Tax Executives Institute Meeting with CRA
December 3, 2013

Question 1: Vision 2020

We invite CRA to provide an update on its Vision 2020 initiative.

CRA Response:

The CRA Roadmap: Current Priorities for Service, Compliance and Integrity sets out a number of key initiatives that the CRA will implement over the next three years to advance core strategic directions. The initiatives are grouped under three headings:

- Improving service to make it easier to comply,
- Ensuring that all taxpayers pay their fair share, and
- Maintaining Canadians' trust.

With regard to improving service, the CRA will direct its efforts to initiatives related to providing convenient, secure online services, tailored help for those that need it, and helping others help Canadians with access to clear, accurate information and timely services. The Agency is expanding its electronic services to allow taxpayers to file returns and make tax payments more easily by bringing many online transactions together in a one-stop shop service. The CRA is exploring ways to provide more direct assistance and information to businesses at key points in their lifecycle that will enable business owners to better, and more easily, fulfill their tax obligations. The CRA continues to acknowledge the role that third parties play in Canada's tax system in terms of influencing and enabling compliance and continues to enhance support to tax preparers to help them provide better service to their clients.

The CRA must also ensure that all taxpayers pay their share, giving Canadians confidence that the tax system is fair. The CRA is ensuring a level playing field for businesses through targeted and connected compliance activities and combatting costly non-compliance, such as international tax evasion and the underground economy. Some of the initiatives include broadly conducting compliance campaigns based on advanced analytics or using technology to tackle employer non-compliance.

Finally, the CRA will also direct its efforts in maintaining the trust that Canadians have in the Agency and Canada's tax system. The Agency recognizes that there is a connection between public trust and confidence in the CRA, and the effectiveness of our programs and services. As such, it is ensuring that our people continuously act with integrity and that information is safe in our systems. The CRA also believes that tax practitioners play an important part in ensuring the integrity of the tax system by ensuring Canadians receive sound tax advice and fair treatment.

By following this roadmap and vision for the future, the CRA has set the direction for strengthening and modernizing how the CRA provides services to Canadians and government.

Question 2: Risk-Based Audits

In response to question 12 in the 2012 liaison meeting agenda, CRA advised that it was too early to (1) draw conclusions with respect to the state of tax-risk governance and (2) share its findings and experiences on the risk-assessment process. Many large taxpayers have now completed the risk-assessment process and also experienced a post-risk-assessment audit. Taxpayer's anecdotal descriptions of their experience with both the risk-assessment process and the first post-risk-assessment audit have varied widely. Would CRA provide an update on its observations and summarize trends or conclusions for the initiative? Can CRA provide a summary of feedback from taxpayers and field auditors?

CRA Response:

As of October 2013, the CRA has held over 175 face-to-face meetings with officials from large businesses. In these meetings, we have provided taxpayers with a very detailed breakdown of how we manage the risk assessment of our large population, including relevant environmental factors, our new Approach to Large Business Compliance, the benefits to both taxpayers and CRA in engaging in this new approach, as well as the role that tax intermediaries can play in creating open and transparent relationships. This initiative is in its third year, and we plan to conduct additional face to face meetings. To this point, the reaction from taxpayers has been very positive. They have been very engaged in the process, and are always eager to learn about their risk rating and how it is determined. It has been so well received that many taxpayers are hoping for more meetings in future years. We hope to explore this option as resources permit. Taxpayers are better able to understand their risk rating and are very appreciative of the opportunity to openly discuss their situation. At the same time, our auditors are keen to discuss relevant tax positions and to learn from them, which will only help improve CRA's future risk assessment approach.

Question 3: Forms, Publications, Electronic Services, e-Filing, & Miscellaneous, including Carryover Items from Prior Years

a. Form T5018. In response to question 8 in the 2012 liaison meeting agenda, CRA said that it would consider permitting a joint venture to report payments made to contractors for construction services on one Form T5018 (Statement of Contract Payments) slip rather than requiring each co-venturer to issue separate T5018s for their proportionate share of payments to the contractors. We invite CRA to advise whether these changes will be implemented and the expected timing for implementation.

CRA Response:

At this time the CRA will not proceed with the TEI proposal as there is no legal provision under the ITA for the Minister to recognize a joint venture election given the provisions that stipulate "each person or partnership… …shall make an information return in the prescribed form in respect of that amount". We note that the formation of a joint venture binds various parties for a common purpose but does not create a new entity. The joint venture is not a "person or

partnership" under the ITA and the requirement of section 238(2) is on the person or partnership to file the information return in the prescribed form. As such, in the context of the ITA, the proposal is not workable. Further, the proposal was brought forward in respect of reducing in burden, but the case made is not clear. Under the Excise Tax Act (ETA), requirements for filing of GST/HST return can be up to monthly and burden is reduced through the election of an operator. In contrast, T5018 filing is an annual requirement and as such does not appear to present the same burden as that which could exist under the more frequent filing requirements of the ETA.

b. Form T5013. In response to question 1(a) in the 2012 liaison meeting agenda, CRA said it is enhancing the electronic return filing system to permit Form T5013 (Statement of Partnership Income) to be filed electronically through the My Business Account (MyBA) portal. The target date for the enhancement to the electronic filing system was January 2014. We invite an update on the expected timing for the added functionality. In addition, please provide an update on the timing for adding the ability to review previously filed Form T5013s online.

   Finally, CRA acknowledged in its response to question 13 in the 2012 liaison meeting agenda that Schedule 50 (Partner's Ownership and Account Activity) of Form T5013 should be modified. Subsequent to the meeting another potential issue about the current format was discovered. Specifically, columns 10 to 13 of Schedule 50 are added to calculate each partner's At-Risk Amount (ARA) at the end of the fiscal period in column 14 [50-440]. Presumably, columns 10 to 12 are equivalent to the additions to ARA adjustments described in paragraphs 96(2.2)(a) to (b.1) of the Income Tax Act (ITA). Column 12 [50-420] is labeled "Partner's share of the fiscal period's resource expenses" and presumably represents the addition to ARA described at paragraph 96(2.2)(b.1), but that paragraph requires the addition of the "amount referred to in subparagraph 53(1)(e)(viii)," which are the proceeds of disposition in respect of resource-related properties rather than a "Partner's share of the fiscal period's resource expenses." Moreover, the "Partner's share of the fiscal period's resource expenses" is already taken into account in the calculation of the adjusted cost base (ACB) (i.e., as a reduction of the ACB of a partnership interest at subparagraph 53(2)(c)(ii)). Accordingly, there would be no need to deduct that amount from ARA a second time. Finally, column 12 on the Form is an addition rather than a subtraction, which is contrary to the ITA. Thus, the description of column 12 [50-420] is misleading or incorrect. Would CRA consider modifying Form T5013 to label Column 12 [50-420] as the "amount referred to in subparagraph 53(1)(e)(viii)" rather than "Partner's share of the fiscal period's resource expenses"? We invite CRA's response.

CRA Response:

The ability to electronically file the T5013 Package will be available starting in January 2014. This means taxpayers and their representatives will be able to file electronically: (i) the T5013 FIN Partnership Financial Return and Schedules; as well as the T5013 Statement of Partnership Income, and Information Slips and Summary. For more information please visit our website http://www.cra-arc.gc.ca/tx/bsnss/tpcs/slprtnr/prtnrshp/menu-eng.html.

At this point in time, we have no update on the timing of when CRA can provide online options to provide details of previously filed T5013 information. We continue to explore the option but further analysis and consultations are required to develop a timeline for delivery.

In response to stakeholder concerns, we have changed the title of box 420 in the 2013 version of Schedule 50 to avoid confusion. The title is now "*Partner's share in certain reductions of resource expenses for the fiscal period*".

We also improved the explanation in the 2013 version of the partnership guide by adding the following paragraph under the title "*The limited partner's ARA*":

> *b.1 are certain amounts deemed under subsections 66.1(7) CEE, 66.2(6) CDE, and 66.4 (6) COGPE, for the limited partner for the fiscal period, that relate to certain amounts receivable by the partnership as consideration for property or services or as proceeds of disposition of Canadian resource property*

c. Electronic Filing of Foreign Reporting Forms. In response to question 1(b) in the 2012 liaison meeting agenda, CRA stated that the International Tax Data Working Group is reviewing enhancements to the filing system in order to permit certain foreign reporting forms to be filed electronically. In addition, the 2013 Federal Budget states that the government will modify the filing system to accommodate electronic filing of Form T1134 (*Information Return Relating to Controlled and Not-Controlled Foreign Affiliates*). We invite an update on this initiative, including the expected timing of when taxpayers will be able to file T1134s and T106s (*Information Return of Non-Arm's Length Transactions with Non-Residents*) electronically.

CRA Response:

As outlined in Economic Action Plan 2013 (EAP 2013), Canadians who hold foreign property with a cost of over $100,000 will be required to provide additional information to the CRA starting with the 2013 taxation year. The criteria for those who must file a Foreign Income Verification Form (Form T1135) has not changed; however, the new form has been revised to include more detailed information on each specified foreign property. The CRA will make improvements to help taxpayers meet their filing obligations with respect to Form T1135, including the ability to file the form electronically in the future. In support of EAP 2013, CRA's focus is to make the system changes necessary to allow electronically filing of Form T1135. Once implemented, other foreign reporting forms such as the T106 (Information Return of Non-Arm's Length Transactions with Non-Residents) and T1134 (Information Return Relating to Controlled and Not-Controlled Foreign Affiliates) will be considered for migration to a similar electronic filing system.

d. Exchange of electronic information. Has CRA made any progress in developing a mechanism for secure (two-way) exchange of electronic information and correspondence between taxpayers and CRA, especially during audits? Many companies are digitizing

records and moving to a paperless environment as much as possible. Interactions with CRA would be significantly enhanced, the flow and speed of the audit process would be improved, and a significant amount of wasted paper would be eliminated if taxpayers and CRA corresponded electronically. Such communication is available through the IronPort encryption internet application used by the Québec Ministry of Taxation (MRQ) and other similarly secure internet sites in other tax jurisdictions.[1]

CRA Response:

The CRA has established a strong foundation in E-Services and continues to seek ways to expand the range of functions that taxpayers and representatives can do online, as well as to make these services as simple and intuitive as possible. The Agency remains focused on making our E-Services the channel of choice for our clients.

One-way secure data exchange is presently possible for business owners and their representatives using the Electronic Transfer of Accounting Data (ETAD) service found within the My Business Account and the Represent a Client portals. This service allows clients to submit accounting data to the CRA during business audits. Also, the ability to securely send the CRA electronic copies of supporting documentation and receipts was launched in October 2012, with the Submit Documents service, for the T2 Corporation Assessing Review Program. This service, found within the CRA secure portals, was expanded in April 2013 to the T1 Processing Review program and beginning in April 2014 Submit Documents will be available for the Office Audit and for the Benefits Eligibility / Entitlement programs. Submit Documents is tentatively planned to become available to GST Audit programs in October 2014 and T2 Audit in October 2015 with the services for additional specialty audits, such as Foreign Reporting, being added after October 2015.

Beginning in April 2013, the CRA began offering business owners, or their delegated authorities, the ability to receive correspondence from the CRA electronically using the Manage Online Mail feature of the My Business Account Portal. The Manage Online Mail service advises Canadians, via electronic notification, that they have new correspondence or an action request from the CRA that they need to view in our secure portal. Further expansion of this service, to include discounters and other types of representatives, is planned for 2014.

Beyond the Electronic Transfer of Accounting Data (ETAD), Submit Documents and Manage Online Mail service initiatives, the CRA is actively analyzing electronic paths that would allow for the two-way exchange of secure electronic information and correspondence between taxpayers, their authorized representatives and the CRA. The protection of secure and confidential information is a priority for the Agency. We are committed to implementing and enhancing services that allow for the timely two-way exchange of electronic information and correspondence between taxpayers and CRA, including during audits, that is both functional and secure.

[1] Over the past several years, the U.S. Internal Revenue Service has been implementing a secure email system to correspond with large-file taxpayers during audits. All or nearly all such cases now employ that system.

e. Income Tax Folios. We invite CRA to provide an update on replacing the interpretation bulletins (ITs) and information circulars (ICs) with Income Tax Folios (*i.e.*, the Folios initiative).

In addition, CRA's stated policy with respect to the application of income tax interpretation bulletins was set forth in the Application section of the "IT - INDEX - Interpretation Bulletins and Technical News Index" and in the Application section of many Interpretation Bulletins.

The policy was, as follows:

> *An interpretation described in a bulletin applies as of the date the bulletin is published, unless otherwise specified. When there is a subsequent change in a previous interpretation or position, and the change is beneficial to taxpayers, it is usually effective for all future assessments and reassessments. However, if the change is not favourable to taxpayers, it is normally effective for the current and subsequent taxation years or for transactions entered into after the date of the bulletin.*

Will similar rules of application apply to Folios?

CRA Response:

Just as a quick clarification, Information Circulars are not being replaced by the Income Tax Folios. The Folios are only replacing income tax interpretation bulletins and income tax technical news publications.

As the TEI is likely aware, the Folio series was launched with eleven publications at the end of March, 2013. At present, there are an additional 34 Folio Chapters in various stages of completion. Many of these (approximately half) are being prepared by private tax practitioners as part of our pilot project with external contributors. For the most part, the folios in the pipeline deal with topics that were identified as priorities during our web analysis and consultation phase early on in the formative stages of the initiative.

There are no specific timelines regarding the publication of upcoming folios other than to confirm that each will be published as it is ready. There is one that has completed both internal and external technical review, so it is almost ready to go through the translation stage. Another has undergone the first stage of internal technical review, so it is moving along as well.

Turning to the second part of the question about application, it should be pointed out that Folios are not intended to be the forum for announcing new positions. Anything contained in a Folio will already be in the public domain. So, it is never really a question of when a Folio is applicable. The better question is, "When is a new position applicable?"

Because the Folios can be revised more easily, they will be updated more frequently than the Bulletins. Essentially, they can be updated as often as necessary to reflect new or changed

content. This means that where there is an effective date relevant to a change, it will be communicated in the publication. Where a change is legislative, the effective date will be determined by the Department of Finance. Other changes, such as changes in a previous interpretation or position, will be publicly announced, whether at a conference or in a technical interpretation and shortly thereafter, published as a folio update along with the effective date. Typically, as was described in the policy you mention, when a change in interpretation is not considered favourable to taxpayers, it only becomes effective in a subsequent year, which would be specified when the new position is announced. The advent of the Folios is not expected to change this approach.

f. Form RC18 "Calculating Automobile Benefits for 2012." In Form RC18, the first amount entered is described as the "cost of automobile you provided (must be at least equal to the fair market value." Subsection 6(2) of the ITA, however, refers solely to "cost" and does not refer to fair market value. Hence, TEI questions why — when making the determination of a reasonable automobile standby charge — Form RC18 states that the cost of the automobile must be at least equal to the fair market value. We invite CRA's explanation.

CRA Response:

In most cases, the cost of the automobile to the employer reflects its fair market value (FMV) as it was acquired through an arm's-length transaction. Subsection 6(2) of the ITA specifies that the cost of the automobile is to be used in calculating the standby charge, and not the FMV. During our meeting we discussed the fact that although the ITA does not define the term "cost", which takes its meaning from jurisprudence and ordinary commercial principles, generally, "cost" includes the amount laid-down to acquire it, including all legal, accounting, engineering or other fees incurred. It is CRA's published position that cost should reflect the true consideration exchanged. Some employers are under the misunderstanding that the "cost of automobile" that is referenced on Form RC18, for purposes of calculating the employee's standby charge for the use of an employer provided automobile, is the amount the employer paid for the automobile even if that automobile was not acquired through an arms-length transaction. The reference to FMV was added to the RC18 to address situations where the employer acquired the automobile for less than FMV in situations such as non-arms-length transactions. To reflect our discussions, the wording on both the hard copy and the web-site version of the RC18 as well as the Automobile Benefits Online calculator is being updated. The term "must" is being replaced by "generally" in the 2014 versions of these documents, i.e., "Cost of automobile you provided (generally equal to the fair market value at the time of acquisition, including GST/HST and PST)".

g. Section 3 of the Revised T1134 Summary. Form T1134 requires disclosure of each corporation that is not dealing at arm's length with the reporting entity and that has an equity ownership percentage in any foreign affiliate of the reporting entity. In a tiered corporate structure, the requirement produces a significant amount of redundant reporting. CRA has indicated that it is considering a policy change to relieve redundant reporting. We invite CRA

to provide an update on whether the burden of redundant reporting in respect of T1134 may soon be diminished or eliminated.

CRA Response:

The CRA has recently developed administrative relief for section 3 of the T1134 Summary to address concerns raised by the tax community. The CRA's Website has been updated accordingly. The administrative relief is as follows:

> *If you are reporting on one or more controlled foreign affiliates, Part I, Section 3 requires you to produce information on the organizational structure once for a group of persons that are related to each other. Under the old version of the form (T1134B), you were able to satisfy this requirement by submitting a group organizational chart that included the requested information. Now, Part I, Section 3 of the new T1134 requires you to enter information of the group's organizational structure to be entered into specific data fields.*
>
> *We understand that if you are reporting on a tiered structure of foreign affiliates in this new format, area B of Section 3 would require you to complete several lines of repetitive information. In order to reduce this filing burden, the CRA will now accept information limited only to each foreign affiliate of the reporting entity that has a direct equity percentage in any other foreign affiliate of the reporting entity. If the foreign affiliate of the reporting entity does not have a direct equity percentage in another foreign affiliate of the reporting entity, but does have an equity percentage, you are not required to provide information regarding this situation in area B of Section 3.*
>
> *In summary, when completing Part I, Section 3B, list the name and country code of the country of residence of each foreign affiliate of the reporting entity that has a direct equity percentage in any other foreign affiliate of the reporting entity. Include the foreign affiliate's equity percentage and direct equity percentage in the other foreign affiliate.*

Further information regarding the new administrative relief can be found on the CRA Website under the header "*Administrative relief for reporting on the organizational structure (Part I, Section 3)*" at http://www.cra-arc.gc.ca/tx/nnrsdnts/cmmn/frgn/1134-eng.html#AdministrativeRelief.

h. Form T1134 (Dormant or Inactive Affiliates). Until 2012, CRA afforded relief from filing Form T1134 in respect of dormant or inactive foreign affiliates (hereinafter the "Administrative Relief"). CRA defined a "dormant or inactive" foreign affiliate as one with less than $25,000 gross receipts during the year and less than $1 million in asset fair market value throughout the year. The 2012 revision to the Form T1134 instructions states that the *total* cost of all foreign affiliates must be less than $100,000 (hereinafter the "Aggregate $100,000 Threshold") for *any* foreign affiliate to be considered "dormant or inactive."

In response to a tax roundtable query at the May 2013 Canada Health and Life Insurance Association conference, CRA stated that the previous threshold for dormant or inactive foreign affiliates created a reporting gap between Form T1134 and Form T1135 (*Foreign Income Verification Statement*). TEI believes that the determination of dormancy and inactivity for reporting purposes should be an entity-by-entity determination rather than an aggregate determination. Moreover, the Aggregate $100,000 Threshold is impractically low. We urge CRA to consider reinstating the Administrative Relief. Will CRA consider making this change?

CRA Response:

The suggestion of determining dormancy or inactivity for reporting purposes on an entity-by-entity basis is not being considered by the CRA at this time because of fairness concerns. Undertaking such a practice would create inconsistency in thresholds among different taxpayers.

Section 233.3 of the ITA requires the reporting of "specified foreign property" where the total of all amounts, each of which is the cost amount to the reporting entity of such property, exceeds $100,000. The definition of "specified foreign property" does not include property that is a share in the capital stock or indebtedness of a non-resident corporation that is a foreign affiliate of the reporting entity for the purpose of section 233.4.

Section 233.4 of the ITA requires reporting of information regarding ALL foreign affiliates. In the past, in order to reduce this filing burden on taxpayers, the CRA administratively provided relief from filing this information for dormant or inactive foreign affiliates. The thresholds of this past administrative relief created a reporting gap between T1135 filing requirements and T1134 filing requirements.

Because the CRA continues to prioritize efforts to ensure compliance surrounding offshore tax matters, it was necessary to close this reporting gap to be consistent with the legislated thresholds. The $100,000 threshold is legislated in section 233.3 of the ITA, which is determined by the Department of Finance. For these reasons, the CRA is not considering the reinstatement of this administrative relief at this time.

i. <u>CRA Collections Policy.</u> Upon the issuance of a Notice of Assessment or Reassessment (NOA or NOR), the CRA accounting system will automatically offset that liability with any refund balance on hand from any tax or taxation year. As a result, when taxpayers receive the NOA or NOR (say, for an income tax audit) in the mail and promptly pay the liability, they often find that a GST refund has already been offset against the liability. As a result, the taxpayer's payment creates an overpayment that must either be reallocated between tax accounts or refunded to the taxpayer. CRA's offset practice thus creates significant reconciling issues for both CRA and taxpayers.

   In addition, some taxpayers report receiving calls from CRA collections officials even before receiving an NOA or NOR, let alone before the expiration of the 15-day grace period

afforded to make a prompt payment of the NOR or NOA without incurring an interest charge.

Would CRA consider reprogramming its standardized accounting system to delay automatic offsets of extant refunds against NORs or NOAs until at least 15 days elapse from the date an NOR or NOA is issued? The 15-day period corresponds to the grace period afforded to taxpayers to receive and promptly pay an NOR or NOA. In addition, since it is difficult for a taxpayer to respond to an inquiry from a CRA collections official prior to receipt of an NOR or NOA, we recommend that CRA consider refraining from calling large file taxpayers before 15 days have elapsed from the date of an NOR or NOA. We invite CRA's response.

CRA Response:

In April 2007, as a result of the 2006 Budget, amendments were made to the ITA to repeal paragraph 225.1(1)(e).

Section 225.1 of the ITA restricts the collection of unpaid amounts for which a taxpayer has been assessed under the Act where the taxpayer objects to or appeals from the assessment. In most cases, the Minister of National Revenue is precluded from taking any of various collection actions, listed in paragraphs 225.1(a) to (g), until either 90 days have passed since the assessment or any objection or appeal by the taxpayer has been disposed of.

Section 225.1 was amended by repealing paragraph (e), which has the effect of allowing the Minister to commence collection by way of deduction or set-off under section 224.1 on the day on which the notice of assessment is mailed.

- Individual and corporate income tax debts are subject to collection restrictions. As a result of the legislative amendments made in April 2007, the Minister has the legislative authority to offset credits, or issue a set-off under section 224.1, and apply any amounts received as a result of these actions to the debt; during the initial 90-day collection restriction period, or in the event that the taxpayer objects to or appeals an assessment. These are the only actions that can be taken during the 90-day collection restriction period, or in the event the taxpayer objects to or appeals an assessment. If a danger of loss is identified and a jeopardy order under section 225.2 is obtained, all collection and enforcement actions can be initiated notwithstanding the collection restrictions imposed.

- Source deduction debts assessed under the ITA, as well as GST/HST debts assessed under the ETA, are not imposed by collection restrictions. Consequently, all collection and enforcement collection actions can be initiated immediately once a notice of assessment or reassessment is mailed.

Generally speaking, a collection officer is not assigned to an account until after the notice of assessment or reassessment has been mailed to the taxpayer.

However, if the assessed amount is substantial, then the debt will be assigned to a collections officer in order for an assessment of the situation to be performed. As a result, the taxpayer may

receive a call from the assigned collections officer asking the taxpayer how they intend to address the debt. The options for individual or corporate income tax debts are; will the debt be paid and if so, when; will security be provided or will they appeal the assessment. The intent of this early intervention by a collection officer is to establish a point of contact should the taxpayer wish to discuss payment of the account before it becomes legally collectable. It should be noted that the CRA's collection policy for payroll and GST/HST debts is pay or secure. These amounts are immediately collectable once assessed. As a result, there could be situations where a taxpayer could be contacted by a collection officer before he has received his notice of assessment through the mail.

In addition, the April 2007 amendments also gave the Minister the authority to hold refunds if the taxpayer has not maintained their compliance requirements, i.e. filing all outstanding returns up to date. If a refund is available to a taxpayer and a return is not filed under the ITA, ETA, the Excise Act, 2001, and the Air Travellers Security Charge Act, the refund will not be paid, applied to another debt or set-off until the return is filed.

Accounting systems

While the accounting system does not provide a "grace period", it does allow for a period of time where interest will be forgiven in accordance with the forgiven interest legislation. The "forgiven interest" date that is shown on the notice of assessment is not meant to provide a grace period or delay collection activity.

The CRA recognizes that due to the timing of the receipt of a payment and the offset of a refund an overpayment situation can occur but in accordance with s. 224.1 of the ITA the accounting system does automatically offset credits to existing debts on an account.

Conclusion

The CRA will continue to act prudently to ensure that amounts owed are paid in the shortest time possible. This includes the offset of credits and the issuance of set-offs pursuant to s.224.1 of the ITA. Our business accounting systems have been enhanced to reflect the legislated authority afforded to the Minister. This reduces the risk of refunding credits where a debt exists, and also reduces the amount of interest would need to be paid if refunds were held for extended periods of time.

With respect to large tax debt assessments, the CRA will continue be diligent in attempts to obtain the greatest tax recovery. At times, this will include contacting taxpayers shortly after the issuance of a notice of assessment or reassessment as stated above.

Consequently, we would not support a change to our collection policy or business systems that would delay the repayment of amounts owed to the Crown.

Question 4: Dispute Resolution

Taxpayers are experiencing lengthy delays in resolving cases and controversies at Appeals. TEI invites a discussion of the status of the workload for the Appeals Branch, including CRA's comments on the following:

a. What is the current estimated elapsed time to resolve a large-file case at Appeals after an objection is filed?

CRA Response:

Currently within the Appeals Branch, the average time to resolve an income tax large file is approximately 400 workable days, while the time to resolve a commodity tax or GST/HST file is approximately 550 days. The elapsed time to resolve cases is significant and can be attributable mostly to:

i. the number of large files relating to the same taxpayers (or groups of related taxpayers), and the need in these cases to resolve issues in prior years before latter ones:

   - to preserve the continuity of tax schedules and balances in subsequent years in matters such as:
     - CCA schedules;
     - loss balances and related requests for prior and subsequent year application;
     - balances relevant for deductions in respect of Cumulative Eligible Capital;
     - Cumulative amounts and other schedules relating to Resource industries;

   or

   - to facilitate the determination of certain deductions or eligibility to certain credits that are dependent on the income of the previous year, such as the determination of investment tax credits;

ii. the number of issues involved in any single objection in a large file, which can be high;

iii. the high degree of complexity and limited supporting jurisprudence in many large file cases, which can require more time for analysis of issues; and

iv. delays that may arise, at times, in receiving representations from the taxpayers.

b. Are there any initiatives underway or under consideration to reduce the backlog of cases at Appeals?

CRA Response:

The Appeals Branch is committed to looking for ways to improve processes and address the backlog. We are considering various workload management approaches, including a detailed review of our processes for the resolution of large files objections to identify ways of expediting the work on these files.

c. From TEI's perspective, one factor contributing to the current backlog of cases is that there seem few incentives for the Audit Division to resolve controversies at the audit stage. Indeed, some taxpayers report receiving adjustments that are clearly unsustainable at Appeals. TEI believes the verification process should be used to identify, audit, and resolve issues with taxpayers. Indeed, far more issues should be resolved at the audit stage because once controversies move past the audit stage, the cost and time to resolve the issue increases substantially.

   To frame the discussion, TEI invites CRA's comments on the following:

   i. Are any initiatives being considered to reduce the number of unsustainable adjustments passed from the Audit Division to the Appeals Branch?

   ii. Does CRA have metrics to measure the *quality* of the adjustments moving from Audit to Appeals? Can such metrics be adapted to evaluate the Audit Division's performance?

   iii. Does CRA employ a quality assurance function to review audit findings prior to the issuance of proposed adjustments or submission of the files for reassessment?

   iv. Can CRA provide suggestions to taxpayers about how to resolve more issues at the audit level as part of the verification process?

CRA Response:

We agree that wherever possible, issues should be resolved at the audit stage. If a taxpayer disagrees with a proposed audit adjustment, they should communicate their position in a written representation and provide it to the auditor within the stated time limit on the proposal letter. At that point, the taxpayer may also request a meeting with the auditors' immediate supervisor to explain their position on the proposed adjustment and ensure that both the auditor and their supervisor have all pertinent facts when reviewing the representations.

i. Are any initiatives being considered to reduce the number of unsustainable adjustments passed from the Audit Division to the Appeals Branch?

In the International and Large Business Directorate, it is mandatory that the team leader/manager only approve a completed audit case once he/she has conducted a thorough review to ensure the audit was conducted properly. This mandatory step is in place to ensure that all proposed audit adjustments are well explained and legislatively accurate.

ii. Does CRA have metrics to measure the *quality* of the adjustments moving from Audit to Appeals? Can such metrics be adapted to evaluate the Audit Division's performance?

The CRA does not have a metric that measures the quality of adjustments moving from Audit to Appeals.

iii. Does CRA employ a quality assurance function to review audit findings prior to the issuance of proposed adjustments or submission of the files for reassessment?

The CRA is continuously reviewing and monitoring its audit processes and controls to identify opportunities for improvement. As a result, audit files are reviewed to ensure that there is a consistent application of standards of quality in all audit programs. In the International and Large Business Directorate, all proposed audit adjustments are reviewed by the auditors' supervisor prior to a proposal being issued. As well, prior to the audit being finalized the supervisor again reviews the audit adjustments with consideration given to any representations submitted by the taxpayer.

iv. Can CRA provide suggestions to taxpayers about how to resolve more issues at the audit level as part of the verification process?

Communication plays an important role throughout the audit, especially when discussing points at issue or when responding to the taxpayer's submissions. As a result, taxpayers are strongly encouraged to communicate their position regarding identified audit issues as well as provide the CRA with any supporting documentation and access to the staff involved in the preparation of their books and records. At the proposal stage, if a taxpayer disagrees with a proposed audit adjustment, they should communicate their position in a written representation and provide it to the auditor within the stated time limit on the proposal letter. At that point, the taxpayer may also request a meeting with the auditors' immediate supervisor to explain their position on the proposed adjustment and ensure that both the auditor and their supervisor have all pertinent facts when reviewing the representations.

Question 5: Operating Expenses Paid by an Employee

Publication T4130(E) *Employer's Guide — Taxable Benefits and Allowances* provides the following guidance about automobile taxable benefits:

Reimbursement of operating expenses

a) If the employee reimburses you in the year or no later than 45 days after the end of the year for all operating expenses (including the GST/HST and PST) attributable to personal use, you do not have to calculate an operating expense benefit for the year. If the employee reimburses you for part of the automobile's operating expenses in the year or no later than 45 days after the end of the year, deduct the payment from the fixed-rate calculation of the benefit.

b) If you provide an automobile to an employee and you require your employee to pay a third party for part or all of the operating expenses (including the GST/HST and PST) in the year, administratively, we will allow you to deduct the portion of the payments

attributable to personal use from the fixed-rate calculation of the operating expense benefit. Note: The portion of the operating expenses that relates to personal use is the percentage obtained by dividing the number of personal kilometers by the total number of kilometers driven by the employee during the year while the automobile was available to the employee.

Paragraph (a) suggests that the employee's taxable benefit can be reduced by the full amount of reimbursements paid to the employer, but that operating expenses paid by an employee to a third party must be prorated by a ratio of personal kilometers driven to total kilometers driven. The rationale for the distinction and the inconsistent treatment of reimbursements to employers versus payments to third parties is unclear. TEI recommends that CRA amend the guidance to allow recognition of the full amount paid by the employee to the third party. We note that Form RC18 (*Calculating Automobile Benefits for 2012*) and the "Automobile Benefits Online Calculator" treat reimbursements to the employer and amounts paid by the employee to third parties identically: the operating expense benefit is fully reduced by the payments and no proration is applied.

Paragraph (b) states that the "fixed rate calculation of the benefit" can be reduced by reimbursements of operating expenses to the employer and operating expenses paid by the employee to a third party. What is CRA's position on the treatment of reimbursements to the employer or operating expenses paid by employees to third parties under the optional-method calculation? Can the operating expense benefit be reduced by reimbursements to the employer or payments to third parties under the optional method?

CRA Response:

In both cases, whether the amount of the benefit is reduced by reimbursements of operating expenses to the employer or through operating expenses paid by the employee to a third party, the treatment of the employee's reimbursement is the same. The operating expense benefit, where it is calculated, is reduced by the amount the employee pays for operating expenses attributable to his personal use of the automobile. Where the employee pays for 100% of personal operating expenses, it is not a question of reducing an operating expense benefit to zero. Rather, there is no benefit to calculate.

Of note, the wording of paragraph 6(1)(k) of the ITA is unambiguous and does not permit a reduction to the operating expense benefit for third party payments by employees, however it provides a simple formula for determining the operating expense benefit of an employee where an automobile is provided to the employee by the employer and operating expenses are paid by the employer. Subparagraph 6(1)(k)(iii) clearly permits a reduction to the operating expense benefit only for amounts paid to the employer. Accordingly, operating expenses paid to third parties unrelated to the employer would not reduce the operating expense benefit.

That being said, the CRA understands that it has become more common for employees to pay some of the operating expenses directly to third parties. By following the strict interpretation of the income tax legislation, the employer should not be allowed to reduce the operating expense benefit by the amount the employee paid towards the operating expense of the vehicle to a third

party, because a "reimbursement" has not occurred. However, the CRA analyzed this situation and recognized the fact that operating expenses paid to third parties includes both personal and business use. Therefore, to alleviate any burden imposed on the taxpayer, the CRA has an administrative position that allows employers to deduct the portion of the payments (paid by the employee directly to third parties) attributable to personal use of the operating expense benefit. This position is included in the CRA's Interpretation 2008-0274071I7, *Reduction of paragraph 6(1)(k) Automobile Operating Expense Benefit*.

In respect of the TEI's suggestion of inconsistent treatment of reimbursements under the CRA's written guidance and the approaches taken in the Form RC18 and the "Automobile Benefits Online Calculator", the CRA will review these publications and online tools for consistency and clarity.

Further, as to whether the operating expense benefit be reduced by reimbursements to the employer or payments to third parties under the optional method, the CRA notes that our guides for 2014 have been updated to allow for either method of calculating the operational expenses benefit.

Question 6: CRA Audit Deduction

When the Audit Division makes an adjustment in respect of an income inclusion item that is a timing difference by increasing taxable income in a particular year (Year 1), will the Audit Division tax the same income in a subsequent year (Year 2)? To illustrate the question, assume a taxpayer enters into an agreement in Year 1 to provide services in Year 2. The taxpayer receives $100M for those services in Year 1 but includes nothing ($0) in taxable income in that particular year and includes $100M in income in Year 2. CRA Audit concludes that the $100M should be included in taxable income in Year 1, determines that no reserve is available to offset the inclusion, and reassesses. The taxpayer files a Notice of Objection for Year 1. CRA Audit then audits the subsequent year and does not reduce taxable income by $100M in Year 2, notwithstanding that subsection 152(4.3) allows consequential assessments beyond the normal reassessment period where a balance, including taxable income, is changed as the result of a decision on appeal. The result is that the taxpayer would be subject to double taxation on $100M (since the amount is included in taxable income in both Year 1 and Year 2) pending resolution of its Notice of Objection. Moreover, if the taxpayer is a large corporation, it is required to remit 50 percent of all taxes in dispute on filing the Notice of Objection. On the facts of the example, the taxpayer would remit 50 percent of the taxes to pursue its appeal of the issue for Year 1 while also effectively paying the full amount of tax in Year 2, as filed. Subsection 248(28) seemingly does not support CRA's taxing the same income twice. We invite CRA's comments on the propriety of taxing the same amount twice.

CRA Response:

The situation you have described suggests that double taxation may occur pending the outcome of an appeal where income is reallocated from Year 2 to Year 1 by Audit. It is our view that this scenario is generally not an appropriate result. In the large file population, taxpayers are

generally audited in cycles and any reallocation of income from one fiscal year to another should be properly reversed as part of the normal audit process or upon taxpayer request.

Generally, Audit would reassess Year 1 to include the income and reassess Year 2 to remove the same amount of income that has been reallocated. In the event that the reassessment of income to Year 1 is reversed by Appeals, subsection 152(4.3) which governs consequential reassessments will permit the CRA to reallocate or include the income back in Year 2.

If for some reason it did, the taxpayer would ask for a Taxpayer Request (i.e., for a downward adjustment) and the auditor would make sure to process the request expeditiously.

Question 7: Employer Provided Social Events

CRA treats the cost of employer-provided social events that are available to all employees at a particular place of business as a non-taxable benefit, provided the cost per employee is *reasonable*. A now cancelled administrative guideline interpreted the reasonable event cost as $100 per person. (*See* ITTN-15 – *Income Tax Technical News* (December 18, 1998) [cancelled]). Fifteen years have elapsed since that interpretation was issued, but the $100 per person cost is seemingly still the controlling guideline. Owing to cost inflation, the nearly automatic imposition of gratuities of 15-18 percent for group events, and the application of taxes to event costs, we believe the $100 amount is too low. We recommend that CRA publish a new guideline reflecting an increased amount for a reasonable per-employee cost. We invite CRA's reaction to TEI's recommendation.

CRA Response:

The CRA is open to the TEI's proposal to consider to increasing the amount that is considered a reasonable per-employee cost for employer-provided social events; however, the consideration of such relief would involve an analysis and support generally found in a business case. To assist in this process, the TEI is invited to provide details that might support such a case.

Question 8: Regulation 102 Waivers

We invite a discussion of CRA's views in respect of its administration of Regulation 102, especially applications for waivers of withholding (Form R102-R), as follows:

a. Increasingly, taxpayers are finding that even timely filed R102-R waiver applications are being rejected. The stated basis for the rejection is that the relevant non-resident employer failed to file Form R105 to obtain a waiver of withholding under Regulation 105. TEI believes the requirements for, and policy underlying, an R105 waiver are separate matters from the employee-level R102-R requirements. Would CRA please explain the policy reason for the linkage between the R102-R waiver and the R105 waiver?

CRA Response:

When a non-resident employee is applying for a Regulation 102 waiver of withholding on the basis that they will be exempt from tax in Canada under a treaty provision that is dependent on the remuneration not being paid by, or on behalf of, a person who is a resident of Canada and is not borne by a permanent establishment in Canada, the current R102-R waiver form does not contain the non-resident employer information required for the CRA to evaluate this remuneration criteria. Where the non-resident employer is receiving a payment from a customer or client in Canada and has applied for a waiver of the withholding tax required under Regulation 105 on the payment, the Regulation 105 waiver application will normally provide CRA with the ability to evaluate this remuneration criteria and therefore determine if the non-resident employees are exempt from tax in Canada. We have been encountering an increasing number of situations where the non-resident employer is not applying for a Regulation 105 waiver, yet they have a substantial number of employees providing employment services in Canada. This represents a concern for CRA as it appears the non-resident employer has a significant presence and is spending a significant amount of time in Canada.

We have been advised by tax practitioners and taxpayers of this situation and the various explanations as to why this may be occurring. This issue is currently under review by the CRA.

We are working on procedures that may allow some of these R102 waivers to be processed. However we are consulting with internal stakeholders and this will take some time. We will let you know when we are closer to resolving this issue.

b. CRA currently requires that R102-R requests for waivers of withholding be made 30 days prior to the start of employment services in Canada or the initial payment. Due to administrative delays and the requirement to obtain an ITN or SIN prior to submission of the application, the waiver request can rarely be filed that far in advance. To enable more efficient compliance with the Regulation 102 regime, would CRA permit retroactive filing of the R102-R waiver?

   In its 2008 report, the Advisory Panel on Canada's System of International Taxation recommended elimination of Regulations 102 and 105. Although TEI agrees with the Panel's recommendation and believes repealing the rules or replacing the waiver process with a self-certification system would be the better course, TEI representatives have met with CRA to discuss and develop other, more practical approaches to comply with the current Regulation 102 requirements.[2] We request an update on CRA's views and proposals for simplifying the Regulation 102 administration and waiver process.

[2] While TEI appreciates the July 12, 2013, Finance release relating to subparagraph 102(6) of the Regulations, which introduced exceptions for those employed with prescribed international organizations and prescribed international non-governmental organizations, and the recent CRA administrative relief for conference attendees, those measures do not go far enough.

In connection with that discussion, we note that the $10,000 threshold in Article XV(2) of the Canada-U.S. Treaty has not been adjusted for inflation since 1980.[3] Since revisions to treaties take considerable time to negotiate, we recommend that CRA consider implementing a reasonable administrative guideline to reduce the burden of adhering to such a low threshold in its administration of R102 waivers. We encourage CRA to work with the Department of Finance to develop a higher *de minimis* threshold and other relief from the current Regulation 102 requirements.

CRA Response:

The CRA will continue to evaluate potential changes to the waiver process for non-resident employees over the next year. At the present time, we cannot provide a more definitive response regarding particular suggestions. The CRA is continuing to pursue potential policies to simplify the Regulation 102 administration and waiver process.

Question 9: Tax Residency Certificates

When entering a competitive bidding process for contracts in foreign jurisdictions, Canadian businesses are frequently required to provide — on an urgent time frame — tax residency certificates to their customers. CRA does not issue tax residency certificates in the name of a Canadian partnership (as defined in the ITA), so separate residency certificates must be obtained in the names of each of the entity's partners. Many Canadian companies experience commercial disadvantages with international competitors where they are required to explain to foreign customers — who are unfamiliar with tax legislation and Canadian administrative practice — how corporate residency certificates are obtained in a partnership setting. (The challenge is compounded where the bidding partnership is in a tiered-partnership structure). In some cases, the customers are unwilling or unable to countenance the delay required to obtain the certificate for all the partners, thereby resulting in lost commercial opportunities for Canadian companies.

Would CRA be willing to issue Canadian tax residency certificates in the name of a Canadian partnership on the basis of the Canadian residency of all its partners? We appreciate that a Canadian partnership does not have a tax residence per se, but in certifying the Canadian residence for all of an entity's partners the Canadian residency of the partnership can effectively be established. If the CRA were willing to issue a Canadian tax residency certificate in the name of a Canadian partnership on the basis of CRA-approved qualifying status of the Canadian partners, the competitive posture of Canadian businesses would be significantly improved. We invite CRA's response.

CRA Response:

The CRA has established procedures for the "certificate of residency" service. Under these procedures, those eligible to obtain a certificate of residency from the CRA are:

- an individual;

[3] To reflect the current costs of doing business, changes in the Consumer Price Index suggest that the $10,000 *de minimis* threshold should be close to $28,000 in 2013.

- a corporation;
- a trust;
- a non-profit organization, or
- a charity

that is considered resident in Canada.

Through these procedures, a certificate of residency may be issued by the CRA as proof that the taxpayer has filed returns as a resident of Canada. Further information on this service is available through the CRA website at http://www.cra-arc.gc.ca/tx/nnrsdnts/cmmn/crtrs-eng.html.

We appreciate the comments of the TEI in this regard. Consideration of such issues gives the CRA the opportunity to review or improve the tools currently in place, and to ensure we are always looking to improve the services that we provide. However, while the requirements and obligations involved in carrying on business in a foreign jurisdiction may present challenges, a certificate of residency is not currently available to a partnership. As you have noted, in itself, a partnership is not considered resident in Canada.

Question 10: Foreign Tax Credits

Assume the following facts: An employee moves from Country A to Canada in December 2012 and becomes a resident of Canada for tax purposes. In February 2013 the employee receives a bonus from the Country A employer for services rendered prior to departure. The amount is fully taxable to the employee in Canada in 2013. The amount is also fully taxable to the employee in Country A, but Country A treats the income as taxable in 2012 rather than 2013 since the bonus relates to services performed in 2012. Would CRA allow the employee to use the 2012 tax paid in country A as a foreign tax credit on the bonus amount received and taxable in Canada in 2013?

CRA Response:

Subsection 126(1) generally provides a foreign tax credit for the amount claimed by a taxpayer in respect of the non-business-income tax paid by the taxpayer **for the year** to the government of a country other than Canada.

For this purpose, the CRA has provided general guidance through its Income Tax Folio S5-F2-C1: *Foreign Tax Credit*. In particular, at paragraph 1.32 of the Folio, the CRA has stated that for an amount of foreign tax to be claimed by a taxpayer in the calculation of a foreign tax credit:

> "*…it must be paid...**for the year**, whether paid before, during or after the year in question. The words, **for the year** relate to the year for which the taxpayer is liable to pay tax (that is, when it is exigible) to the foreign jurisdiction for the income which is considered to have been earned under the foreign jurisdiction's tax law, even though the income may not be realized in Canada during the same tax year.*"
> (emphasis added)

Therefore, in the situation described, the CRA is of the view is that no foreign tax credit would be available under subsection 126(1) for the employee's 2013 Canadian taxation year in respect of the foreign income tax paid to Country A on the bonus because the foreign tax would not qualify as income or profits tax paid to Country A for the employee's 2013 taxation year in Country A.

Despite this fact, it may be possible for the employee to consider the amount of foreign tax paid to Country A for the purposes of claiming a foreign tax credit in Canada for the employee's 2012 Canadian taxation year. However, based on the formula for determining the foreign tax credit available under subsection 126(1), the amount of a 2012 foreign tax credit claim in Canada would be dependent upon the amount of foreign non-business income from sources in Country A that can be attributed to the part of the employee's 2012 Canadian taxation year in which the employee was resident in Canada. This calculation would not include consideration of the bonus that is included in the employee's income subject to tax in Canada in 2013.

As can be seen in the situation described above, despite the relief afforded in Canada through the foreign tax credit calculation, it is conceivable that a mismatch in the timing of foreign income recognition could result in the possibility of double taxation. However, in such circumstances, it may be appropriate to consider Canada's bilateral tax conventions, which generally provide for a mutual agreement procedure under which relief may be requested through the negotiation of the respective competent authorities. Alternatively, consideration could be given to approaching the Department of Finance and requesting a legislative change.