BUCHANAN BARRY LLP
CHARTERED ACCOUNTANTS

TAX NEWSLETTER

September 2013

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IMMIGRATING TO CANADA

Have you or a family member recently immigrated to Canada? Do you know someone who will be moving here?

There are many tax issues which the prospective immigrant should take into account. Consultation with a professional familiar with this field is always advisable. Below are some tips and traps to be aware of:

Tax on worldwide income

The most important thing to know is that, once a person becomes resident in Canada, they are **taxable on their worldwide income from all sources**, including foreign income. This will include, for example:

- pensions from the home country;
- interest being earned in bank accounts in the home country;
- gains from selling property in the home country.

You should also know that Canada now has tax treaties or "tax information exchange agreements" with over 100 countries. Canada continues to sign such agreements with more and more countries, specifically for the purposes of exchanging information; and new mechanisms for computerized exchange of information are going to be introduced in at least some situations. **Expect the Canada Revenue Agency (the "CRA") to find out** about pension income, bank interest, sales of real property and other sources of income in the home country. Taxpayers who do not report their income can be subject to severe penalties and even prison sentences.

Reporting foreign assets and trusts

All Canadian residents must state, on their annual income tax return, whether they have foreign property (cost exceeding $100,000), or, in some cases, whether they are beneficiaries of foreign trusts or own shares (directly or indirectly) in foreign corporations. Starting in the 2013 taxation year, the information required for reporting foreign assets and investments will be very detailed.

New immigrants need to take particular note of this requirement, and disclose assets or investments they have left behind in the home country. However, this requirement is waived for new immigrants for the year they first become resident in Canada.

Steps before immigrating to Canada

There are a number of tax planning steps that the prospective immigrant should consider before moving to Canada.

- Arrange to receive all payments for pre-immigration employment outside Canada before immigrating. If employment income is received after immigration, it should be taxable in Canada.
- For immigrants with substantial assets, consider setting up an "immigration trust". If structured properly, this should allow the

immigrant to keep funds offshore and not have to pay any Canadian tax on the income for five years.

- Note that capital property (*e.g.*, real estate) is generally deemed disposed of and reacquired at fair market value on immigration. This should boost the cost base of the property up to its current value, for purposes of future capital gain or loss calculations. The immigrant may want to obtain a formal valuation of such properties to document the value for future reference.

- Any Canadian professionals who are advising the immigrant (*e.g.*, lawyers or accountants) should render an account for time spent to date before the immigrant moves to Canada. The account should not bear GST or HST.

Tax issues after becoming resident

If you are a new immigrant, you should consider the following:

- As noted above, you should pay tax on your worldwide income from all sources. Make sure to identify and report these to the CRA, even if you have left the income offshore. Note that some forms of income (*e.g.*, pension income) may be given special relief by the tax treaty between Canada and your home country (if applicable).

- Obtain a Social Insurance Number upon arriving in Canada. This number will be used as your CRA account number.

- If you are carrying on business, consider whether you need to register for GST/HST, and to collect and remit GST or HST on your revenues.

- Have you become resident in Canada for tax purposes? Aside from the ordinary meaning of "resident", if Canada has a tax treaty with the home country, check how the "tie-breaker" rule applies if you might still be resident in both countries. For example, if you still have a home in both countries and travel back and forth, the answer may not be obvious.

- If you control a foreign corporation, you generally have to report its passive income as "foreign accrual property income" (FAPI), and pay Canadian tax on such income each year. The FAPI rules are very complex and you will need professional advice.

- If you receive income that is subject to foreign tax (*e.g.*, foreign withholding tax on interest or pension income), you can normally claim a "foreign tax credit" for this tax on your Canadian return, up to a limit of your Canadian tax on the same income. The rules can become complex, but in general you should end up paying the higher of the two countries' tax rates in total.

- If you are a US citizen, you must continue to file US tax returns even though you are no longer resident there. To reduce the impact of double taxation, you will want to claim the US "foreign earned income exclusion" against your employment or self-employment income in Canada, as well as US foreign tax credits and any relief provided by the Canada-US tax treaty. Professional advice from a specialist in both Canadian and US tax law is usually recommended. Note also that the US and Canadian tax systems differ in many ways, and your calculation of income for the two systems may be very different.

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- Consider setting up a TFSA (Tax-Free Savings Account) and contributing funds to it so that you can earn a certain amount of investment income tax-free. (If you are a US citizen, this is normally not advisable.)

- After your first year of earning employment or business income, set up a "registered retirement savings plan" (RRSP) and contribute the maximum possible to it (unless you are planning to emigrate from Canada within a few years, in which case there may be negative tax consequences).

- If you have children under age 6, apply to the CRA for the Universal Child Care Benefit. If you have children under age 18 and your family is relatively low-income, apply for the Canada Child Tax Benefit. If your family is low-income, apply for the GST/HST Credit. (See cra.gc.ca for more information.)

- Payments under pre-existing spousal support obligations may be deductible for Canadian tax purposes. If the payments qualify, keep good records and make the claim on your Canadian tax return.

- A person who dies while owning property in the US, or a US citizen who dies, is subject to US estate taxes. A credit to reduce or eliminate this tax is provided by the Canada-US tax treaty.

GIANT TECHNICAL BILL PASSED — HUNDREDS OF TAX CHANGES

On June 26, 2013, Parliament finally passed Bill C-48, a giant income tax "technical bill" that had been in the works for 11 years and subject to numerous revisions.

Some of the most important amendments in the bill that are now law include:

- Non-resident trusts: many such trusts are now deemed resident in Canada, and in certain cases, Canadian beneficiaries may be liable for the trust's Canadian tax.

- Foreign affiliates: very complex changes to the rules that tax passive income earned by foreign corporations owned by a Canadian resident.

- Charitable donations: if an "advantage" is provided by the charity in exchange for a donation, the donation is still valid but only the "eligible amount" qualifies for a tax credit.

- Non-competition payments are now almost always taxable.

- Contingent amounts are now usually disallowed as expenditures.

WHAT IF YOU DISAGREE WITH THE CRA?

What do you do if the CRA issues you an income tax or GST Notice of Assessment (or Reassessment), and you believe the CRA is wrong and that you should not be paying so much?

The CRA's role

As you may know, the CRA doesn't create the law. The rules for our income tax system are set out in the *Income Tax Act* (Canada), as amended by Parliament every year. Similarly, the GST rules are enacted in the *Excise Tax Act*. The Department of Finance

(www.fin.gc.ca) is responsible for designing and drafting changes to these Acts.

The CRA's job is to administer and enforce the system. As such, **the CRA is bound by the law**. However, sometimes the CRA's interpretation of the law is different from that of taxpayers, and can successfully be challenged. More commonly, the CRA assessor or auditor may simply not have understood the facts of your case.

Objection (appealing within the CRA)

The first step is to make sure that you **understand the rules** of the *Income Tax Act* (Canada) as they apply to your situation. Sometimes, even though the rules seem unfair, they are being correctly applied. If the rules are clear, then no matter how much you dislike paying the extra tax, you may have no choice.

Don't hesitate to get professional tax advice at this stage. An hour spent with an expert tax lawyer or accountant will be well worth it, if as a result you can know whether the assessment is simply a clear application of the law, or whether you have a realistic chance on objection or appeal.

The next step is to contact the CRA and request an adjustment. Sometimes a phone call or meeting with CRA officials can help iron out your problem and clarify the issues, though you may wish to put your request in writing. You can also request adjustments online using cra.gc.ca/myaccount.

You will have to file a **Notice of Objection** (see CRA Form T400A, for income tax objections) before the deadline for doing so expires. The deadline is **90 days** from the date of mailing of the notice of assessment or reassessment to which you are objecting (or, for personal tax returns, one year from the original April 30 or June 15 deadline for filing the return in question, if that is later). The date showing on the Notice of Assessment is normally presumed to be the date of mailing (*Income Tax Act* (Canada), subsection 244(14)).

Even if you are negotiating a solution and CRA officials have agreed orally or in writing to your position, **you *must* file the Notice of Objection if the deadline is approaching** and no reassessment has been issued to your liking. Otherwise you lose your legal right to appeal. The CRA's promise to correct an assessment will not be binding until the reassessment is actually issued.

Within about 12 months after you file the Notice of Objection, your case should be reviewed by an **Appeals Officer**. (The terminology is confusing here: you have filed an *objection*, not an *appeal*, but it is an "Appeals Officer" who considers your *objection*.) This officer is internal to the CRA but is independent of the Audit section which normally issues the reassessment. Thus, you are assured that your case is being given a "fresh look" by someone who has no preconceptions as to the result.

If you meet the Appeals Officer and they agree with you, the reassessment should be "vacated", or will be "varied" to reflect your position (and a new reassessment issued), and that should be the end of the matter. If not, the reassessment should be "confirmed". You will thus receive a Notice of Decision or Notice of Confirmation by registered mail. At this point you have exhausted your routes of appeal within the CRA, and must resort to the courts if you are still not satisfied.

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Appealing to the Tax Court

You have **90 days** from the day the Notice of Confirmation or Notice of Decision is mailed to you to appeal to the **Tax Court of Canada**. If you miss the deadline, an extension of up to one year may be available, but only if certain conditions are met. After the one-year extension, you are completely barred from appealing.

If the amount at stake involves less than $25,000 in total *federal* tax and penalties for any given taxation year, not counting interest, you may choose to use the Tax Court's **Informal Procedure**. (Including provincial tax and interest, this typically covers disputes of up to about $35,000-$40,000 per taxation year assessed.) Otherwise, unless you give up your right to appeal the excess, you are required to use the court's **General Procedure**. Note that for appeals filed before June 27, 2013, the above monetary limit is $12,000.

The Informal Procedure is informal in terms of paperwork, but there is still a formal hearing before a judge in a courtroom. You can simply write to the Tax Court to say that you are appealing, though using their standard Notice of Appeal form is advisable. You can file your appeal online at tcc-cci.gc.ca. There is no filing fee. You do not need to retain a lawyer, though you may if you wish. Many taxpayers want their accountant there to present their case.

In theory, you are supposed to receive a decision within 12 months of filing your appeal, but it often takes somewhat longer.

For the General Procedure, you should retain a lawyer. (Technically, you can act for yourself, but given the complex court rules and procedures involved it is not advisable.) A case under the General Procedure can easily take two years or more to get to trial, and even longer before the judge issues a decision.

Note that the appeal is *only* about whether the assessment is correct. If the CRA acted unreasonably towards you, that doesn't matter, and the Tax Court will take no notice of such evidence.

Do you pay the balance owing?

In general, while your case is under objection or appeal to the Tax Court, you cannot be forced to pay the balance owing (there are some exceptions to this rule). Interest will continue to accrue on the unpaid balance, however; the current rate is 5%, compounded daily (the rate is set every quarter). This interest is non-deductible.

The CRA has the right to withhold any refunds or rebates (income tax or GST) that you are entitled to, and apply them to the tax debt. Other than such "set-off", however, the CRA cannot take other collection action to enforce payment.

Should you pay anyway?

If you believe that your case is likely to lose, *or* if you have the funds available, it is usually a **good idea to pay the balance**. That will stop the non-deductible interest from accruing in the event you lose. And if you win, you will receive refund interest (currently at a rate of 3% compounded daily for taxpayers that are not corporations) when the overpaid balance is refunded to you.

Note that if you have a GST/HST assessment, or an assessment relating to source deductions (such as payroll) that

were withheld and not remitted, there are no restrictions on CRA collection action, and the CRA will normally take action to collect the balance even while the assessment is under objection or appeal. (It is possible to get Collections officers to use their discretion to hold off on collection action, if you appear to have a good case and it appears that you will still have assets after the case is resolved.)

Beyond the Tax Court

After the Tax Court of Canada has given its decision, either you or the CRA can appeal to the Federal Court of Appeal. Appeals can only be taken on matters of law; you cannot appeal the judge's findings of fact (such as whether any evidence you gave was credible), unless you can show that the judge made a "palpable and overriding error", which in practice is almost impossible to do.

Administrative Appeals —
The "Taxpayer Relief Package"

There is one set of rules that are within the CRA's discretion, and for which you cannot file a Notice of Objection or appeal to the Tax Court. These are part of the CRA's **"Taxpayer Relief package"** (formerly called "Fairness").

The "Taxpayer Relief package" has a number of components. One of them allows the CRA to **reopen your return and issue a reassessment to reduce your taxes for any past year**, going back up to 10 years from when you apply. If, for example, you discover that you neglected to claim a credit or deduction that you could have claimed several years ago, you can apply to the CRA to reassess your return for this purpose. Once 90 days have passed from the original assessment, and one year has passed from the original due date for the return, you cannot file a Notice of Objection and so you cannot force the CRA to do this. But in many cases the Agency will honour your request, particularly where the failure to make the claim was a result of an oversight on your part.

Another element of the "Taxpayer Relief package" allows the CRA to **waive interest and penalties**, again provided you apply within 10 years of the taxation year during which the interest accrued. The CRA may waive these if you can fit into the Agency's guidelines under its Information Circular (07-1) relating to waiver of interest and penalties. Grounds for waiver include:

- a serious illness or accident that prevented you from filing or making a payment on time;
- serious emotional or mental distress, such as caused by illness or death in the immediate family;
- disasters such as a flood or fire;
- civil disturbances or disruptions in services, such as a postal strike;
- processing delays that resulted in you not being informed, within a reasonable time, how much was owing;
- incorrect information that you received from the CRA;
- "financial hardship": your inability to pay the total owing due to the amount of accrued interest.

If you are unhappy with the CRA's decision on a "Taxpayer Relief" issue, you can ask for a "Second Level Review", which is undertaken by more senior officials within the CRA. If you are still unhappy with the decision, you can **apply to the Federal Court for "judicial review"** of that decision.

Conclusion

As you can see from the above, the remedies and approaches to take in dealing with the CRA will vary significantly depending on what relief you are seeking. If you take the wrong legal step (*e.g.*, you appeal to the Tax Court of Canada when what you are seeking is a waiver of interest, or you appeal an assessment without first filing a Notice of Objection), you should lose, as the deadline for taking the right legal step should have expired. The whole area of disputes with the CRA is a minefield, and obtaining expert professional advice is usually recommended.

AROUND THE COURTS

"Tax protestors" hit with costs awards by Tax Court

In our March 2013 letter, we reported on the *Meads v. Meads* decision, in which a judge of the Alberta Court of Queen's Bench wrote a detailed treatise to explain why the so-called "tax protestor" arguments are utter nonsense and will always be rejected by the Courts. The judge noted that, now that it is clear that these arguments are doomed, tax protestors should expect to be sanctioned by the Courts.

This process has now started. In two decisions issued by the Tax Court of Canada on July 30, 2013, *Dillon v. The Queen* and *Dalle Rive v. The Queen*, the Court dismissed such taxpayers' appeals. In each of these cases, the Tax Court judge awarded **costs of $1,000** against the taxpayer — essentially a fine for abusing the Court system. These were Informal Procedure appeals, in which normally the Tax Court cannot award costs against a taxpayer. However, such costs can be awarded against a taxpayer who has abused the Court's process.

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If you have any questions regarding the foregoing or other tax matters, please contact our tax group at (403) 262-2116.

Buchanan Barry LLP
Chartered Accountants
800, 840 – 6th Avenue SW
Calgary, Alberta T2P 3E5

Tel (403) 262-2116
Fax (403) 265-0845
www.buchananbarry.ca

This letter summarizes recent tax developments and tax planning opportunities; however, we recommend that you consult with an expert before embarking on any of the suggestions contained in this letter, which are appropriate to your own specific requirements.