRIF minimum withdrawal factors that apply in respect of ages 71 to 94, on the basis of a five per cent nominal rate of return and two per cent indexing. These assumptions are more consistent with long-term historical real rates of return on a portfolio of investments and expected inflation. The new RRIF factors will permit holders to preserve more of their RRIF savings in order to provide income at older ages, while continuing to ensure that the tax deferral provided on RRSP/RRIF savings serves a retirement income purpose. Table A5.2 shows the existing and proposed new RRIF factors. There will be no change to the minimum withdrawal factors that apply in respect of ages 70 and under, which will continue to be determined by the formula 1/(90 – age).

The new RRIF factors will apply for the 2015 and subsequent taxation years. To provide flexibility, RRIF holders who at any time in 2015 withdraw more than the reduced 2015 minimum amount will be permitted to re-contribute the excess (up to the amount of the reduction in the minimum withdrawal amount provided by this measure) to their RRIFs. Re-contributions will be permitted until February 29, 2016 and will be deductible for the 2015 taxation year.

Overall, we are pleased with these new minimum RRIF withdrawal rules which will enable the RRIF annuitant to preserve more of their capital that is subject to a tax deferral.

10. Section 55 amendments

Section 55 of the *Income Tax Act* is one of the most complex provisions in the Act. Overly simplified, it

prevents an otherwise tax-free dividend paid to a corporation and treats the amount as proceeds of disposition (resulting in a capital gain) to the extent that the tax-free inter-corporate dividend was paid and the fair market value of the share of the corporation was reduced thereby resulting in reduced tax on an otherwise disposition of that share. Section 55 does not apply to the extent that the corporate payer paid such amounts out of its “safe income.”

The Tax Court of Canada, in its recent decision in *D&D Livestock*, decided in favour of a taxpayer who calculated its “safe income” in a novel way. The government was obviously not amused and is introducing legislation to prevent such future planning. The balance of the proposed amendments are beyond the scope of this summary, but suffice it to say that Section 55 will continue to be one of the most complex provisions in the Act.

11. Amendments to the Failure to Report Income penalties

Under current law, penalties may apply when a taxpayer fails to report all of their income on their income tax return. Where a taxpayer fails to report an amount of income in a taxation year and had failed to report an amount of income in any of the three preceding taxation years, the taxpayer is liable to a penalty equal to 10 per cent of the unreported income for that taxation year under subsection 163(1) of the *Income Tax Act* (the penalty is actually 20 per cent if the CRA imposes a parallel 10 per cent penalty under provincial legislation).

Another penalty (the “gross negligence” penalty), under subsection 163(2) of the *Income Tax Act*, applies if the taxpayer knew or, under circumstances amounting to gross negligence, ought to have known that an amount of income should have been reported. The amount of this penalty is generally equal to 50 per cent of the understatement of tax payable (or the overstatement of tax credits) related to the omission. The penalty for repeated failure to report income does not apply if this penalty applies.

The Budget documents state the following:

The repeated failure to report income penalty can sometimes be disproportionate to the actual associated tax liability, particularly for lower income individuals. In some cases, it can also result in a greater penalty than would be levied if the gross negligence penalty applied.

Budget 2015 proposes to amend the repeated failure to report income penalty to apply in a taxation year only if a taxpayer fails to report at least $500 of income in the year and in any of the three preceding taxation years. The amount of the penalty will equal the lesser of:

a) 10 per cent of the amount of unreported income; and

b) an amount equal to 50 per cent of the difference between the understatement of tax (or the overstatement of tax credits) related to the omission and the amount of any tax paid in respect of the unreported amount (e.g., by an employer as employee withholdings).

No changes are proposed to the gross negligence penalty, which will continue to apply in cases where a taxpayer fails to report income intentionally or in circumstances amounting to gross negligence. This measure will apply to the 2015 and subsequent taxation years.

Our firm has plenty of experience with the application of subsection 163(1) penalties. We agree with the government that the application of these penalties can often times be disproportionate to the amount of tax at stake. Accordingly, we applaud this change but wish that the government would have gone further.

For example, it would be better if the minimum amount for the application of subsection 163(1) would be, say, $10,000 instead of the proposed $500. It should be noted also that the current subsection 163(1) regime will continue to apply to assessment of the 2014 tax returns, which many Canadians are busy preparing at this moment. Notwithstanding, we are happy to see this proposed change.

12. Alternative arguments in support of assessments

The Budget documents state the following:

An income tax assessment is a calculation of a taxpayer's total tax liability for a particular taxation year. Long-standing jurisprudence has held that on appeal from a tax assessment, the question to be answered is, generally, whether the Canada Revenue Agency's assessment is higher than mandated under the Income Tax Act. The understanding in such an appeal was that, although the total amount from all sources that is assessed cannot increase after the expiration of the normal reassessment period, the basis of the assessment could change. This would allow, for instance, a reduced liability in relation to one item included in the computation of an assessment to be offset by an increased liability in relation to another item.

Consistent with this principle, there is a specific provision in the Income Tax Act which provides that the Minister of National Revenue may advance an alternative argument in support of an assessment at any time after the normal reassessment period. The purpose of this provision is to allow the Minister to advance an alternative argument after the relevant reassessment period has expired. This process of raising arguments and counter-arguments "in the alternative" is a conventional part of the litigation process.

A recent court decision held that, while the basis of an assessment can be changed after the expiration of the normal reassessment period, each source of income is to be considered in isolation and the amount of the assessment in respect of any particular source of income cannot increase.

Budget 2015 proposes that the Income Tax Act be amended to clarify that the Canada Revenue Agency and the courts may increase or adjust an amount included in an assessment that is under objection or appeal at any time, provided the total amount of the assessment does not increase. Similar amendments are proposed to be made to Part IX of the Excise Tax Act (in relation to the Goods and Services Tax/Harmonized Sales Tax) and the Excise Act, 2001 (in relation to excise duties on tobacco and alcohol products) to help ensure consistency in administrative measures in federal tax statutes.

These measures will apply in respect of appeals instituted after Royal Assent to the enacting legislation.

Legislation overriding the Federal Court of Appeal decision in Last v R. to allow for alternative adjustments in support of assessments causes significant concerns for taxpayers because such amendment will increase delay, uncertainty and complexity in tax disputes, and will consequently increase the time and costs for taxpayers pursuing tax disputes. While it does not appear that the government will be able to increase an assessment that is in dispute as a result of this proposed legislation, the tax benefit of an adjustment in a taxpayer's favour may be reduced or eliminated by other unrelated adjustments in the government's favour as a result of this amendment. An example of how this proposed legislation may apply is as follows:

Taxpayer is reassessed on the basis that a disposition of property occurred on income rather than capital account. Taxpayer appeals the reassessment to the Tax Court of Canada on the basis of advice of the strength of the argument that he disposed of the property on capital account. In reply to the

taxpayer's appeal, the government might appreciate that the taxpayer's argument is strong and therefore look for a new unrelated alternative adjustment that it can make by denying the deductibility of various business expenses incurred by Taxpayer in the same taxation year. Consequently, Taxpayer would be required to argue both the first issue (income vs. capital) and the new unrelated second issue (deductibility of business expenses) subsequently raised by the government.

Going forward, taxpayers and their advisers will have to carefully consider what other adjustments may be made in the Minister's favour before deciding whether to pursue a tax dispute. A dispute of any issue will require an examination of every unrelated issue that may exist in the same taxation year. For taxpayers with complex or uncertain tax positions that are unrelated to amounts in dispute this exercise of identifying potential adjustments in the government's favour may significantly increase the time, costs and uncertainty involved in the tax dispute resolution process – a process that is already lengthy, expensive and uncertain.

Presumably, Courts may award costs, regardless of the outcome, to a taxpayer presented with a new issue on their appeal. A taxpayer should be able to determine the scope of litigation at the outset and should not have to guess at every potential alternative adjustment that may be later argued by the government.

13. Implementation of the OECD Common Reporting Standard

Our firm has written and lectured extensively on the United State's version of information exchange – FATCA. We have also commented on the OECD's initiative to follow FATCA with its "Common Reporting Standard" ("CRS"). The OECD announced in October 2014 that 51 countries were committed to implementing the CRS. Canada was one of the countries that announced its commitment.

The Budget confirmed Canada's commitment to CRS and stated the following:

Canada proposes to implement the common reporting standard starting on July 1, 2017, allowing a first exchange of information in 2018. As of the implementation date, financial institutions will be expected to have procedures in place to identify accounts held by residents of any country other than Canada and to report the required information to the Canada Revenue Agency. As the Canada Revenue Agency formalizes exchange arrangements with other jurisdictions, having been satisfied that each jurisdiction has appropriate capacity and safeguards in place, the information will begin to be exchanged on a reciprocal, bilateral basis. Draft legislative proposals will be released for comments in the coming months.

This is big news. Our firm will have plenty to say about this initiative in the coming days and months. However, suffice it to say for now that those who thought FATCA was bad had better get ready for CRS. We now live in a time of automatic information exchange. Accordingly, the person who thinks that they will be able to hide their assets in a foreign jurisdiction and avoid tax on any resulting income is foolish. The clock is ticking for such people.

14. Exemption from employment withholdings for certain non-resident employers

Under current law, a non-resident employee that carries out their employment duties in Canada is subject to Canadian tax on such amounts. In addition, an employer, including a non-resident employer, is generally required (pursuant to the rules set out in subsection 153(1) of the *Income Tax Act* and Regulation 102 of the Regulations to the *Income Tax Act*) to withhold and remit amounts on account of the income tax liability of an employee working in Canada. However, for many non-resident employees,

such employment income is exempt from Canadian tax by virtue of a tax treaty that Canada may have with the non-resident's home country if certain specific conditions are met. Under current law, an employee specific waiver from withholding may be obtained by the employer in order to provide relief from such withholding. However, the waiver process can still be burdensome and time consuming.

In response to criticism about the waiver process, the Budget announced a new exception to the withholding requirements for payments by "qualifying non-resident employers" to "qualifying non-resident employees", in respect of payments made after 2015. The Budget documents explain this further:

An employee will be a qualifying non-resident employee in respect of a payment if the employee:

• is exempt from Canadian income tax in respect of the payment because of a tax treaty; and

• is not in Canada for 90 or more days in any 12-month period that includes the time of the payment.

In order to be a qualifying non-resident employer, an employer (other than a partnership) must be resident in a country with which Canada has a tax treaty. In order for an employer that is a partnership to qualify, at least 90% of the partnership's income for the fiscal period that includes the time of the payment must be allocated to persons that are resident in a treaty country. In all cases, the employer must not carry on business through a Canadian permanent establishment of the employer in its fiscal period that includes the time of the payment and the employer must be certified by the Minister of National Revenue at the time of the payment. Certification may be denied or revoked if the employer does not meet the conditions described above or fails to comply with its Canadian tax obligations.

Although a qualifying non-resident employer will not be obligated to withhold under these circumstances, it will continue to be responsible for its reporting requirements under the Income Tax Act with respect to amounts paid to its employees. Certification will not affect the determination of a non-resident's Canadian tax liability. Employers will continue to be liable for any withholding in respect of non-resident employees found not to have met the conditions set out above. However, no penalty will apply to a qualifying non-resident employer for failing to withhold in respect of a payment if, after reasonable inquiry, the employer had no reason to believe, at the time of payment, that the employee did not meet the conditions set out above.

We applaud this initiative. This should make it simpler, in many cases, to relieve cross-border employers from the withholding obligations under Regulation 102.

15. Update on consultations

The Budget announced the following with respect to existing consultations or new consultations:

a) Eligible capital property regime consultation

As predicted in our Budget prediction blog, the Budget announced an update with respect to its ongoing consultation. The Budget did not say much other than it is the intention of the government to release detailed draft legislative proposals for stakeholder comment before their inclusion in a Bill.

b) Captive insurance amendments/consultation

The Budget documents stated the following:

The Government has become aware of alternative arrangements that are intended to achieve tax benefits similar to those that the 2014 amendment was intended to prevent. Under these alternative arrangements, the affiliate receives consideration with an embedded profit component (based upon the expected return on the pool of Canadian risks) in exchange for ceding its Canadian risks. The Budget 2014 amendment may not apply to these alternative arrangements if the affiliate does not enter into an insurance swap transaction that provides it with economic exposure to the Canadian risks. Although existing anti-avoidance or other rules in the Income Tax Act may apply to such alternative arrangements, such challenges can be time- consuming and costly. Accordingly, specific legislative action is proposed to clarify that these arrangements give rise to FAPI.

Budget 2015 proposes to amend the existing anti-avoidance rule in the FAPI regime that relates to the insurance of Canadian risks. This amendment is intended to ensure that profits of a Canadian taxpayer from the insurance of Canadian risks remain taxable in Canada. In particular, it will be amended so that:

- *a foreign affiliate's income in respect of the ceding of Canadian risks is included in computing the affiliate's FAPI; and*

- for these purposes, when an affiliate cedes Canadian risks and receives as consideration a portfolio of insured foreign risks, the affiliate is considered to have earned FAPI in respect of the ceding of the Canadian risks in an amount equal to the difference between the fair market value of the Canadian risks ceded and the affiliate's costs in respect of having acquired those Canadian risks.

This measure will apply to taxation years of taxpayers that begin on or after Budget Day.

The Government invites interested stakeholders to submit comments on this measure by June 30, 2015.

This is a very targeted measure and appears to be consistent with the intent of the 2014 Budget proposal.

c) Multinational enterprise consultation update

The Budget provided the following update:

Input from stakeholders on these issues has helped shape Canada's ongoing participation in the international discussions related to the OECD/G-20 BEPS project. The Government looks forward to the conclusion of the project and to discussions with the international community on the implementation of its recommendations.

The Government will proceed in this area in a manner that balances tax integrity and fairness with the competitiveness of Canada's tax system. Improving business tax fairness and competitiveness has been a central element of the Government's approach to fostering an environment in which businesses can thrive and compete in a global economy. Taxes are one of the main factors that drive investment decisions and the Government is committed to maintaining Canada's advantage as an attractive destination for business investment.

Accordingly, stay tuned appears to be the message!