Member Advisory

January 2009

Canada Revenue Agency (CRA) Tax Roundtable

The annual Canada Revenue Agency (CRA) Roundtable Meeting was held in May 2008. A number of CRA representatives were in attendance, along with representatives from the profession.

As in previous years, two concurrent roundtable sessions were held, one focusing on GST issues and the other on income tax matters. All participants also attended a general wrap-up session. General process and procedure tips were also discussed, including the training of CRA staff, access to working papers, payroll remittances and customer service.

For more information on the session, contact Senior Professional Advisor Al Budlong at a.budlong@icaa.ab.ca.

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GST QUESTIONS

GST/HST Reporting Periods

1) We have experienced situations where the CRA's record of a taxpayer's GST filing period does not match our own/our client's. For example, if a company is incorporated in April, and commences operations May 1. Also on May 1 the owner's contact CRA for a business and GST number. When answering CRA's questions they state they have not yet decided upon the corporate year-end. Later, in consultation with their CA, they select September 30 as the year-end. The year-end Financial Statements, T2 and GST returns are prepared and filed for September 30 year-end. During the following year the client receives communication from CRA stating they have not filed a GST return. Investigation of the situation discovers that CRA acknowledges they did receive the GST return, that they had arbitrarily assigned a December year-end to the company, and had discarded the GST return filed by the CA firm. No communication is sent from CRA when the original GST return is discarded. Forced to file a [second] GST return for December, not late, the client is also charged a late filing penalty.

While the matter was ultimately resolved, we would note that the taxpayer's records now reflect late filing of the December GST return and any future adjustments are subject to penalty. As well, the taxpayer now inappropriately lacks a "perfect compliance history", precluding taking advantage of the opportunity to file quarterly installments. Had the Agency been able to revise the fiscal period for the first year of filing, these issues could have been avoided. Can the Agency please advise:

> a) Why is it when a GST return is filed with the incorrect year-end the return is just discarded without notifying the taxpayer or may be returned with a form letter indicating they were not expecting a return for this period? This form letter does little to resolve the matter, as it provides no information on the returns CRA is expecting. This is especially frustrating when the return is submitted with additional information attempting to explain the discrepancy and, hopefully, resolve the matter, and a further form letter which provides no indication CRA has considered the additional information provided. Could these form letters be changed to:
>
> > i) Indicate the fiscal periods for which GST returns are expected so the registrant is able to determine where the discrepancy lies?
> >
> > ii) Comment on the explanations provided, rather than ignore this correspondence?
> >
> > iii) Contact the client (or their representative) by telephone in an effort to determine why the taxpayer is submitting returns the Agency is not expecting?

Response

When we receive a return for a period that does not correspond to any period for which we are expecting a return, we cancel the return and send a letter to the taxpayer to inform them we have cancelled the return. The letter indicates to the

taxpayer the period covered by the return that was cancelled and also that we will be sending the taxpayer GST/HST return(s) with the required reporting period dates. This return is then sent by separate cover.

Phone contact has been considered but the processing area feels there is no value added by calling the taxpayer. The letter indicates that the return is not for a period for which we are expecting a return and gives the year-end that we have on record. The year-end, if invalid, cannot be changed just through phone contact.

b) Would it be possible for CRA to simply accept the fiscal period provided in the taxpayer's initial GST filing, similar to a corporate tax return, and adjust their systems accordingly. Commonly, the issue arises because a taxpayer selects a year-end other than that envisioned when registering for the GST.

Response

According to subsection 244(4) of the *Excise Tax Act*, an election for a fiscal year must specify the date it becomes effective and must be filed "before the day that is one month after the effective date". If the taxpayer wished to amend their fiscal year in their first year of filing, they would need to make this election within their first month of being registered. If we receive returns with notations that they wish their fiscal year amended or if a taxpayer contacted us to advise us of the same, we would be unable to amend the fiscal year for the previous year.

The fiscal year-end must be determined by an election. Because an election is required, the year-end cannot be set by a notation or entry on the return. If we are contacted at the time of registration and the year-end has not been determined, we will suggest that December 31 be chosen and the taxpayer will be advised of how and when to elect a change.

c) Whether CRA will implement a mechanism whereby a rejection on their part of a timely filed return can be corrected to reflect that return as timely filed.

Response

It is the responsibility of the accountant and their clients to choose a fiscal year-end and communicate this to CRA in a timely manner. When registering for a GST number, if the client does not indicate what fiscal year-end they want, the system automatically defaults to Dec. 31st. Clients receive confirmation of registration along with a questionnaire asking for more information on the GST account. Clients should let CRA know as soon as possible what fiscal year-end they want so the system can be set up properly to avoid problems when filing the GST or T2 returns.

There is no mechanism to accept invalid returns as a timely filed return. If a return cannot be processed, it is cancelled. Considering a cancelled return as filed on time may undermine complying with filing requirements. Details of cancelled

returns do remain on our systems and can be considered in compliance and collection activities.

GST/HST Rulings

2) Often a GST auditor will make an assessment or propose an assessment based on a technical argument. We are asked to provide additional information to convince the auditor and his/her Team Leader that the interpretation or argument is incorrect. However, we have repeatedly been refused access to the internal "ruling" given to the auditor by the Technical Interpretation Service (TIS) and to the submission that the auditor provided to get that opinion.

Can we please see a change in administrative policy that will allow us to work with the CRA in coming to an interpretation based on all the information that should be considered? This will expedite the completion of the audit and hopefully reduce the number of Objections, or at least simplify the points to be considered by an Appeals officer if there is a difference in interpreting the transactions involved.

Response

GST/HST Memorandum 1.4 states, in part, that the CRA may not issue a ruling:

- **"when a transaction on which a ruling has been requested is the same in character as a transaction completed by the requestor in a prior period, and the application of the relevant legislation to the earlier transaction is under discussion with the requestor, in dispute, or under assessment or proposed assessment, but is not before the courts;" or**
- **"when the request concerns a matter in respect of which the Appeals Branch is considering a Notice of Objection filed by the requestor;".**

This indicates that we have the flexibility to determine whether a ruling will be issued and requires GST/HST Rulings to use their judgment when making such determinations. In fact the memorandum goes on to state:

"In some circumstances the CRA may rule on an issue that is under audit. In such a case, the rulings officer will communicate with the CRA auditor to discuss the request."

When a request comes from Audit, GST/HST Rulings provides an internal memorandum to Audit based on the scenario provided. When asked to do so, and where appropriate given the particular circumstances, we may provide a ruling on an issue under audit or appeal as long as the decision taken is discussed with all CRA parties involved and agreement by all parties is attained. Where a taxpayer would like an opinion from GST/HST Rulings it should discuss the situation with the auditor. The taxpayer should submit the request and make the auditor aware it has done so. In the case of an audit, such requests should usually be made prior to issuing a Notice of Assessment/Re-assessment. Auditors are encouraged to share with the taxpayer all information used in arriving at their assessment.

GST/HST Registration

3) GST registrations are taking much longer now than in the past. With the recent changes implemented by the CRA requiring BN requests to be faxed for processing the revised system does not allow for timely feedback or confirmation from the CRA acknowledging the request. Accordingly, requests are lost, delayed or otherwise not dealt with. A better system is needed to address urgent and special situations involving GST registration and BN requests.

What is the CRA's position on this matter and what can be done to address these concerns?

Response

Registrations are to be completed by the Prairie Regional Correspondence Centre within 5 business days from the day of receipt. Accountants are provided with the 1-866-218-4847 number to call for urgent requests or registrations that have not been handled in a timely manner. Based on the feedback received, the Correspondence Centre will review the procedures for this phone line to enhance the service level.

4) Face to face interaction with the local office is by appointment only and we are finding that requests for appointments are being screened and refused. The use of the "Urgent" registration process, either through Regina or the local office, can speed up the process. However, with registration often required to allow use of the provisions found in 156, 167 and 221(2) of the ETA, and with the participants often being newly created corporations, sometimes the most efficient means of getting the process completed is a meeting with an experienced CRA officer.

Why are professionals being second-guessed by the staff answering the telephones? We are not getting the impression that there have been too many requests for appointments, so what is the reason for the roadblock and how do we remove it?

Response

When a Business Enquiries agent receives a call from a taxpayer requesting an appointment, the agent will first determine if the caller's request can be resolved via the telephone call. The purpose of this, if applicable, is to take the necessary action to resolve the enquiry at the time, without having to inconvenience the caller by having them report in person. In addition, an agent takes into consideration that an in-service appointment may not be the best means to resolve a particular enquiry. In some instances, the in-person enquiries agent may not have the functionality to resolve a particular request and it may have to be referred to the Tax Centre (eg., request for a BN for a Manitoba corporation). Agents are normally able to determine this at the time of the call and, as a result, would be less inclined to arrange for an in-person appointment. However, if the caller clearly indicates that they want an appointment to address the situation, the agent should proceed to arrange for this.

5) We were quite disturbed to review the decision of the Court in Westborough Place (007 GTC 856), where the court concluded the Agency had retroactively cancelled the GST registration of a major supplier to the taxpayer to support its denial of significant Input Tax Credits arising from GST paid on that supplier's invoices. Some commentators have suggested this cancellation of registration was undertaken to frustrate the taxpayer's claims. We have also seen a few cases in recent months where taxpayers have been reassessed to deny inappropriate claims processed with the aid of a CRA representative.

a) With this in mind, we would ask that the Agency share what information it can regarding its processes for dealing with such individuals.

b) Has, or would, the CRA consider imposition of civil penalties under Section 285.1 against its own employees engaged in inappropriate actions such as those identified above?

Response

The confidentiality provisions of the *Excise Tax Act* (ETA) prevent us from commenting on specific cases. The CRA is committed to administering the ETA in a fair and impartial manner. To this end, the CRA undertakes compliance audits and investigations to ensure that ETA obligations are fulfilled. Allegations of employee misconduct are treated very seriously by the CRA, and it investigates all such cases.

GST/HST Business Consent Forms

6) The consent forms are taking 5-7 business days to be entered into the CRA computer system when it used to take 24 hours. Is there any way this process can return to a 24-hour turnaround?

Response

Business Consent forms are processed at the CRA's Taxation Centres.
The standard processing time for these forms has always been 10 days. During certain periods, the CRA may be able to process these forms in a much shorter timeframe. However, during peak periods, processing timeframes may be closer to the standard. Due to the high volume of these forms received, the CRA cannot commit to a 24-hour turnaround time. CRA continues to enhance electronic services. As of October 2007 business owners are now able to authorize their employees, or third party representatives (such as a tax services or payroll business) to deal with the CRA on their behalf through 'Represent a Client'.

7) We are seeing the consent form entered incorrectly by CRA; ie., as an individual and not a firm, although clearly marked "Firm". This causes problems as we cannot get

information and have to contact a supervisor or resend the form. These delays increase the length of time it takes to get the GST numbers and can delay closings.

Is there a method that firms can use to make it clear that the consent is for a firm?

Response

Your concern is noted, and we will ensure that our staff are reminded of the importance of entering the information correctly. We will also review the form to see if changes can be made to make the selection of a firm versus an individual clearer.

Suggestions For Solution:

1. Should be able to go to CRA locally and register a company, since the new ways are not working; it was easier and faster to go into the local office.

2. Should have a separate telephone line for firms, to be used, for example, for urgent requests and to find out about registrations.

Response

The Canada Revenue Agency (CRA) has developed toll-free networks to provide accessible, equitable and cost-effective telephone services to all taxpayers. Our toll-free networks allow the CRA to distribute calls to available agents across Canada, enhancing accessibility to telephone services. These toll-free networks are available for various lines of business including but not limited to Individual Income Tax Enquiries, Business Enquiries and Child and Family Benefits. Providing a dedicated line to a specific client group would require a significant increase in financial resources in order to maintain a group of dedicated agents for this purpose. In addition, such a measure could result in the perception that the CRA is providing preferential treatment to a specific client group over the needs of average Canadians.

As noted previously, representatives may contact the Prairie Regional Correspondence Intake Centre at 1-866-218-4847 to address urgent request.

Call Centre Issues

8) When calling to inquire about an account we are getting unreasonable questions, eg., CRA for amounts filed on a particular return. As a firm we would not have this amount of details on the client.

Would the CRA review this process and standardize the questions to information that a firm would typically have?

Response

It is the CRA's policy to protect the confidentiality, integrity and availability of the information and assets in its care. Pursuant to section 295 of the *Excise Tax Act*, and section 241 of the *Income Tax Act*, the CRA is precluded, with certain exceptions, from disclosing any taxpayer information to any person. Confidentiality measures are in place to protect taxpayer information. If an authorized representative calls on behalf of a taxpayer, the representative will be required to answer the same confidentiality questions as are required of the taxpayer.

9) We are finding that we are getting inconsistent information and instructions from the agents on the information lines, eg., where to send consent forms, or where to send request for business numbers.

Is there a way to ensure the information provided by the agent is consistent and correct?

Response

Business Enquiries Agents have at their disposal a Reference Guide to provide them with direction as to where a particular request is to be sent for processing. Agents will advise a caller where to submit their request based on the type of request being submitted and where the particular type of request can be processed. Certain requests must be processed in a Taxation Centre, while others can be processed in the Prairie Regional Correspondence Centres located in Regina and Saskatoon.

For example, a request for a BN for a business that has incorporated federally or with our participating provincial partners ((Nova Scotia, New Brunswick, Manitoba and British Columbia) is processed in a Taxation Centre, while on the other hand, a request for a BN for a business that has incorporated with any of the other provinces is processed at the Prairie Regional Correspondence Centres. A request to update a consent form is processed in the Taxation Centre and should be sent to Winnipeg. (An exception is when the RC59 Consent is attached to the RC1 BN Request Form that is sent to the Correspondence Centre.) As a result, an external client may be advised on one occasion to send a specific request to the TC and on another occasion to send a different type of request to the Prairie Regional Correspondence Centres. While it may appear to the external client that agents are providing inconsistent and/or incorrect information, this is not necessarily the case.

Voluntary Disclosure

10) Voluntary Disclosures for GST have been held in abeyance due to problems with the calculation of penalty and interest. They appear to be moving forward now. Has the CRA come up with a permanent solution for this problem or are we using a work around?

Response

System changes are being identified and worked on where necessary to have the GST assessments processed correctly.

Internet Based Supplies

11) Parliament expanded the zero-rating provision for Internet-based supplies under section VI V 10.1. The intent of Parliament, as stated in Information Guide GI-034, is that all assessments based on the narrow interpretation taken by the CRA between 2000 and 2007 should be refunded. We have heard that auditors are requiring applicants to produce the same degree of information that is identified in VI V 10.1 and in GI-034, even though this was not identified earlier and may be impossible to achieve now. For example, requesting that a customer from several years back sign off a statement that they were not registered for GST will be fruitless if the individual has changed email addresses or simply refuses to reply.

Is the CRA going to show some administrative tolerance where it is reasonable that the customers were non-resident and not likely to be registered for GST?

Response

As indicated in GST/HST Information Sheet GI-034 *Exports of Intangible Personal Property*, to support the zero-rating of supplies of intangible personal property under section 10.1 of Part V of Schedule VI suppliers must verify and maintain satisfactory evidence of the registration and residency status of the recipients of the supplies. The Information Sheet also explains what the CRA will generally accept as proof of registration and residency status for purposes of zero-rating.

Whether satisfactory evidence of registration and residency status to substantiate zero-rating has been obtained by the supplier in any given case is ultimately a verification issue that must be resolved by Audit on a case-by-case basis.

Zero-rating under the proposed provision applies to eligible supplies of intangible personal property made after March 19, 2007. It also applies to eligible supplies of IPP made on or before March 19, 2007, in respect of which GST/HST was neither charged nor collected. If a particular registrant has made such supplies and the CRA has taken an amount into account in assessing their net tax for a reporting period as GST/HST that became collectible in respect of such supplies, they may obtain a refund of any resulting overpayment of net tax, penalty or interest by requesting that a reassessment be made to take into account that no tax was collectible by them in respect of the supplies.

In order to qualify for such a refund, the registrant must have satisfactory evidence of the registration and residency status of the customers, which is a determination that must be made by Audit on a case-by-case basis. It is important to note that the Information Sheet does not state that all assessments made between 2000 and 2007 in relation to this issue will be refunded.

Standardized Accounting

12) With the "new" "standardized" accounting provisions enacted in 2006, there are a number of issues that have arisen. One issue is the filing of corporate T2 returns for "shelf companies" that were inactive and have been activated to carry on a commercial activity. Presently the CRA is seeking returns on these companies for the periods of inactivity and holding GST refunds until theses returns are filed.

Why is this necessary? If the company is a shelf company that was idle, what type of amounts do you expect to be filed on the T2 return?

Response

New legislation effective April 1, 2007 states that if you have to file any returns under the *Excise Tax Act*, the *Income Tax Act*, the Excise Act 2001 or the *Air Traveller's Security Charge Act,* refunds will be held until all outstanding returns are filed.

13) On the same issue as question 12 above, the CRA is now seeking corporate tax returns for municipalities and holding payment of GST refunds as part of the process of standardized accounting.

What is the purpose of this? How many years back does the CRA want corporate tax returns on these matters? Why?

Response

These are considered MUSH accounts (Municipalities, Universities, Schools and Hospitals)

Compliance Refund Hold Administrative Policy Expiration Date
In April 2007, new legislation was implemented that required refunds and/or rebates not to be issued to taxpayers until all outstanding returns had been filed and/or any outstanding amounts owing had been paid. Subsequently, CRA implemented an administrative policy not to hold refunds/rebates for municipalities, universities, schools, hospitals, non-profit organizations, federal crown corporations and Indian band councils that, although required to file, had not filed returns for previous years. The administrative policy allowed for a grace period ending March 31, 2008.

Registered charities, Hutterites, and provincial crown corporations are not required to file a corporation income tax (T2) return and are not subject to the provisions of the compliance refund hold.

Once the grace period expires, corporate entities from these sectors will only be required to file their corporate income tax returns with a fiscal period ending after April 1, 2008 in order to be considered compliant in respect to the automatic compliance refund hold policy. For more information, please refer to the Trust Accounts Division communication released March 24, 2008, http://infozone/english/r5044502/RCD/communication.asp?Division=TAD&Year=2008&refNumber=033

For a list of the corporations types see Module 6 "Corporations" of the Reference Guide for Business Window Agents under the heading "Outstanding Corporate Returns"
http://infozone/english/r5011204/csd/Manuals/BWRef_Guide/Module6/emodule6-42.htm#Refund_Holds.

14) Effective April 1, 2007 a person will not be paid a net tax refund, an overpayment of net tax, a refund, or a rebate until the person files all returns under the *Excise Tax Act*, the *Income Tax Act*, or the *Excise Act*.

Could you provide an example of how this would work? For example, if a taxpayer is filing a GST return with a net tax refund of $2,000 and there is an old corporate income tax return that has not been filed, presumably this refund will be withheld. When the return is filed and the refund is paid, how will the interest be calculated? Also, if you could provide other examples of how the offset would work it would be much appreciated.

Response

Interest will be paid 30 days after the later of:

- **The period end date**

OR

- **The date the return was received**

Example1

GST return for period end Dec 31/07, due date Jan 31/08.

- **Client files GST return Jan 31/08**
- **Client files T2 return Apr 30/08**

They are non-compliant. GST refund interest will be paid 30 days after Jan 31/08, ie., March 1/08 to the disbursement date.

Example2

GST return for Dec 31/07 due Jan 31/08.
Client filed GST return Jan31/08 for a refund BUT owes an amount to another revenue line, the money goes to the other revenue line with the effective date being the later of:

- **The date of the debt**

OR

- **The date of the credit.**

This is of course assuming the corp. is collectible.
NB: Any refund interest that would BECOME payable will also go to the other revenue line if it is required.

15) We understand that the CRA continues to focus its efforts to prevent improper GST refunds by identifying high-risk businesses before and at the time of assuring refund claims.

a) In this context, what does the CRA consider to be a high-risk business and what factors are considered in identifying such businesses?

b) Are there any particular sectors or industries in which the CRA is currently focusing its efforts with respect to GST compliance?

Response

The CRA is not in a position to make comments with respect to these issues at this time.

16) Prior to the implementation of Standardized Accounting on April 01, 2007, GST Notices of Reassessment were typically one page in length covering the entire audit period. Subsequent to April 01, 2007, a GST Notice of Reassessment issued as a result of an audit are numerous pages in length consisting of a lead "Results" page followed by numerous "Summary of Assessment" pages for each particular reporting period of the audit.

a) Is the individual "Summary of Assessment" page a legal Notice of Reassessment in itself?

b) When preparing a GST Notice of Objection, can a person object to an individual reporting period (i.e. one month of the audit period) for which a "Summary of Assessment" was issued as opposed to the entire audit period?

Response

Section 300 of the ETA requires the Minister to send a notice of assessment to the person assessed. The form of that notice is not prescribed.

In Stephens v. R., 87 D.T.C 5024, in the context of liability under the *Income Tax Act*, the Federal Court of Appeal held that: "The form of the notice does not matter; the notice must simply be expressed in terms that clearly make the taxpayer aware of the assessment made." In that case, the assessments were issued on letterhead from Revenue Canada – Taxation rather than the Department of National Revenue and had the printed signature of a person who was no longer the Deputy Minister. Despite these errors, the document satisfied the "notice of assessment" requirements because they were not misleading to the taxpayer.

In CCI Industries Ltd., Re, 2005 ABQB 675, the Alberta Court of Queen's Bench found that an audit proposal letter qualified as a notice of assessment since the key feature of a notice of assessment is to make the taxpayer aware that the CRA has made an assessment.

The Notices of Reassessment issued since April 1, 2007 are made up of a "Results" page and one or more "Summary of (Re) Assessment " pages.

The first page of the Notice of (Re) Assessment provides the combined results for the period covered by the audit. Each additional page refers to the assessment for the reporting period identified.

The box at the top right corner of each page provides the following information:

Date of Mailing;
Business Number; and
Period Covered.

The box "Period Covered" will either contain the dates of the beginning and end of the audit period or the notation "Refer to Summary". If the box contains particular dates, it indicates that each consecutive reporting period within the audit period has been assessed. If it contains the notation "Refer to Summary", it indicates that one or more reporting periods have not been assessed.

In numerous cases, the courts have found that a Notice of Assessment is a matter of substance, not of form. The Appeals Branch will accept a Notice of Objection for a reporting period for which a Summary of Reassessment has been issued.

Assessments

17) The Appeals division's authority to review an assessment derives from subsection 301(4), not section 296. The limitation periods for reassessment in section 298 apply to assessments and reassessments under section 296, and section 298 does not refer to reassessments under subsection 301(4).

Can the Appeals Division create an upwards assessment for a particular reporting period that is statute barred? If so, is there an administrative policy that the Appeals Division follows to prevent this from occurring?

Response

Subsection 301(3) provides that upon receipt of an objection, the Minister shall, with all due dispatch, reconsider the assessment and vacate or confirm the assessment or make a reassessment. This grants authority to make an upward reassessment.

There are no legislative provisions that allow for the withdrawal of a valid objection once it has been filed. The Minister must reconsider the assessment and notify the objector of his decision. Therefore, once identified, an upward adjustment must be processed.

It is a policy of the Appeals Branch that the Appeals Divisions will process upward adjustments when the following conditions are met:

i. **it is with respect to a matter under dispute or an item related to it;**
ii. **the normal reassessment period must not have expired if the adjustment results in an upward reassessment, except in cases of misrepresentation**

that is attributable to neglect, carelessness or willful default or the commission of any fraud in filing a return or supplying any information under the *ETA*;

iii. the upward adjustment is of relative importance, and

iv. the upward adjustment has been approved by the Chief of Appeals.

In fact the ability to proceed with upward adjustments is essential to maintaining the integrity of the tax system.

An internal directive on this subject was issued in February 2001 and is still in force.

18) The TCC and the FCA have confirmed (in Systematix and other cases) that a registrant must meet the specific requirements in the Input Tax Credit (GST/HST) Information Regulation in order to qualify to claim an input tax credit, by virtue of subsection 169(4). There is, however, no reference to the requirements in subsection 169(4) or the Regulation to claims for rebates under Part IX, and accordingly, there appears to be no legal basis for the Minister to disallow a rebate claim due to a lack of the technical supporting documentation set out in the Regulation. Nevertheless, it is reasonable that the Minister can require some level of documentary support for a rebate claim by virtue of section 299.

Please comment on the documentary requirements that CRA would propose to apply on a rebate application, and whether it would propose to apply the strict tests in Systematix and other similar cases to a rebate claim.

Response

Paragraph 169(4)(a) of the *Excise Tax Act* (ETA) and the Input Tax Credit Information (GST/HST) Regulations only apply to the documentary requirements for claiming input tax credits and do not apply to rebates contained in Division VI of Part IX.

Subsection 286(1) provides that every person who makes an application for a rebate shall keep records in such form and containing such information as will enable the determination of the amount of any rebate or refund to which the person is entitled.

Provisions applicable to various types of rebates are contained in Division VI of Part IX (Sections 252 to Sections 264). Each of these sections provide for certain filing requirements to claim the rebates, including requirements to provide prescribed information.

Section 262 sets out the application requirements in respect of rebates under Division VI, other than section 253, whereby it requires an application for a rebate to be made in prescribed form containing prescribed information and to be filed with the Minister in prescribed manner. For a rebate application form or the manner of filing that form, "prescribed" means authorized by the Minister. In the case of information to be given on a form, "prescribed" means specified by the Minister. There are no regulations for purposes of section 262.

For example, form GST189, General Application for Rebate of GST/HST, includes the requirement to provide an original document and is, therefore, a part of the prescribed information. Further, in Part F of the same form, the applicant is required to certify that in addition to any documents submitted with the rebate application, books, records and invoices are available for inspection, hence bringing all these documents under the ambit of prescribed information.

19) After a period of more than three years of ongoing paper inquiries and numerous phone calls, faxes, and other detailed correspondence, CRA has still not resolved a GST issue for a corporate client, being a refund of a 2004 credit, per CRA's records, due the client. They did, at long last, recently [March 22, 2008] credit back to the client less than 70% of the 2004 credit, saying they could only reconstruct that amount of the credit, and that they didn't know where the other 30% went to. We have spent multiple hours over the past three years attempting to recover the credit, and are baffled by the result CRA arbitrarily imposed this year.

a) Where are the statements of accounts being processed and is there a person(s) responsible for this function?

Response

As of April 10, 2007, GST clients should receive a regular monthly statement of arrears when there is activity on their account. The Statement of Arrears is computer generated on the 14th of each month and mailed to business clients from one of our print to mail locations.

For a detailed statement of account covering periods and/or activity prior to March 31, 2007, a request should be made to the GST Accounting area of the client's designated Tax Centre. These requests are completed by GST Accounting Officers and mailed to the client.

b) How do we more effectively resolve this type of situation in the future?

Response

Although it is difficult to answer this question without the account details, we acknowledge the frustration that was experienced in this situation. With the new GST system and enhancements such as receiving Notices of Assessment for every return or rebate we assess or reassess, as well as the new statements such as statement of arrears, statement of interest calculated, notification of installment interest and notification of returned payment, your clients will be more aware of what is happening with their accounts. This will also help us to resolve discrepancies on accounts faster.

20) The information contained in the CRA Info Sheet GI-025 appears to contradict the provisions in the ETA.

How does a taxpayer protect themselves from an incorrect audit assessment with respect to vacation properties that are used in commercial activities?

Response

Where a taxpayer disagrees with an assessment with respect to vacation properties, the taxpayer may, within ninety days after the day the notice of assessment is sent to them, file a notice of objection to the assessment pursuant to section 301 of the *Excise Tax Act*. For additional information on the objections and appeals process please refer to GST New Memorandum Series 31.0, *Objections and Appeals*.

Greenhouse Gas

21) In general, what is the GST/HST treatment for purchases of a Greenhouse Gas Credit ("GHG") from the following entities:

i) a person in a commercial activity?
ii) a person acting as a private individual or a non-profit organization (trading in GHGs)?
iii) a regulated trading organization (such as proposed by the Province of BC)?

Response

For Questions 21 (i) and (ii):

The characterization of a supply (i.e., determining whether the supply is one of property or service) is fundamental to the application of the GST/HST. In order to provide a definitive opinion on the application of GST/HST to specific purchases of GHGs, the CRA will have to consider the terms of the agreement between the parties to see how the agreement for the supply would be characterized under the *Excise Tax Act* (ETA). In characterizing the supply, we would consider how federal and provincial laws treat the GHGs and the specific regulations that apply to their transfer, sale or purchase. As there is no provision in the ETA that specifically addresses the supply of GHGs, the normal rules in the ETA would apply.

For Questions 21 (iii):

The GST/HST treatment of GHGs traded through a regulated trading organization will depend on the regulatory framework governing the trading of GHG. We cannot provide a general interpretation of the treatment of GHG traded through a trading organization without more information.

22) If allowed by provincial jurisdictions, what is the tax treatment for GHGs purchased in HST provinces, but utilized or transferred in non-HST provinces? And the reverse?

Response

As noted in the previous question, the CRA will have to consider the terms of the agreement between the parties to see how the agreement for the supply will be characterized under the *Excise Tax Act* (ETA). Where Greenhouse Gas Credits (GHG) are purchased by a GST/HST registrant, the registrant may be entitled to claim an input tax credit in respect of the GST/HST paid or payable in respect of the credits, to the extent the registrant uses the GHGs in a commercial activity.

Where GHGs are purchased in a non-participating province by a GST/HST registrant but used in or transferred to a participating province, the registrant may be required to self-assess the 8% rate of the provincial component of the HST.

23) What is the GST treatment for the contributions or payments to provincial and federal government funds due to regulatory requirements? Further, are these contributions or payments on account of business and deductible for Income Tax purposes?

Response

The GST/HST treatment of such contributions or payments will be dependent on the regulatory framework that authorizes such payments and therefore, we cannot provide a general interpretation with respect to their treatment under the *Excise Tax Act*. However, we would be pleased to respond to any ruling request with respect to a specific set of facts relating to these types of payments.

Given that most taxpayers will be required to reduce their GHG emissions relating to their business operations, the CRA expects that contributions or payments to provincial and federal government funds due to regulatory requirements will normally be made or incurred for the purpose of gaining or producing income from the business, and should be deductible in computing income for income tax purposes, unless it can be considered that the expenditure provides the taxpayer with ongoing benefits with a view to bringing into existence an asset of enduring benefit. In that situation, the expenditure may be considered to be on account of capital. Where it is determined that a capital asset has been acquired, the expenditure would have to be analyzed to determine whether it constitutes a depreciable property or an eligible capital property. Further, we note that where the contribution or payment is a fine or penalty imposed by the provincial or federal government, the amount would not be deductible by virtue of section 67.6 of the *Income Tax Act*. We refer you to our *Income Tax Technical News*, Issue Number 34, for our general comments regarding the income tax treatment of GHG credits.

Financial Institutions

24) Can you please advise us as to the status of the GST legislation in relation to the requirement for certain entities to file Form 111 (Financial Institution Annual Information Schedule)?

a) Has any consideration been given to eliminating the need for 149(c) de minimus financial institutions (such as large retailers with credit card operations) to file the above form?

Response

Form GST111 is required to be filed by a financial institution once per fiscal year, within six months of the end of its fiscal year.

The filing of Form GST111 is authorized under subsection 238(4), which states:

> **Every return under this Subdivision shall be made in prescribed form containing prescribed information and shall be filed in prescribed manner.**

The definition of prescribed in subsection 123(1) states, in part:

(a) in the case of a form or the manner of filing a form, authorized by the Minister,
(b) in the case of information to be given on a form, specified by the Minister,

Where Form GST111 is not filed as required or is filed but the information is incomplete, certain penalties may apply.

For example, section 284 provides that every person who fails to provide any information or document when and as required under this Part or under a regulation made under this Part is, except where the Minister waives the penalty, liable to a penalty of $100 for every failure unless, in the case of information required in respect of another person, a reasonable effort was made by the person to obtain the information.

In addition, section 283 could apply where a person fails to file a return when required pursuant to a demand issued under section 282. The penalty in this situation is equal to $250.

b) What will the penalties for non-compliance be?

Response

Form GST111 is required to be filed by a financial institution once per fiscal year, within six months of the end of its fiscal year.

The filing of Form GST111 is authorized under subsection 238(4), which states:

> **Every return under this Subdivision shall be made in prescribed form containing prescribed information and shall be filed in prescribed manner.**

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Where Form GST111 is not filed as required or is filed but the information is incomplete, certain penalties may apply.

For example, section 284 provides that every person who fails to provide any information or document when and as required under this Part or under a regulation made under this Part is, except where the Minister waives the penalty, liable to a penalty of $100 for every failure unless, in the case of information required in respect of another person, a reasonable effort was made by the person to obtain the information.

In addition, section 283 could apply where a person fails to file a return when required pursuant to a demand issued under section 282. The penalty in this situation is equal to $250.

c) Is there any further guidance as to the use of estimates (ie., what are the parameters for determining if it is reasonable in the view of CRA) and related penalties (where viewed as not being reasonable)?

Response

There are certain lines on Form GST111 where estimated amounts may be used, if the actual amounts are not reasonably ascertainable. The financial institution must use its best efforts to provide the most accurate information as possible. It is recognized that where estimates are used, certain totals may include estimated amounts.

Guide RC4419, *Financial Institution GST/HST Annual Information Schedule*, provides further guidance and instruction for lines that allow estimates. For certain lines, the guide provides explanations as to when amounts reported for income tax purposes can be used. For example, estimated amounts on lines 150, 160, 170, 171, 173 and 180 may be derived from amounts reported in the General Index of Financial Information (GIFI). As well, on line 060, an estimated amount may be used for the total amount of exempt supplies of financial services made during the fiscal year. The amount should be based upon revenues reported for income tax purposes that are attributable to the financial institution's exempt supplies of financial services.

Joint Ventures

25) For the past number of years the CRA has indicated that they would be "expanding" the prescribed activities for the joint venture election under section 273 of the ETA.

What progress has been made on this matter and is there changes coming in the foreseeable future?

Response

The responsibility for prescribing joint venture activities for purposes of section 273 of the *Excise Tax Act* rests with the Department of Finance. Currently, only

two activities have been prescribed as set out in the Joint Venture (GST/HST) Regulations.

However, over the last number of years the Department of Finance has undertaken a review of the Regulations and has identified other specified activities for which the joint venture election will be available. We understand that they are still reviewing activities for prescription. They are also reviewing the existing legislative/regulatory approach to determining eligibility for the joint venture election based on the representations they have received with respect to prescribing various activities. Upon completion of their review, we understand that the legislation and/or Regulations will be amended to include the specified activities that have been identified in their review to date.

We are not aware of any impending announcements by Finance on this issue.

Agents

26) A recent Tax Court of Canada decision ruled that an Alberta commercial condominium association was acting strictly as agent of the condominium owners (2004 TCC 406 TCJ McArthur). The decision was not appealed.

Does the CRA accept this position if the association and its members agree that agency was their intent and, if so, what degree of documentation will be required for ITCs claimed by one of the owners who is engaged in commercial activity?

Response

In the case of The Owners: Condominium Plan No. 9422336 v The Queen, the Tax Court of Canada decided that the Appellant, a commercial condominium corporation, was not an independent entity carrying on business on its own, but rather an agent with the authority to affect the legal position of the unit-owners (principals). The fact that the CRA did not appeal this decision should not be interpreted as an indication that the CRA accepts this decision. This case was decided under the informal procedures of the Tax Court of Canada and is not considered by the CRA to be precedent-setting. Therefore, notwithstanding the decision in this case, the CRA's position remains that it is a mixed question of fact and law as to whether an agency relationship exists between a condominium corporation and the unit-owners. Please refer to GST/HST Policy Statement P-182R, Agency, for more information on agency relationships.

In any situation, where a person acts as agent on behalf of one or more persons (principals) in acquiring or importing property or services, it is the principals who are liable to pay the consideration in respect of the supply, and therefore, are the recipients of the supply. As a result, even if the agent pays the consideration and tax on behalf of the principals, it is the principals who are entitled to claim an ITC in respect of the tax payable.

Generally, subsection 169(1) of the ETA provides that each registrant principal/recipient is entitled to claim an ITC for the tax that becomes payable by the principal/recipient to the extent to which the principal/recipient acquired or imported the property or services for consumption, use or supply in the course of

its commercial activities. However, subsection 169(4) provides that a registrant principal/recipient cannot claim an ITC until it has obtained sufficient evidence in such form containing such information as will enable the amount of the ITC to be determined, including any such information prescribed under the Input Tax Credit Information (GST/HST) Regulations (Regulations). Such evidence might include invoices, written agreements, letters or other supporting documentation. Finally, it should be noted that the Regulations provide that instead of the recipient's name being shown on invoices of $150 or more, the name of the duly authorized agent or representative may be shown, for example, when supplies of property or services have been acquired or imported under the agent's or representative's name.

Excise Tax

27) Can you please advise us as to the status of the development of the 'non-taxable' insurance premium list for purposes of Part I tax?

Response

Discussions have been underway since the fall of 2007 between the Canada Revenue Agency (CRA) and the insurance industry, namely the Insurance Brokers Association of Canada (IBAC), to generate a list of classes of insurance not available in Canada and classes of insurance for which the capacity in Canada is limited.

On March 14, 2008, IBAC provided CRA with a draft list of Insurance Coverage not Available in Canada for consideration. A list of Insurance with Limited Capacity will be provided at a later date.

The list of coverage not available in Canada may eventually be used as a guide to post to the CRA website. This should alleviate some of the administrative challenges faced by a taxpayer or their insurance broker when applying for an exemption under subsection 4(2) of Part I of the *Excise Tax Act*.

CRA is currently evaluating how these lists could be incorporated into the exemption claim process. In cases of insurance coverage listed as not available in Canada, the taxpayer may be exempted from the requirement to provide the information on five declinations from the insurance industry on the form E638 Application for exemption from insurance premium taxes imposed under the *Excise Tax Act* - Part I. The taxpayer may also be exempt from providing five forms E638A Statement of Availability or Declination from Authorized Insurers – Tax on Insurance Premiums (Part I of the *Excise Tax Act*) or five letters of declination.

A review process and committee would likely be required in order to maintain this list, and might involve other entities, such as the Insurance Bureau of Canada (IBC).

INCOME TAX QUESTIONS

1) The My Account and My Business Account services facilitate gathering information by taxpayers and their representatives greatly. Would the Agency consider adding information from their files relating to the General Rate Income Pool, Low Rate Income Pool, Refundable Dividend Tax on Hand and Capital Dividend Account of corporate taxpayers to facilitate comparison of taxpayer records of these amounts to the Agency's records?

Response

The Agency has systems-maintained balances for the General Rate Income Pool, Low Rate Income Pool, and Refundable Dividend Tax on Hand. The capital dividend account balance is calculated manually when Form T2054 - Election for a Capital Dividend under Subsection 83(2) is filed, and is not stored. We can consider providing these balances on My Business Account, but due, to other enhancements currently under development, they cannot be considered in the short term.

Follow Up Question

HQ indicated that they would consider adding the specified balances noted in the question to "My Business Account" but is not able to consider it in the short term. As this information has been requested by the accounting profession for some time now, can CRA provide a more specific time-frame in which this will be considered. Alternatively, would CRA consider providing Capital Gains and Capital Losses only as a step toward assisting accountants with CDA.

Response

We agree that the services ICAA would like added to MyBA have value and would complement those currently offered for the corporate tax program. We will of course add them to the list of services being considered for future development. With respect to timing however, resource availability and other constraints dictate that we determine new service additions well in advance of their implementation date. Our next development window for new services not already under development is April 2010.

2) The GRIP rules related to 2001 – 2005 provide for taxpayers to add amounts "reasonably considered" to relate to high rate income received from connected corporations as dividends in those years to their own GRIP pool. Assume a wholly owned subsidiary (Subco) reported income and paid dividends as follows:

In 2001, Subco paid tax on $100,000 of general full rate taxable income.
In 2002, Subco paid a $150,000 dividend to its parent corporation.
In 2005, Subco paid tax on a further $150,000 of general rate taxable income.

It seems clear that Subco's GRIP at the start of fiscal 2006 was $4,500 (calculated as $63,000 (63% of 2001 full rate income) plus $94,500 (63% of 2005 full rate income) less $150,000 of dividends paid in 2002).

Would the CRA concur that it is "reasonable to consider" all of the $150,000 dividend to be paid out of Subco's general rate income, and therefore an addition to Parentco's GRIP pool, given that the entire dividend reduced Subco's GRIP addition related to the 2001 through 2005 fiscal years?

Response

Subco's GRIP at the start of fiscal 2006 would be $7,500, calculated as $63,000 (63% of the full rate taxable income of $100,000 in 2001) plus $94,500 (63% of $150,000 full rate income in 2005) less the $150,000 in dividends paid in 2002.

We also agree with your view concerning the interpretation of paragraph 89(7) (c) of the *Income Tax Act* ("ITA") and its application in this particular situation between a Parent and Subsidiary. This issue is similar to the one that was addressed in Income Tax Rulings document 2007-0243051C6. As the Parent received a dividend from a "connected corporation" (as provided for in subsection 186(4)) that was deductible from its taxable income pursuant to subsection 112(1) of the ITA, then the Parent could increase its GRIP "to the extent that it is reasonable to consider" that the dividend is attributable to a GRIP addition of the payer corporation pursuant to subsection 89(7).

3) Assume that Opco's taxable income for the fiscal year ended December 31, 2007 is $500,000, computed as follows:

Active business income	$400,000
Specified Investment Business Income	$300,000
Net Income	$700,000
Charitable Donations	$(200,000)
Taxable Income	$500,000

Subco claims the small business deduction on $400,000 of income. It appears that Subco's GRIP for 2007 will be determined as follows:

Taxable Income	$500,000
Small Business Deduction ($64,000) x 100/16	(400,000)
Aggregate Investment Income	(300,000)
	(200,000)
x 68% =	(132,000)

(a) Does the Agency concur that the result is a negative offset of $132,000 to Opco's GRIP in respect of fiscal 2007?

(b) Does the Agency concur that a reduction to GRIP in such a case is an inappropriate result and, if so, will they communicate this view to the Department of Finance?

Response

a) Per subsection 89(1), the portion of the "general rate income pool (GRIP)" formula that determines the income that is taxable at the general corporate tax rate can result in a positive or negative amount.

b) As mentioned on the Agency web site, since the calculation resulting in a negative amount, as in the above example, seeks to identify the portion of a CCPC's taxable income that was subject to a beneficial treatment by way of a reduced tax rate or refundable tax, it should not exceed taxable income itself. In accordance, any prescribed form (schedule 53) that is filed with a negative amount (at line 150) will be processed by the Agency as if the amount were 0. Schedule 53 will be revised to ensure that this calculation does not produce a negative result. The revised schedule will be available in October 2008.

4) Subsection 89(11) is an election for a corporation to not be considered a CCPC for purposes of the small business deduction provisions. This election must be filed with the tax return for the fiscal year in which it becomes effective, and the corporation ceases to be a CCPC at the start of that taxation year. A corporation which ceases to be a CCPC is deemed to have a fiscal year end immediately prior to ceasing to be a CCPC. Could a corporation with a December 31 fiscal year end file a corporate tax return for the period of January 1, 2008 to July 31, 2008 as a CCPC, then file a return for the period from August 1 to December 31, 2008?

Response

Subsection 89(11) of the *Income Tax Act* ("the Act") permits a corporation to file an election to be treated as not being a Canadian-controlled private corporation (CCPC) for purposes of the small business deduction in subsection 125(1) of the Act and most of the new rules concerning the tax treatment of eligible dividends.

Generally speaking, where an election under 89(11) is filed by a CCPC prior to the due date of the Income Tax return for a taxation year, the treatment would apply to that entire taxation year. As a result, there is no need to file as a CCPC for a portion of the year and file a separate return for the balance of the year.

This interpretation does not effect the application of subsection 249(3.1) of the Act where a corporation ceases to be a CCPC as defined in subsection 125(7) of the Act. Where a corporation ceases to be a CCPC, subsection 249(3.1) deems that a new taxation year begins at that time. Accordingly, if the corporation ceases to be a CCPC on July 31, 2008, a new taxation year would be deemed to start on August 1, 2008.

5) Assume Holdco has a single asset, shares of Opco valued at $1 million with a nominal adjusted cost base. It has no liabilities and nominal share capital. Holdco has a December 31 year end. Holdco sells its Opco shares for $1 million in early 2008, pays a capital dividend of $500,000 and pays a taxable dividend of $410,000. It designates the taxable dividend as an eligible dividend. All payments are made prior to December 31, 2008. Holdco files an election not to be a CCPC under Subsection 89(11). As such, it had no LRIP at any time up to December 31, 2008.

(a) Does CRA concur that Holdco will be eligible for $133,333 of refundable dividend tax ($500,000 taxable capital gain x 26 2/3%) which is recovered due to payment of the taxable eligible dividend paid?
(b) Does CRA concur that Holdco had no LRIP when its eligible dividend was paid, such that there is no excessive eligible dividend declaration?
(c) Would the CRA consider this transaction to have the effect of artificially reducing Holdco's LRIP pool such that the entire dividend would be deemed excessive?

Response

This question appears to be an actual fact situation relating to a proposed transaction if not a completed transaction. Confirmation of the tax implications inherent in a proposed or actual transaction given in this format is not binding on the CRA.

(a) **When a private corporation pays a dividend, it will be entitled to a "dividend refund" pursuant to subsection 129(1) of the act equal to the lesser of:**

- **1/3 of the amount of all taxable dividends paid, and**
- **the RDTOH account balance at the end of the year (as calculated on the T2 Corporation Income Tax Return).**

Insufficient information has been provided to determine the amount of the dividend refund that Holdco should be entitled to. However, based on the information provided, Holdco may be eligible for a potential dividend refund of $133,333 ($500,000 x 26 2/3%) according to subsection 129(1).

(b) **The CRA does NOT concur as we are unable to determine whether or not Holdco had "low rate income pool (LRIP)" when its eligible dividend was paid. Subsection 89(8) "LRIP addition – ceasing to be a CCPC" indicates the balance(s) that would be included in LRIP (please refer to Schedule 54 for a detailed breakdown of the calculation, as found in Part 4 entitled "Worksheet for adjustment when a corporation ceases to be a CCPC or DIC"). Sufficient information has not been provided to be able to calculate an amount in the example provided.**

(c) **Assuming that Holdco filed the election not to be a CCPC under Subsection 89(11) on or before its filing-due date for the taxation year ending on December 31, 2008, any dividends elected as eligible dividends will not generally result in an excessive eligible dividend designation to the extent**

that the corporation has no LRIP. The LRIP is generally made up of ineligible dividends (i.e. taxable dividends other than eligible dividends) received from other corporations, and income that was subject to a beneficial treatment by way of reduced tax rate or refundable tax. Subsection 89(8) addresses the issue of "LRIP addition – ceasing to be a CCPC". As noted in response to b) above, insufficient information has been provided in order to determine whether this scenario "artificially reduces Holdco's LRIP such that the entire dividend would be deemed excessive".

6) The Copthorne Holdings case (2007 DTC 1230; TCC) indicates that penalties cannot be applied in a situation where the GAAR applies, as taxpayers are not permitted to self-assess under GAAR. Does the CRA concur with this view? Assuming the CRA believes penalties can apply in a GAAR assessment, is it the Agency's position that taxpayers can and should self-assess under the GAAR and, if so, what is their legal basis for this conclusion?

Response

The CRA did not appeal the decision of the TCC concerning the penalty portion of the assessment. However, the Taxpayer has appealed the decision of the TCC to uphold the GAAR assessment.

Although the penalty issue is not under appeal the case is still an active case, and therefore it would not be appropriate to respond to the query at this time.

7) In several technical interpretations the CRA has indicated that section 84.1 could apply in transactions between unrelated taxpayers on the basis they do not act at arm's length. Has the CRA reviewed their position in this regard in light of the decision in the McMullen case (2007 DTC 286; TCC) and, if so, can they comment on the circumstances where they would consider section 84.1 to apply where a corporation acquires shares of a corporation from an unrelated party (i.e. circumstances which would lead them to either conclude the parties do not act at arm's length or that the GAAR has been offended)?

Response

Section 84.1 describes the circumstances in which consideration received by a taxpayer on a sale of shares to a corporation should be accounted for as a dividend. Section 84.1 does not deem the purchasing corporation to pay a dividend to the selling taxpayer where the purchaser and the taxpayer deal at arm's length.

Pursuant to paragraph 251(1)(c), it is a question of fact whether, at a particular time, unrelated persons deal with each other at arm's length. For example, in paragraph 26 of Interpretation Bulletin IT-419R2, we mention that where one party to a transaction is merely "accommodating" the other party in an attempt to obtain a certain tax result may be a situation where the parties are not dealing at

arm's length because they do not have separate economic interests which reflect the ordinary commercial dealings between parties acting in their own separate interests.

In McMullen, the Court found that section 84.1 did not apply because the taxpayer and the purchaser corporation were dealing at arm's length as they had a separate economic interest and were not acting in concert. Furthermore, it concluded for the purpose of section 245 that there were no avoidance transactions as the transactions were primarily arranged for *bona fide* purposes, other than to obtain a tax benefit.

Therefore, the decision in McMullen will be limited to that particular case as it was concluded on a finding of facts. The CRA will continue to apply section 84.1 I.T.A. or subsection 245(2) I.T.A., in those situations where the purchaser corporation acts as an "accommodator" or "facilitator" for the taxpayer in order to avoid the application of section 84.1 of the ITA.

8) Subsection 74.5(1) sets out criteria under which the attribution rules will not apply. One requirement of this provision, where a loan is utilized as consideration, is that interest be paid each year within 30 days of the year end. Would the CRA accept a loan which provides that any interest not physically paid by that date be deemed paid by an advance from the lender to the borrower bearing interest at the prescribed rate at that time?

As an example, assume a "loan for value" was advanced in the amount of $100,000 when the prescribed rate was 3%. The $3,000 interest payment was remitted by January 30 of all prior years, but was overlooked in respect of 2006. The amount of $3,000 was therefore deemed to be a new loan, bearing interest at the 5% rate applicable on January 30, 2007. On May 15, 2007, the borrower remits a payment of $3,043.56, being the $3,000 loan deemed advanced January 30, 2007 plus $43.56 of interest ($3,000 x 5% x 106 days from Jan 30 – May 15, inclusive, divided by 365 days). The borrower continues to pay $3,000 of interest annually, by January 30 of each subsequent year.

Would the Agency accept that there have been two loans, both of which bore interest at the appropriate prescribed rate with interest paid in timely fashion, such that subsection 74.5(1) exempts the earnings on the borrowed funds from the attribution rules?

Response

The exception to the attribution rules per subsection 74.5(1) ceases to apply if interest payable on the loan in respect of any year is not paid within 30 days after the end of the year, even if the interest is subsequently paid.

It is a question of fact as to whether or not a particular amount is paid and the Agency is prepared to look beyond one particular piece of evidence to determine whether the borrower has effectively transferred an amount to the lender on account of the interest due.

In our view, a loan created in the event of unpaid interest does not constitute payment of interest but would represent a deferral of the payment so required.

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9) Where an EPSP has made a bonafide loan to the corporation that created the EPSP would the Agency ever consider that paragraph 12(1)(n) could apply to recharacterize the loan amount as income on the basis that it considers the bonafide loan as "any amount received out of or under an employees profit sharing plan"?

Response

The CRA may question whether or not the arrangement is an Employees Profit Sharing Plan ("EPSP") as defined in subsection 144(1) of the *Income Tax Act*. It is questionable whether an EPSP exists where the trustee of the trust purporting to be an EPSP lends the funds back to the employer. The CRA will consider the purposes of the series of transactions and their effects under the Common Law or the Civil Code, depending upon which one is applicable, and when the amounts paid to the arrangement are returned, in one form or another, to the employer. Subsection 245(2) may also be considered depending on the facts and the circumstances.

10) Subsection 85(7.1) provides for the Minister to permit a taxpayer to amend a previously filed T2057 election. In accordance with the preamble of this subsection, the Minister must form the opinion that the amendment is "just and equitable". Does the CRA have any guidelines, internal or published, that the taxpayer and their advisors may use to distinguish between the circumstances where "just and equitable" permits an administrative amendment, and those situations that require a rectification order? For example, where promissory note consideration exceeds hard adjusted cost base in ss.84.1, (reference the Dale case), is a rectification order necessary, or will the CRA accept an amended election without more?

Response

Guidelines exist in the Information Circular IC 76-19R3 as to when it would be "just and equitable" to accept late or amended elections. Those specific references are provided at paragraphs 16, 17, 18 and 19.

However, the Canada Revenue Agency does not have authority to amend contracts between parties. For example, filers have the right to amend an election under section 85 of the *Income Tax Act* if the purpose is to amend their "agreed amount" and not to amend the terms of the underlying contract. When an amendment to an election is dependent on changing a fundamental aspect of the contract, it will be necessary to obtain a rectification order.

CRA may oppose applications to obtain rectification in the courts in circumstances where we are not satisfied that the original intentions of the contracting parties are being respected. This will include amendments to achieve after-the-fact tax planning results. We may choose not to oppose an application

for rectification where the amendments are integral to achieving the original intentions of the parties.

A court order will be required in any circumstances where an amendment to the election requires a retroactive change in the fundamental basis of the contract or where the change is based on correcting a corporate error. The CRA should be advised whenever a filer will be seeking a rectification order in respect of a filed return or election. This may be done by informing the auditor on the case if it concerns the basis for a proposed adjustment or by informing the ADA of the filer's TSO.

In the past we have made administrative concessions because section 85(7.1) had interpretational issues regarding what exactly may be changed. However, the law has been clarified that we cannot make retroactive changes without the benefit of a court order.

Cases such as Juliar and Sussex Square Apartments have provided clarification that Revenue (CRA) is bound by court orders and may, subject to statute-bar limitations, be required to make retroactive assessing changes. The *Interpretation Act* was amended to include section 8.1 which provides more explicit statutory recognition of the fact (from the case of Legeaux et Freres) that the Income Tax statutes are subject to the action of common and civil law that concern commercial law. That is, in general, the common law or civil law of a Province applies first relative to commercial transactions and then the income tax consequences flow from that.

Generally speaking, promissory notes are frequently the source of problems on rollovers because of the restriction in paragraph 85(1) (b), that the elected amount cannot be less than the non-share consideration. While shares are variable in value with the assets of a company, the non-share consideration represents "fixed" value and, therefore, immediate proceeds. This is the problem as well with subsection 85(7.1), because we cannot amend anything other than the "agreed amount". We have no power to amend the consideration or the type of consideration as that is a matter of the contract. In that circumstance, the legal contract must be amended and the only route is through an application for a rectification order to the court.

Valuation Clauses: Where the value of the assets transferred may be subject to a valuation adjustment, and thus affect the amount of the consideration and the "agreed amount" in an election, the parties to the contract may include a valuation clause to permit an adjustment based on a determination of value at a later time if that becomes a matter of dispute. In the circumstance where such a "valuation clause" is included in the original contract, this becomes a part of the contract and the parties may pursue such amendments within the parameters of such a clause, without a court order. An essential element of this policy is that the CRA must be notified in advance of this "valuation clause"; this is normally accomplished by filing a copy of the contract with the election form. This policy is a result of court guidelines provided in the case of Guilder News Co., (73 DTC 5048). Guidelines are provided in Interpretation Bulletins IT-169 and IT-405.

11) Is the CRA committed to using the "Short Cut Method" for excess capital dividend elections under Part III prior to issuing a Notice of Assessment? If so, prior to the CRA auditing the taxpayer, may taxpayers use this method, rather than ss.184(3) that requires the following:

a) Canada Revenue Agency Capital Dividend Election Form T2054 in duplicate together with attached Calculation of capital dividend account;

b) Certified copy of Directors' Resolution authorizing the Corporation to elect pursuant to subsection 184(3);

c) Letter from the Corporation electing under subsection 184(3);

d) Certified copy of Directors Resolution authorizing the Corporation to elect pursuant to subsection 184(3) of the *Income Tax Act* (Canada) (the "Act");

e) Schedule of information required by Regulation 2106(a)(iv);

f) Certified copy of Declaration of Directors of the Corporation declaring that the shareholder concurs with the making of the separate dividend election pursuant to subsection 184(3) of the Act, with concurrence of the shareholder attached thereto; and

g) T-5 Statement of Investment Income for the taxable dividend.

h) T1 incorporating the taxable dividend into the shareholders income.

Response

The Short Cut Method is an administrative practice that is currently in place to allow corporations who have filed excessive capital dividend elections to treat the excess portion as a taxable dividend in the hands of the shareholders, without requiring the assessment and subsequent reversal of Part III tax, and without requiring the documentation indicated in Regulation 2106 of the *Income Tax Act*. Note that as the Short Cut Method is not specifically governed by *Income Tax Act* legislation, it is subject to review at any time, and as such the CRA is unable to provide an open-ended "commitment" to this process. More appropriately, we can confirm that it is current policy to accept the Short Cut Method as an alternative to the legislatively sanctioned 184(3) election provided for in the *Income Tax Act*. It should be noted, however, that the CRA determines whether the circumstances of a specific case warrants the usage of the Short Cut Method, and it is up to the discretion of the officer processing the excessive election to decide if the Short Cut Method is appropriate in each situation. Further, if the processing officer determines that the Short Cut Method is not appropriate in any given situation, the corporate taxpayer would then be required to provide the full documentation according to Section 184 and Regulation 2106 of the *Income Tax Act*.

12) Administrators of the Scientific Research and Experimental Development Program for the CRA advise that information contained in normal business records should be sufficient to support a claim for eligible SR&ED expenditures and related investment tax credits. Record keeping systems maintained by the majority of claimants are designed to support the determination of income for income tax purposes. The level of support for eligible SR&ED expenditures linked to the work contemplated by subsection 248(1) appears to be inconsistent with the normal business records theory and the administrative practices of CRA.

a) Is this policy only intended for first time claimants?

b) If the policy is not only intended for first time claimants, then the actual field experience of administrative practices of CRA appears to be contrary to the stated policy related to compliance burden as auditors frequently require documentation in excess of that kept for normal business purposes. What steps will CRA take to ensure that the administration of the SR&ED documentation requirements is consistent among claimants?

c) Although the courts have consistently accepted the validity of credible verbal evidence, CRA administrative practice denies acceptability and is reluctant to assess the credibility of the parties supplying the information. Technical Reviewers are more inclined to discuss technical matters with technical personnel but want written proof, not verbal evidence, and will refuse a claim despite physical evidence (like a prototype) and verbal evidence by those doing the work where written records of the work done is meagre. Financial Reviewers want direct written evidence produced at the time the work was done that references the task level work, using the same labels used to describe the work in the Science Description submitted with the claim. Without this your claim has a high probability of denial as being "unsubstantiated".

In light of the incentive nature of the SR&ED Program, is CRA open to considering a balanced approach between written and verbal evidence?

d) How does CRA reconcile the trend towards increased documentation for SR&ED claims with the stated objectives in the 2007 Federal Budget and various CRA publications addressing the issue of reducing the cost of compliance?

Response

Subsection 230(1) of the *Income Tax Act* (ITA) requires "[e]very person carrying on business …[to] keep records … in such form and containing such information as will enable the taxes payable … to be determined." It is important to note that the purpose of record retention is to determine "taxes payable" and not income for income tax purposes. Record retention in respect of the Scientific Research & Experimental Development (SR&ED) Investment Tax Credit (ITC) is covered in the ITA.

In determining the eligibility of a SR&ED claim, the Research & Technology Advisor (RTA) will assess the work claimed against the definition of SR&ED found in subsection 248(1) of the ITA. The Financial Reviewer (FR) will ensure the eligibility of the expenditures. Together the RTA and the FR will ensure there is a link between the cost and the activity.

The primary focus of record systems is financial and they are used to determine income for income tax purposes and various sales-based taxes. There may be some information in the financial records which may support a SR&ED claim in other cases there may be little or no information in the financial records relevant to supporting the SR&ED work. In such cases where the financial records do not support the SR&ED work or the linkage between the expenditure and the activity,

the CRA will request contemporaneous evidence to support the claim. This other documentation and information may be material that the taxpayer has kept for himself that can also be used to verify the claim. The comments from CRA regarding normal business records were never intended to apply to situations where the taxpayer keeps nothing except financial information but rather that the CRA would attempt to use whatever the taxpayer had with the understanding that a taxpayer performing SR&ED will be keeping some other documentation of that effort for his own purposes.

This evidence will be outside the financial records and may include: background literature related to the objectives and the SR&ED plan, project plan and objectives, notes on hypotheses and tests on experimental procedures and test results, project note books, progress reports and final project reports, photographs of the experiment, technical drawings, prototypes of equipment, and scrap production. As the project description is not contemporaneous information, it alone is not considered supporting evidence. Where there is a failure to provide relevant supporting evidence, it will likely result in the disallowance of the claim.

(a) **Regardless of whether the claimant is making their first claim, there must be evidence:**

- **that the work took place**
- **when the work took place**
- **that there was a systematic investigation and**
- **the nature of the work performed.**

Verbal evidence alone is not usually sufficient to support the claim. Verbal evidence will usually corroborate the other evidence and it will not contradict the other evidence.

Where there is no evidence to support the technical aspects of a claim, only financial transactional information, or if there are inconsistencies between the different pieces of information, the acceptance of any claim is at risk.

(b) **The CRA is concerned about inconsistencies in the administration of any of the legislation it administers. Consultations with small business have identified the issue of SR&ED documentation requirements. To address this, when the CRA issues publications it will include explanations of issues relating to documentation and the taxpayer's responsibilities.**

(c) **Jurisprudence demonstrates that the courts view documentation as cogent evidence of SR&ED. Verbal evidence alone may not be sufficient to substantiate a SR&ED claim. We encounter cases where the documentation contradicts the project description and/or the verbal explanations. This may include when and where the work took place. A prototype by itself does not support that it was built for its technological content, when it was made and who produced it. As with other types of claims (eg., RRSP deductions) requiring conditions be met for qualification, if they are reviewed by the CRA, they will not be allowed solely on the basis of oral evidence.**

(d) **The SR&ED program provides various outreach services and is committed to reducing the compliance burden in its small business action plan, which will make the SR&ED program easier to access. Through these services, taxpayers will have greater understanding of the program enabling them to make proper decisions to support their SR&ED claims.**

Generally, documentation created during the process of performing your SR&ED should be sufficient to substantiate a claim; thereby we are not requiring additional documentation and this is consistent with the objective of reducing the cost of compliance.

13) CRA Financial Reviewers have recently undertaken to require SR&ED Claimants to justify expenditures claimed by reference to the appropriate provisions of the *Income Tax Act*. At this point, the requests have been directed towards the identification of overhead expenditures by reference to the appropriate provision of the Income Tax Regulations. We have now seen it being extended to section 37 expenditures and even within the SR&ED definition section of 248(1) between (a),(b),(c) versus (d).

Is this trend intended to create a rationale for denial of misclassified expenditures where the eighteen month period has expired? What is the purpose of requiring the specific identification of the legislation?

Response

To qualify an SR&ED claim must fit within the legislation. When assessing the eligibility of a SR&ED claim, the CRA takes the following steps:

1. **Ensure the work meets the definition of Paragraphs 248(1) (a-c).**

2. **Verify any work that is considered support work under Paragraph 248(1) (d).**

3. **Identify any work that is specified in Paragraphs 248(1) (e-k) has been excluded from the claim.**

4. **Verify the cost allocation on a project by project basis and in a manner that is consistent with the financial legislation.**

The need to separate support work under Paragraph 248(1)(d) from Paragraphs 248(1)(a-c) work arises because Para 248(1)(d) work cannot stand alone, it must be linked (commensurate and directly in support) to Para 248(1)(a-c) work. Further, Para 248(1) (d) identifies eight specific activities that maybe considered support activities. The CRA is concerned that any support activities claimed meet these tests.

There are many limitations placed upon the financial expenditures, and the consequences can vary, depending on the type of expenditure. To qualify as overhead and other expenditures the cost must qualify under the "directly attributable" rules found in Regulations 2900(2) and (3). The criteria are different if the expenditures are for:

- **the provision of premises, facilities or equipment or**

- **other expenditures that may not have been incurred if the SR&ED had not taken place.**

When a claim is prepared under the traditional method, the line for overhead and other expenditures may have been used as a "catch-all" category with contracts and/or materials included at this line. CRA reviewers are requesting this information to ensure that the expenditures have been properly categorized, all of the implications have been correctly recognized, that no ineligible costs are included, and to educate the claimant on the correct reporting for future claims. It is important for the taxpayer/claims preparer to understand how the work or expenditures claimed fit within the legislation to avoid problems if the claim is reviewed.

An expenditure identified within the filing deadline, on the prescribed form, but reported on the wrong line will, provided the rest of the claim is a complete, not be disallowed. The expenditure would be corrected prior to (re)assessing the return.

14) The federal government recently announced that the SR&ED program will be promoted and expanded. One of the announced measures was an increase in the number of technically experienced reviewers (presumably meaning engineers and the like). What is the CRA action plan to hire these individuals and what time frame is this to be implemented?

Response

The 2008 Federal Budget included an additional $10 million annually to allow the CRA to implement an action plan to improve the administration of the SR&ED program by increasing the CRA's scientific capacity and improving its services to claimants. Included in this funding was a commitment to increase the number of technical reviewers who determine scientific eligibility and provide some of our advisory services.

The money must first be allocated and a plan is currently being developed that should see the CRA bringing these individuals on staff in the later half of this fiscal period (ending March 31, 2009). Once they are hired, they will receive training and gain experience before they become fully effective.

15) What specific Sectors currently have 'specialists' in place and manned? In public forums, CRA is constantly exposing the need for transparency and openness. Yet attempts to contact a National Sector Specialist directly have been refused by individuals in CRA . Please comment on the process for advisers to access the National Sector Specialists.

Response

The group called "Industry Specialist Services" is responsible for over 20 industries. There are currently 15 specialists in place who are responsible for issues of national concern related to their industries. They are located close to the hub of the particular industry of specialization, if possible. For example, the two

oil & gas specialists are located in Calgary. The following is the organization chart for Industry Specialist Services, which is organized into three groups: Financial Industries, Manufacturing and Service Industries and Resource Industries.

Industry Specialist Services:

Financial Industries

John Luck, Coordinator (613) 957-3626
Vacant, Assistant Coordinator

Financial Industries Specialists

Angelo Bertolas - Banking
Emidio De-Angelis - Banking
André Gauthier - Financial Services
Margaret McCreery - Insurance
Doug Watson - Financial Products
Bill Tryon - Insurance

Manufacturing & Service Industries

Joanne Verkerk, Coordinator (613) 952-0607
Jean Gagné, Assistant Coordinator

Manufacturing & Service Industries Specialists

Tony DiBartolomeo - Automotive and Other Manufacturing
Bill Dobson - Health and Public Sector
Vacant - Construction & Real Estate
Bill MacGregor - Agriculture, Aquaculture and Fisheries
Tim Truckle - Pharmaceutical, Chemical, Food, Beverage, Tobacco, and Alcohol

Resource Industries

Jane Stalker, Coordinator (613) 957-3626
Vacant, Assistant Coordinator

Resource Industries Specialists

Bernard Ross - Forestry & Mining
Cheryl Hildebrand - Forestry & Mining
Zul Ladak - Oil & Gas
Peter Lee - Oil & Gas
Bob Seney - Media, Telecommunications & Utilities

Please note that other areas of CRA, for example Appeals, also have specialists who deal with their particular circumstances. However, the ISS industry specialists have a broader mandate which includes dealing with all areas within the CRA, other government departments (domestic and foreign) and, of course, Industry. The ISS specialists are Industry's window to the CRA.

In respect of the process of accessing Industry Specialist Services, it has been our experience that our specialists are accessible to advisers. However, if there is an ongoing audit, the first contact at CRA should be the audit manager. Also, because of the small size of Industry Specialist Services, it is usually more efficient for Industry Associations, such as SEPAC (Small Explorers and Producers Association of Canada) or CAPP (Canadian Association of Petroleum Producers) to raise industry wide issues with the specialists.

Given that we have not been aware that accessibility to the specialists is a concern, we ask that anyone who has a specific situation where it was a concern to contact the appropriate coordinator noted above so that any such concerns can be appropriately resolved.

16) An August, 2007 CRA Release (2007-0240201C6) notes that where the CRA Appeals Branch and the taxpayer have not been able to reach a settlement, taxpayers may consider mediation as an option, rather than immediately filing an Appeal with the Courts. Could you please provide an update on your experiences with mediation?

Response

As you may know this redress program began as a pilot project in the late 1990s with the objective to enhance the administrative appeals process for both the client and CRA. Procedures were developed in consultation with internal and external stakeholders. The pilot program area was later expanded to all regions and more recently added to the CRA external web site. To date there has only been one case where this process was utilized, that being a valuation issue and both parties were satisfied with the outcome.

17) New Guide RC4420 permits taxpayers to file a complaint with CRA on Form RC193 with respect to service.

a) If a taxpayer was having an undue delay with respect to obtaining a Clearance Certificate to permit the wind-up of an Estate, would this be the type of situation that could be addressed?

b) What other situations would be addressed under this Guide?

Response

a) The first thing that ought to be examined is whether or not the taxpayer/representative has attempted to resolve the issue with the area/supervisor responsible for the service (Estates & Trusts). If he/she has exhausted that avenue, the taxpayer/representative may then file a formal service complaint. Once received, the complaint would then be referred to the Business Line responsible for the service (Estates & Trusts in the present example), who would then determine if the delay is indeed undue and respond to the taxpayer/representative. The important thing to remember is that the Business Line is responsible for resolving the complaint—that means addressing all the issues that the taxpayer/representative have complained about, not necessarily making the complainant "happy."

b) RC 4420 is a very comprehensive publication and on page 3 (under the heading *"Is this pamphlet for you?"*), it clearly spells out the normal conditions that could lead to a taxpayer filing a service complaint, such as:

■ Mistakes, which could refer to misunderstandings, omissions or oversights;

■ Undue delays;

■ Poor or misleading information;

■ Staff behaviour.

Before you consider this complaint process, <u>you must</u>:

■ First, try to resolve the issue with the employee you have been dealing with (or phone the number you've been given); and

■ then, if you are not satisfied, talk to the employee's supervisor.

18) On March 29, 2007 CRA noted that partnerships will not have to file a partnership Form T5013 even if one of the partners is a corporation or trust, regardless of what the 2007 Guide T5013 said.

The Release also said that CRA is considering a change to their Administrative Policy under these circumstances; however, it has not yet been implemented. Please update us on the status of this matter.

<u>Response</u>

A similar question was asked in the 2007 Roundtable regarding the error in the filing requirements for partnerships. The CRA released the following statement as was noted in Tax Topics #1830 released on April 5, 2007:

CRA Correction to Notice Re Partnership Information Returns

CRA would like to make a correction to information provided in a previous "Notice to the reader" posted on March 27, 2007.
The message [was] pertaining to Partnerships having to file a T5013 information return where there are five members or fewer, and at anytime during the fiscal period of the partnership, any of the members was a corporation or trust. This item is incorrect and should be disregarded.
At this time, the CRA is considering a change to our administrative policy, however it has not been implemented. Sufficient notice will be provided allowing affected partnerships to make the required changes that would allow them to meet the obligation.

Currently the CRA is still reviewing its administrative policy with respect to this issue.

19) A number of taxpayers were assessed a penalty for remitting their source deductions at CRA, rather than a financial institution, as was required in their circumstances. A penalty was applied even though CRA may have received the funds

early. This issue has been addressed in the February 26, 2008 Federal Budget. However, with respect to previous penalties, is there any scope for a waiver of the penalty, especially if the funds were in CRA's hands in advance of the due date?

Response

Prior to the legislative proposal (Feb 26, 2008) a threshold 2 remitter was required to pay their remittance at a financial institution, whether it was paid early or not. If they did not comply they were assessed a 10% penalty for not complying with the ITA. However, in November 2007, following the Minister's decision, CRA began reviewing all penalties assessed as of January 2007 to determine if discretion can be applied, on a case-by-case basis. Early payments were also being reviewed and in cases where the penalty would not be cancelled, the penalty rate of 10% would be adjusted to reflect the graduated rates of:

3% for late payment within three days of the due date
5% for a payment that is four or five days late
7% for a payment that is six or seven days late
10% for a payment that is eight or more days late

As a result, all penalties were reviewed and discretion was applied on a case-by-case basis and if a penalty was not cancelled in it's entirety, the employer should contact CRA in writing in order to have his account reviewed again. The office contact is as follows:

Nova Scotia TSO - Sydney Site
47 Dorchester Street
Sydney NS B1P 6K3

20) The 2007 Federal Budget permitted Canadian-Controlled Private Corporations to file its income tax installments on a quarterly basis if they meet certain criteria such as having taxable income for either the current or previous year not exceeding $400,000. One other criterion is that the CCPC has no compliance irregularities. Could you please discuss what you would consider a compliance irregularity?

Response

We consider you to have a perfect compliance history if, during the previous 12 months: you remitted on time all the amounts required for income tax, GST/HST, Canada Pension Plan contributions and Employment Insurance premiums; and you filed on time all returns required under the *Income Tax Act* or under Part IX of the Excise Tax Act (GST/HST).

21) Could a person who is age 71 in 2008 who had previously matured his/her RRSP under the old rules repay the RRIF payments until December, 2008, such that they will not have to be included in income on the 2008 return?

Response

The *Budget Implementation Act*, 2007, (Bill C-52), which received Royal Assent on June 22, 2007, included changes to the definition "minimum amount" under a RRIF in subsection 146.3(1) of the *Income Tax Act* (the "Act"). Certain changes are transitional and affect RRIF annuitants who turned 70 or 71 in 2007, or who turn 71 in 2008. Specifically, the 2008 minimum amount is zero if the annuitant on January 1, 2008, turned 71 in 2008. This is provided for in paragraph (b) of the coming-into-force (CIF) of the change to the definition "minimum amount".

Therefore, such an annuitant who does not want the payment that would have been the 2008 minimum amount paid to him or her should instruct the RRIF carrier not to make that payment. As the legislated minimum amount is zero, the carrier should follow the annuitant's instruction. This ensures that the amount will not be included in income.

Although the law provides that the 2008 minimum amount for these annuitants is zero, some of these annuitants may still be paid the amount that would have been the 2008 minimum amount. Consequently, the new law also includes certain transitional changes to the meaning of "eligible amount of the taxpayer for the year in respect of registered retirement income funds" in clause 60(l)(v)(B.2) of the Act.

Paragraph 60(l) of the Act is the provision that allows a taxpayer to deduct certain amounts in computing income for a year if certain amounts are included in income for that year, and in that year or within the first 60 days of the following year, the taxpayer makes a contribution to an RRSP, a RRIF, or uses the amount to purchase an eligible annuity described in paragraph 60(l).

So, for 2008, the amount that would have been the 2008 minimum amount is an "eligible amount" under clause 60(l)(v)(B.2) of the Act if it is paid to an annuitant who turns 71 in 2008, and included in his or her 2008 income. The annuitant can use this amount to make a deductible contribution to an RRSP, a RRIF, or to purchase an eligible annuity, thereby ensuring that the payment will not increase 2008 taxable income.

The amount paid in 2008 that would have been 2008 minimum amount has to be reported in box 16 of a 2008 T4RIF slip. If the annuitant contributes part of this amount to an RRSP, a RRIF, or uses it to purchase an annuity, an official receipt must be issued to the annuitant.

The annuitant includes in income on line 115 of his or her 2008 tax return the amount shown in box 16 of the 2008 T4RIF slip. If that amount is contributed to an RRSP, the annuitant completes Schedule 7 and deducts the amount on line 208 of his or her 2008 tax return. If that amount is contributed to a RRIF or used to purchase an annuity, the annuitant deducts the amount on line 232 of his or her 2008 return.

> **Please refer to the 2007 Budget Questions and Answers at the following websites:**
>
> **http://www.cra-arc.gc.ca/tax/registered/budget2007-e.html#T4RIF**

http://www.cra-arc.gc.ca/tax/registered/budget2007-e.html#minimum

22) Where an individual has received a foreign pension which has foreign taxes withheld, and the pension is split with the spouse under the new pension splitting rules, can the foreign taxes withheld be split on the same basis? We understand that Canadian source deduction taxes **must** be split between the spouses.

Response

Section 60.03, subsection 56(1), and subsection 153(2) effectively treat any split-pension amount as pension income to the pension transferee and the portion of the tax deducted or withheld in respect of the split-pension amount as tax deducted or withheld on account of the pension transferee.

Where the foreign pension income qualifies as pension income eligible for income splitting under the Canadian income tax and the pensioner and the pension transferee have jointly elected under section 60.03 to split such foreign pension income any foreign tax withheld may also be split on the same basis.

Pension income splitting would not be allowed for the following types of income:

- **Foreign pension income that would not qualify as pension income for the Canadian income tax,**
- **Foreign pension income that is tax-free in Canada because of a tax treaty, and**
- **Income from United States individual retirement account.**

Reference:

1) **Form T1032**
2) **RC4018, Electronic Filers Manual for 2007 Income Tax Returns, February 2008, "What's New?"**
3) **General Income Tax and Benefit Guide-2007, page 17, "Line 115 – Other pensions or superannuation… Pensions from a foreign country"**
4) **Form T1 5000- D1, Federal Worksheet: T1-2007, "Line 314 – Pension income amount"**
5) **Ernst & Young's Guide to Preparing 2007 Personal Tax Returns, Chapter 2, Pension and other income**
6) **Finance Consolidated Explanatory Notes, section 60.03, subsection 56(1), and subsection 153(2)**
7) ***Income Tax Act*, Part I, section 60.03, subsection 56(1), subsection 153(2), subsection 118(3), subsection 118(7) and 126(1)**

23) Do you have any comments on the application of the new restrictive covenant proposals which are to take effective for transactions after October 7, 2003?

Response

We have no comments to make at this time.

24) Now that the February 8, 2007 Tax Court of Canada case (Greber Professional Corporation vs. M.N.R., 2006-1418(CPP)) is more than a year old, do you have any guidelines or comments with respect to owner-managed corporations using employee profit-sharing plans with the implication of avoiding Canada Pension Plan payments?

Response

The Agency is not in a position at this time to provide guidelines or additional comments as we are currently consulting with stakeholders in cases where EPSPs are established for reasons of tax planning, income splitting, and avoidance of CPP contributions or EI premiums.

25) Where a taxpayer has not previously filed forms such as Form T5018 (construction reporting), or Form T1135 (foreign investments over $100,000), or any of the other multitude of forms, is it possible to make a Voluntary Disclosure even though the current form is not one year late? Please provide some comments with respect to Voluntary Disclosures as they relate to late forms.

Response

IC00-1R2 paragraph 39 states that the disclosure must include information that is:

i) at least one year past due, or

ii) less than one year past due where the disclosure is to correct a previously filed return or where the disclosure contains information that also meets the condition of (i) above.

If the disclosure includes other returns or forms that are at least one year past due, the current form, although not one year past due, can be included in the disclosure pursuant to IC subparagraph 39 (ii).

IC00-1R2 paragraph 35 indicates that to satisfy the completeness criterion, a taxpayer must disclose all taxation years or reporting periods where there was previously inaccurate, incomplete, or unreported information relating to any and all tax accounts with which the taxpayer is associated. Should this result in disclosure of returns or forms more than one year past due, the current year returns or forms may be included.

26) Registered Retirement Savings Plan letters

Could we have an update with respect to the many letters that were sent by CRA to RRSP contributors noting that they “may have” RRSP excess contributions subject to a tax of 1% per month?

Response

At this time, there is no HQ approved response to this query.

27) Can CRA offer practitioners a process to use when applying for a Business Number for a newly incorporated company that is more efficient than present? Currently, when a client incorporates a company, we apply for the Business Number and wait for a letter from CRA advising of the number. In some circumstances the letter advising of the Business Number has not arrived prior to the first income tax return filing deadline. We call the CRA for the number but are advised they cannot release it to us as we do not have authorization (although we were the representative that completed and filed the form to request the number). If the return is filed leaving the Business Number blank on assessment a number is assigned which is different from the Business Number that was assigned as a result of the initial request. This requires the process of merging these two accounts.

Response

For the Prairie Regional Correspondence Centre, accountants have been provided with the 1-866-218-4847 number to call when the expected turnaround time of 5 business days plus mailing time has been exceeded or the registration is extremely urgent.

Accountants can also indicate on the registration form that they would like a call to advise them of the Business Number once registered.

When the accountant will be the ongoing authorized third party representative for the client, they may submit a completed RC59, Business Consent Form, along with the RC1 registration request to the Correspondence Centre, either by fax or by mail. The updating of the authorization will be performed in conjunction with the registration. The RC59 is not required if the accountant has submitted the RC59 on a previous occasion and recorded in CRA systems.

Representatives contacting the CRA post-registration will only be given access to the BN if they have been authorized via RC 59 to obtain information by their client. Business Enquiries agents responding to account specific enquiries from a third party representative are required to apply confidentiality measures and ensure the representative is properly authorized on the account before releasing account information, inclusive of the BN.

28) CRA's recent "matching" of slips to returns program in the last couple of years has generated many automatic reassessments with an additional "failure to report income" penalty. There are instances where income is reported on different returns and in different percentages due to simple trust arrangements, which is compounded by the fact most information slips (T3s, T5s, T5013s, etc.) only have space to report one SIN. From an administrative perspective, is it possible to contact the taxpayer, or their tax advisor where CRA is aware there is a professional tax advisor involved, before the reassessment is raised?

Response

We would first like to clarify that the CRA does not complete automatic reassessments for income that is shown on T3 or T5 supplementary slips. Matching cases that are identified for the non-reporting of income reported on T3 or T5 slips are always subject to a manual review by an assessor. The CRA uses a comprehensive computer routine to identify potential instances of unreported income. In that routine there is a joint income check where we attempt to exclude situations where it is evident that the income has been split between spouses. For instance, where a financial institution advised us that an individual had a single T5 slip, we would review that taxpayer's account and the spouse's account. If we are able to determine that the two spouses together reported the full amount of the slip, we would not generate a case for review by an assessor.

Once a case is generated for review, the assessor attempts to resolve the case. This may involve looking at the paper return, reviewing the information sent to the CRA by the slip issuer, reviewing the spouse's return or verifying notes entered in our system during previous reviews (Notepad). If the foregoing does not resolve the discrepancy, our procedures are to contact the taxpayer or representative to reconcile the reporting of the T5 or T3 income. We strive to provide the taxpayer or representative with the opportunity to clarify the situation. However, the tax return may be adjusted if the requested information is not received within a specified timeframe or if we are unable to reach the individual or representative.

As a result of a concern brought up at the 2005 Ponoka forum, we made a commitment that we would do a controlled sample during the 2005 Matching program where contact would be made before a reassessment was processed to check if income had already been reported by or split with the spouse. 200 cases were completed using the special contact instructions, resulting in a 55% adjustment rate as compared to 59% for the 3,000 cases where our regular procedures were followed. The additional contact resulted in our clerks completing 1.38 files per hour versus 5.0 cases per hour for the remainder. As a result of this, it was concluded that the cost increase versus the benefit derived would be prohibitive if this was undertaken on a larger scale.

The Winnipeg Tax Centre took several steps to address concerns that you had raised in the past. For the 07/08 matching program, the matching work for T3 and T5 was conducted early on in the program to give taxpayers and representatives more time to get information. Sometimes it is difficult for the assessor to speak directly with a taxpayer or representative and we need to leave a message. To facilitate the exchange of information, we installed a local 1-800 line with voice mail. This allowed us to receive messages 24 hours a day, 7 days a week. Finally, we ensured that our staff made full use of the Notepad feature in our system. Notepad is used by our staff to record the details of any prior contact with representatives and taxpayers regarding interest splitting and reporting details. This will help to ensure that information gathered in the course of a review is taken into account in any subsequent reviews.

As mentioned above, we strive to ensure the accuracy of matching reassessments by contacting the taxpayer or representative as required. To avoid reversals, it is imperative that any requests for clarification be responded to expediently. One of our goals is to try to improve the reversal rate and the two measures we

implemented last year resulted in a decrease to the percentage of reversed reassessments. For the 07/08 program the reversal rate on T3 matching nationally was 4.28% and on T5 matching was 4.54%. For the WTC, the reversal rate on T3 was 5.71% and on T5 3.83%. For the 06/07 program the reversal rate on T3 nationally was 7.65% and on T5 5.97%. For the WTC the reversal rate was 16.5% and on T5 5.61%.

NOTE: Due to timing, reversals related to reassessments processed in one program are often counted in the following year. Also, in the 06-07 program, we completed significantly fewer reassessments related to T3 slips (2,976 versus 8,603 in 05-06). These factors inflated the 06-07 reversal rate as there were 441 reversals processed in 06-07 that related to 05-06 original reassessments.

HQ has been contacted to see if there are any future initiatives to deal with this problem. Some changes that are being considered that could mitigate the issues include the following:

(1) Require the issuer of the slip to capture the social insurance numbers of all account holders on the slips. A cost benefit analysis would need to be conducted to determine whether such a change would be warranted.
(2) Field 9919 that pertains to electronically filed (efile/netfile) returns should be completed for joint accounts (ie., % of slip). It is not mandatory for the taxpayer or agent to enter this information, however it is recommended in resolving some situations as our assessors refer to those keying fields when conducting their reviews.
(3) The agency is looking at various options related to the exchange of information electronically (E-docs). However, this analysis is in its early stages and we are some time away from implementation.

29) The new T2 corporate income tax form requests disclosure of the taxable capital employed in Canada for the previous tax year. For many small business clients we have never had to perform this calculation, although we clearly know the balance is less than $10 million. Will the CRA consider taking steps to add a box on the T2 return that can be checked indicating taxable capital is less than $10 million?

Response

There are two areas on the T2 return that touch on Taxable Capital Employed in Canada:

The first area is on page 2 where two questions at lines 233 and 234 ask if the TCEIC is over $10,000,000. If a corporation does not tick the "yes" box, then they are stating their TCEIC is less than (or equal to) $10,000,000. Adding another question on page 2 to ask if the TCEIC is $10,000,000 or less would be redundant.

The second area of the return that touches on TCEIC is in the "Small business deduction" area. In this area, corporations are instructed to calculate [(TCEIC minus 10,000,000) x 0.225%] and to enter the result at line 415. They are using the

TCEIC from the prior year in some cases and from the current year in other cases. If this is the concern, CRA could consider adding another instruction to this area rather than adding a question. The instruction could be just below line 415 that says: "If the TCEIC is $10,000,000 or less, enter 0 at line 415, otherwise, read the notes under the "* Large corporation" heading below."**

30) The CRA has implemented a new system and "standardized accounting system" recently. As such, CRA has transferred positive accounts balances (rather than refunding the amount) from a business's corporate tax account to the GST account (where at that moment in time their may be an amount owing) without any input of the taxpayer or the advisers. The taxpayer then files their GST return which shows balance and cheque attached with payment. CRA then subsequently issues a refund (generally without interest even when held longer than time period allowed) to the taxpayer, but the refund appears to come from the GST account. The taxpayer is not expecting such from the GST account. Taxpayers file their corporate returns and account for corporate tax on a separate basis than GST accounting. This creates numerous problems for taxpayers, not the least of which is the CRA is not following the directions provided on the returns filed by the taxpayer to refund the overpayment made on the corporate tax account. This also increases the administrative burden on taxpayers to track account balances where the CRA has transferred funds without confirming the transfer with the taxpayer in advance.

Please comment on the above and how the Agency intends to address the transfers between accounts which taxpayers have not initiated nor authorized.

Response

Per Subsection 164(2) of the *Income Tax Act* - Application to Other Debts: Instead of making a refund or repayment that might otherwise be made under this section, the Minister may, where the taxpayer is, or is about to become, liable to make any payment to Her Majesty in right of Canada or in right of a province, apply the amount of the refund or repayment to that other liability and notify the taxpayer of that action.

It's inevitable that since April 1, 2007, taxpayers will spend more time reconciling transfers between accounts. Details of offsets/allocations and transfers are reflected on statement of arrears.

The system may transfer reassessment pre-payments held in the non-filing period to a reassessed debt even though those pre-payments are protected. The corporation should advise us which particular tax year each pre-payment is intended for, so that we can transfer and protect pre-payments in a particular year. Once the pre-payments are protected in a particular year, the system wil not apply them to reassessed debts in other tax years. Soon, we will begin to contact corporations with pre-payments in the non-filing period to request that they specify the tax years to which these payments/credits are intended, however, corporations can contact us at any time to request transfers to specific tax years.

31) With the new standardized accounting provisions enacted in 2006, there are a number of issues that have arisen regarding the filing of corporate T2 returns for shelf corporations that are inactive. Presently the CRA is seeking corporate income tax returns for these corporations for the periods of inactivity. If the corporation is a shelf corporation that is inactive, what type of financial statements are expected to be filed on the return?

Response

The inactive corporation should be filing a Schedule 100 (Balance Sheet) and an entry in lines 200 280 and 200 282 indicating that the corporation is inactive for the filing period.

32) On the same issue as above, the CRA is now seeking corporate tax returns for municipalities that are exempt from income tax and holding GST refunds as part of the process of standardized accounting. What is the purpose of this? For how many years does the CRA require corporate tax returns?

Response

The purpose of this is to encourage compliance.

Per Subsection 164(2.01) of the *Income Tax Act* - Withholding of refunds: The Minister shall not, in respect of a taxpayer, refund, repay, apply to other debts or set-off amounts under this Act at any time unless all returns of which the Minister has knowledge and that are required to be filed by the taxpayer at or before that time under this Act, the Air Travellers Security Charge Act, the Excise Act, 2001 and the Excise Tax Act have been filed with the Minister. [S. 164(2.01) is added and comes into force on April 1, 2007.]

The CRA implemented an administrative position to ease the administrative burden for numerous corporate entities that are exempt from paying federal income tax under subsection 149(1) of the *Income Tax Act* and have not filed their required corporation income tax (T2) return in previous years. Corporate entities in the municipality, university, school, hospital, non-profit organization, federal crown corporation, and Indian band sectors will not have their refunds or rebates held for outstanding T2 returns with a fiscal period ending on or before March 31, 2008. This administrative position is for purposes of the automatic refund hold only and does not alleviate their legislative responsibility to file their annual corporate tax return.

However, failure by these entities to file T2 returns by their due dates for the taxation years ending April 1, 2008 and forward will result in a compliance refund hold on their refunds or rebates.

Registered charities, Hutterites, and provincial crown corporations are not required to file a corporation income tax (T2) return and are not subject to the provisions of the compliance refund hold.

The only thing that really has changed is that, because of the implementation of the compliance refund hold legislation, we as an Agency are now obliged to

withhold their refunds from other business lines such as GST if they are not fully compliant in their filing obligations. There was a recognition that this new legislation would force many tax exempt corporations, who never filed a return, to start filing T2 Corporation Income Tax Returns.

These corporations will not be able to file a T2 Short as they would not qualify as Canadian-Controlled Private Corporations. From a processing prospective, all that is required is the first page of the T2 return to be filled out and line 200 085 to be ticked with one of the four options as to the paragraph under which the corporation claims exemption from tax. However, normally we require financial statements to be filed in GIFI format (Schedules 100 and Schedule 125) or Schedule 100 only where a corporation has no income or incurred expenses during the year.

33) The CRA recently changed its procedures such that all Notices of Objection for Alberta registrants are sent to a "Western Intake Centre" in Surrey, B.C. We have seen a number of appeals transferred out of Alberta to tax services offices in other parts of the country that may not be as busy. While this may appear to be efficient from the CRA's perspective, it makes resolution of the appeal more difficult from the taxpayer's perspective. In our experience, the resolution of most appeals requires one or more meetings with the appeals officer to properly communicate and explain the nature of the business and the documentation. An appeals officer in a distant tax services office is generally unwilling to travel to Alberta to meet with a taxpayer. As a result, this critical part of the dispute resolution process does not occur unless the taxpayer and his advisor travel to meet the officer. Can the CRA comment on this?

Response

As you know, part of the Appeals mandate is to conduct impartial reviews, and because the office resolving the objection may be different than the one that raised the (re)assessment, the overall impartiality of dispute resolution process is improved. In addition, these Intake Centres (IC) concentrate large volumes of work, enabling improving overall resource utilization, as ICs can adapt more quickly to the peaks and valleys of the incoming workload, resulting in more effective timeliness resolving disputes. Generally, files will continue to be processed in the region from which they originated. In addition, ICs will continue to ensure centres of expertise are maintained, by distributing work to offices that have expertise in certain economic sectors, such as banking, insurance, and oil and gas.

A vast majority of files are resolved without the need for a meeting. We understand that sometimes face-to-face meetings are desirable and required to facilitate the resolution of a file. If it is determined that a face-to-face meeting is necessary, arrangements can be made with the closest service delivery point to facilitate this requirement. While there are very good reasons for a face-to–face meeting, we wish to reduce meetings where self-explanatory information is handed over to the Appeals Officer. When this happens the redress process becomes more expensive and less effective.

34) The CRA recently began issuing separate Notices of Assessment in respect of each reporting period covered by an audit, along with a summary showing the amount owing for all reporting periods together (*i.e,* the sum of all the individual Notices of Assessment). We would appreciate you confirming that a taxpayer may file a single Notice of Objection in respect of both the summary and all the individual Notices of Assessment where the taxpayer is objecting in respect of an issue included in all the Notices of Assessment.

Response

A Notice of Reassessment issued by CRA Audit Division may include assessments in respect of any number or combination of reporting periods and is made up of a "Results" page and one or more "Summary of (RE) assessment" pages.

The first page of the Notice of Re(Assessment) provides the combined results for the period covered by the audit. Each Summary page refers to the assessment for the reporting period identified.

The "Period Covered" field on the first page indicates the reporting period covered (when there is only one), the reporting periods covered when they are consecutive, and "Refer to Summary" when the reporting periods are not consecutive. That is to say if the box contains the dates of the audit period, it indicates in each consecutive reporting period within the audit period what has been assessed or reassessed. If it contains the notation "Refer to Summary", it indicates that one or more reporting periods has not been assessed.

Our position is that where the CRA has issued one Notice of (Re) Assessment that includes assessments in respect of a combination of reporting periods, Appeals will accept one Notice of Objection regarding any issue(s) included in those assessments. In the Notice of Objection, the taxpayer should specify the issue(s) and amount in dispute for each reporting period.

35) Officers of the Winnipeg Tax Centre are calling the accounting preparer of a corporate tax return requesting information pursuant to a “review” of the corporate tax return. We welcome the initiative to promote efficiency but have concerns with the timing of this process. The officers generally require their questions be answered quickly; however an immediate response may not be possible or may not fit a practitioner’s workflow. Often practitioners believe it is prudent to notify a client that CRA is requesting information with respect to details of or the composition of balances in the tax returns filed. Can the need for response time be communicated to the review team?

Response

We are aware that in some situations taxpayers, or their representatives, may not be able to respond within the usual 30 days for specific information and the corporation processing officers, upon request, have the discretion to allow for additional time to respond.

36) Has any action been taken with respect to the outstanding difficulties surrounding the change of a CA firm name or use of a CA firm trade name in the Represent a Client service? Our last understanding was that no other action was possible other than having every client sign a revised authorization form containing the new name.

Response

With respect to individual taxpayers (T1013), a request can be made to the CRA to update the name of the representative on the taxpayer's authorization automatically. The CRA needs details of the circumstances for the name change to determine if there was a change in the legal entity. If the documentation provided shows that the name change did not change the legal entity, the CRA may choose to update its records to make the necessary changes to the name of the representative on the taxpayers' file without requesting new T1013 authorization forms. The CRA may still require new authorizations if the documentation provided indicates that the legal entity did change. Requests to update the name of the representative may be faxed to Benefit Programs Directorate at 1-613-941-6120.

With respect to businesses (RC59), because of the complexity of CRA business programs, a request to make an automatic change to the name of the authorized representative cannot be accepted. This is because the BN (Business Number) system is considerably more complex than CRA's Individual Programs system and attempts at an automatic name update could potentially create greater problems. Therefore the CRA requires new authorization forms when an authorized business representative has a name change.

It may be worth pointing out that when a business is registered as a representative with the "*Represent a client*" service, the business name may be updated using the maintenance options available within the service. When the business name is updated that way, all individual and business clients who granted authorizations for *online* access, whether it was done online or using a paper authorization form (T1013 and RC59), the authorizations are automatically updated and there is no need to submit new authorization forms. This method of updating the name of the business does not require manual intervention from the CRA. However, because the update is transparent to the representatives' clients, CRA recommends that the representative advise its clients of the name change to avoid any confusion.

37) Can the CRA confirm that the Prairie Region Correspondence Centre in Regina, SK is providing verifications of a corporation's CDA (Capital Dividend account) upon request by taxpayers/ practitioners?

Response

The Prairie Region correspondence centre provides written confirmation of a corporation's Capital Dividend Account (CDA) upon written request of taxpayers and/or authorized representatives. The request must include the calculation of the CDA balance or an explanation of why the calculation is not included.

Confirmations are provided as a courtesy only and are processed on a first in first out basis.

38) Practitioners have encountered difficulties meeting the time limits set by the Agency for providing information pursuant to a post-assessing review, an audit or review request, and by the Appeals Division in the conduct of an appeal. More so than in the past, post-assessing review will not extend the response time. This situation is exacerbated by summer and early fall requests for information, given these fall during vacation times. Other review requests similarly will not or cannot be extended much beyond 30 days. While we understand that all information should be available at the time a Notice of Objection is filed so that the Appeals Division can commence their review as scheduling permits, in cases where the audit subject (corporation for instance) has since been sold or wound up, or in receivership, the ability to timely access information may be out of the client's hands. There is a perception that the CRA does not extend sufficient latitude for reply given the staffing shortages faced by professional firms.

It has not been uncommon that an appeals officer is unavailable for comment or question, and phone calls are not returned in the final week or few days prior to the officer's response deadline imposed on the client. The appeal is then terminated or the assessment confirmed for lack of information presented. A client must proceed to Tax Court for a full hearing regarding the client's situation.

We understand that practitioners have brought such matters to the attention of the Appeals Division team leaders over the past few years, but such situations continue. Please comment.

Response

The Appeals Division is firmly committed in resolving objections in a fair and impartial manner by reviewing all information pertaining to an issue(s).

Generally, we expect all requested information to be available at the objection stage. However, we do recognize that there may be circumstances where the taxpayer/representative requires additional time to gather the documents. We will consider on a case-by-case basis whether granting a reasonable time extension is warranted.

Taxpayers/representatives should contact the Appeals Officer upon receiving a request for information letter and discuss any potential delay(s) in providing the information. If the Appeals Officer is not available for comment or to answer a question, the taxpayer/representative should contact the Team Leader to discuss his/her concern.

39) What is the Fairness committee's position with respect to waiving the penalty, which can be $2,500, for a late-filed foreign reporting Form T1135? In a recent VIEWS**,** the Agency confirmed that the policy change to assess the penalty (rather than issue a warning for the first late filing) was not communicated to the public in 2006. Accordingly, practitioners and the public had no knowledge penalties were about to be assessed. The VIEWS suggested the Fairness procedure was the appropriate avenue for waiver of the

penalty. However, discussions with respect to Fairness requests in progress appear not to be favorable in this regard. Is the Agency giving consideration to the fact that taxpayers were not informed of a change in policy?

Response

Compliance Programs Branch (CPB), International & Large Business Directorate, the area functionally responsible for T1135 forms, has been reviewing the issue of waivers/administrative tolerances. CPB has decided not to establish an administrative policy to automatically cancel or waive the penalties on these information returns.

The Taxpayer Relief Operational support Section, Taxpayer Relief and Service Complaints Directorate, agree that a lack of knowledge of the law and the fact that no tax is assessed on the information returns are not grounds to grant relief. Information returns do not generally assess a tax amount, however, they have file due dates that are required to be met. The penalties are charged to promote compliance by taxpayers to ensure timely filing of such returns

Taxpayers seeking relief should follow the guidelines as outlined in Information Circular IC00-1R2 - Voluntary Disclosures Program and IC07-1 - Taxpayer Relief Provisions. The decision to waive or cancel penalties and interest should be made on a case-by case basis, taking into consideration the circumstances of each case.

40) Subsection 163(1) applies a 10% penalty for the second case of an unreported amount of income in a three-year period. Will the penalty apply in a situation where the first occurrence results in a refund or NIL reassessment? We are concerned about the harsh nature of this penalty in situations where the first failure to report income did not result in any underpayment of tax. Two scenarios are envisioned:

Situation A: In 2005 a taxpayer fails to report a T4 slip in his return of income. However, the tax deducted on the T4 caused a refund to be issued upon inclusion of the income. In 2007 the taxpayer fails to report a T5 slip and the reassessment does result in additional tax owing. Will the subsection 163(1) penalty apply?

Situation B: In 2005 a student who filed a voluntary tax return to claim the GST credit failed to report a T5 slip. However, the income inclusion was offset by unused personal tax credits available and a NIL reassessment was issued. In 2007 the taxpayer fails to report a T4 slip and the resulting reassessment does result in additional tax owing. Will the subsection 163(1) penalty apply?

Response

The correct reporting of net income is important as it is used in determining entitlements under the Canada Child Tax Benefit Program, the Goods and Services/Harmonized Sales Tax Credit Program as well as various other provincial programs that we administer. Net income is also used to determine certain non-refundable tax credits including those that other individuals may claim for a taxpayer. In addition to potentially understating taxes payable, under reporting

income increases the risk of taxpayers receiving excess benefits under these programs.

The intent of the 10% omission penalty in subsection 163(1) of the *Income Tax Act* is to address situations where income is repeatedly understated and can be applied even if the taxpayer has no tax payable. It applies only to a second or subsequent occurrence within a period of four years.

The Minister can, within reason, exercise some discretion in the application of the repeated failure to report penalty. The Minister has an undefined discretion in enforcing penalties based on policies adopted, so long as that discretion is exercised with good faith and respects the intent of the legislation. These policies can be subject to periodic review.

An important factor to consider for the Minister to exercise his discretion in the taxpayer's favour is that the taxpayer has made some reasonable effort to comply with the law. As such, an omission penalty would not be applied where the taxpayer was missing a slip but tried to reasonably estimate the amount. We regret that we cannot specifically comment on the two scenarios presented above.

Taxpayers can consider the following avenues of recourse should they find that an omission penalty has been levied against unreported income:

- **Call Individual Income Tax Enquiries to obtain details of how this penalty is applied.**
- **File an Objection indicating they disagree with the assessment and/or our interpretation of the law.**
- **Submit a request under the Taxpayer Relief Provisions. These provisions permit us to:**
  - **help taxpayers resolve problems that arise through no fault of their own, and**
  - **be more flexible and responsive to a taxpayer's circumstances when it would be unreasonable or unfair to penalize the taxpayer.**

More details can be found on our website at www.cra-arc.gc.ca.

41) After many years of accepting RC59 forms and other documents from corporate taxpayers when signed by an officer or director of the corporation without question, a new policy appears to have been put in place along with the new RC59 Business Consent Form, designed to allow "on-line" access to certain information. Part 5 of the form (Certification) states in part:

> "This form must be signed by an authorized person of the business such as ……. a director of a corporation, …."

The CRA is now comparing the name of the "authorized person of the business" on the form to its records and, where its records are incomplete, refusing to accept the RC 59 form, even if that form is only to replace a previous version of the RC 59 form which was

signed by exactly the same individual and only lacked the “online” consent provision. To our knowledge, this is not done with any other form or election required to be filed by a corporation, unless the “authorized person” is not an officer or director, in which case most forms usually make it clear that a copy of the authorizing agreement is to be provided along with the form.

The generic form letter that is sent out with a refusal to register a consent is unclear on what the problem is, and what needs to be done to fix it—for example, where a corporation incorporated in 1991 has been successfully filing with the CRA ever since was sent such a letter, the letter stated: “the authorized signature indicated on this form does not correspond with the name that appears in our records.” The form letter went on to say “Please enter any missing information or correct any inaccurate information on the form and return it to us as soon as possible”. While the letter went on to provide the name and phone number of a responsible staff member in the Business Number Services Unit, who when contacted was very personable and helpful, this contact might not have been required had the form letter been properly designed. What it should have said, in this case, was:

> *“We have no information in our system regarding the directors or officers for this corporation. Please provide us with a copy of the most recent Annual Return or Notice of Change of directors for the corporation along with the Social Insurance Number for each director, so that we may update our records and process this consent form”.*

The directors of an Alberta corporation are a matter of public record easily obtained from Corporate Registry. Will the CRA consider verifying the directors without having to reject documents? If an update of its records is necessary, the CRA could provide a form letter advising taxpayers exactly what corporate documents will be required to provide the necessary “proof” so that it will update its records and allow the RC59 to be processed.

Will the CRA consider making the necessary changes to its processes?

Response

Many taxpayers and taxpayer representatives believe new procedures were recently adopted for the processing of an RC59. However, the requirement to match the name on the RC59 form against the records in the BN System first appeared in the December 2001 Business Registration Procedures manual. This insertion was introduced to highlight the importance of conducting due diligence in processing this form. Further, the implementation of My Business Account and its Internet service offerings provided the Business Registration Programs Support Section with the opportunity to update the RC59 form. These updates included the option to request online access and to provide greater clarity of the certification area.

CRA uses the honour system when processing information returns and, depending on the type of return, advises clients the CRA has the right to conduct a subsequent review/assessment. The CRA cannot afford the same luxury to the RC59 since, once processed, it immediately provides CRA agents with consent to release confidential information to a third party. Therefore, the CRA must immediately verify the RC59 certification area against the CRA’s records.

Although federal and provincial corporate registries keep the names of directors/offices in their records, we are reluctant to use the information since there could be a delay with the corporate clients providing them with timely updates. Therefore, we request the information directly from corporate clients to ensure we receive the most recent information.

We are in agreement the wording of the RC59 follow-up letter needs improvement. The suggested wording *"We have no information in our system regarding the directors or officers for this corporation. Please provide us with a copy of the most recent Annual Return or Notice of Change of directors for the corporation along with the Social Insurance Number for each director, so that we may update our records and process this consent form"* is definitely more descriptive in identifying our needs and, as such, we are prepared to adopt it.

42) A July 4, 2007 press release by the Department of Finance indicated that the Minister of Finance had just announced draft amendments to make the tax system more efficient. It was announced that the new regulations would reduce delays in the preparation and issuance of T3 information slips relating to distributions of publicly traded trusts and T5013 slips relating to allocations from publicly traded partnerships.

We believe that part of this system is working reasonably well—that is, we have been able to find T3 information for clients on a timely basis for a number of publicly traded trusts, where investment managers had not prepared T3 slips for clients quickly. In some cases, public trust information posted to the CDS website early in January, 2008 had still not been passed on to taxpayers by their investment managers by the middle of March, some two months or more after they had it.

Has the CRA any information on whether T3 slips filed for 2007 were generally being received earlier than in past years; ie., has the change made the system any more efficient?

Response

As this is the first year with respect to the legislative change, it is still too early to comment on its success. We do know that not all entities were able to make the necessary changes to the systems to enable to post the financials by the due date. However in discussion with representatives of the Investment Industry Association of Canada (IIAC), they do believe the changes have helped their industry.

We are aware that there are still some concerns about the posting of the financial data and then making amendments after the 60/67 day deadline date. However this is a situation that existed before the legislation was introduced and will continue to be an ongoing issue.

(Note: The 60/67 day rule falls under Regulation 204.1(3). Public trusts must post information on or before the day that is 60 days after the end of the taxation year. The 67 day rule comes into effect when the public trust is, at any time in the taxation year, a public investment trust; these trusts would then have to post information on or before the day that is 67 days after the end of the calendar year.)

43) Possible 88(3) matter that appears unfair to some taxpayer's in certain situations.

Facts:

1. Canco is in the Oil and Gas business;

2. Canco forms a wholly owned subsidiary in country x ("Forco");

3. Forco is a controlled foreign affiliate of Canco;

4. Forco will be undertake various exploration activities;

5. Canco will make a capital contribution (through the purchase of treasury shares) of $50 million in Forco;

6. Forco used the $50 million in exploration activities that did not result in a discovery and, as such, the value of Forco is nominal;

7. Canco would like to realize a loss on its investment in Forco.

Under existing rules, Canco could liquidate and realize a capital loss in respect of the disposition of its shares in Forco. However, a proposal contained in a Department of Finance comfort letter (paragraph 6) dated April 12, 2006 states the following:

"any loss of the taxpayer resident in Canada from the disposition of a particular share of the foreign affiliate that was redeemed, acquired or cancelled by the foreign affiliate in the course of the liquidation and the dissolution would be deemed to be nil;"

This treatment appears to leave Canco at an economic disadvantage and does not allow Canco to obtain any benefit of the loss that has been realized.

Response

Under the proposed version of subsection 88(3) included in the draft legislation on foreign affiliates issued on February 27, 2004, paragraph 88(3)(c) deems the taxpayer's proceeds of disposition of the shares of the foreign affiliate to include an amount equal to the total of all amounts each of which is the cost to the taxpayer of a distributed property received by the taxpayer as a consideration for the disposition of the shares. In this respect, the cost to the taxpayer of property distributed to the taxpayer on the dissolution (other than an excluded property and a share of another foreign affiliate) would be deemed, by proposed paragraph 88(3)(b), to be equal to its fair market value. According to this version of subsection 88(3), there is no provision deeming a loss on the shares of the foreign affiliate that is liquidated to be nil.

Since the publication of the draft legislation on February 27, 2004, the Department of Finance issued some comfort letters indicating that some changes would be made to the *Income Tax Act*. Those changes have not yet been incorporated in draft legislation. We do not comment on comfort letters written by the Department

of Finance before they are incorporated in draft legislation. Requests for comments on comfort letters should be addressed to the Department of Finance.

If our understanding of the comfort letter of April 12, 2006 as it concerns subsection 88(3) is correct, the rules described in that part of the comfort letter (which include the deeming rule for the loss on the shares) would be additional and distinct rules applicable when certain circumstances are met and where a taxpayer elects in writing to have these rules apply. This loss denial rule is apparently similar to the loss denial rule found in paragraph 88(1)(b) of the *Income Tax Act* and operates when electing to transfer property of a wound-up foreign affiliate to its parent at its tax-cost. The comfort letter of April 12, 2006 does not indicate that the proposed legislation contained in the draft legislation of February 27, 2004 will be changed in other circumstances or where the taxpayer does not elect in writing to apply the new rules.