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CRA Provides Relief from International Income Tax Issues Raised by COVID-19 Travel Restrictions

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The COVID-19 pandemic has resulted in the imposition of safety measures by governments around the world, including that in Canada, to protect the health of their citizens. Similarly, businesses have imposed safety measures to protect their employees. These measures include restrictions on travel (travel restrictions).

On May 19, 2020, the Canadian government issued Guidance on *International Income Tax Issues Raised by the COVID-19 Crisis* (Guidance), in which it outlines potential Canadian income tax issues resulting from pandemic-related travel restrictions and the Canada Revenue Agency's (CRA's) proposed response to address these issues. The administrative positions described below are applicable only for the period between March 16 and August 31, 2020, but may be extended if necessary.

A. Income Tax Residency

Individuals

If an individual remains in Canada due to COVID-19-related travel restrictions, the CRA has confirmed in the Guidance that this factor alone will not cause the individual to be resident in Canada under the common law test of residency. Similarly, in computing the 183-day threshold for deemed tax residency, the CRA will not factor in the days during which an individual is present in Canada and unable to return to the person's country of residence solely as a result of travel restrictions.

Corporations

Under general Canadian tax principles, corporate residence focuses on the locus of the corporation's central management and control (CMC). Specifically, where CMC of a corporation is exercised by the board of directors, the place where the directors of the corporation habitually hold their meetings (and make the major strategic and policy decisions for the corporation) will generally determine the tax residence of the corporation. However, due to current travel restrictions, board members present in Canada may be unable to attend meetings in a foreign jurisdiction. In these circumstances, a corporation may be considered a tax resident of both Canada and the foreign jurisdiction.

With respect to corporations *resident in a treaty country*, Canada's network of tax treaties typically resolves the issue of dual corporate residency in one of two ways: (i) by determining the corporation to be resident in the country under whose laws it was created; or (ii) by applying a residency "tie-breaker rule" that looks to, *inter alia*, the corporation's place of effective management. In the latter case, the CRA has stated in the Guidance that such corporations will not be considered resident in Canada solely because a director participated in a board meeting from Canada due to COVID-19 travel restrictions. However, corporate residency determinations involving potential dual residents of *non-treaty countries* will be determined on a case-by-case basis.

The CRA has also confirmed that this approach will be adopted in respect of other foreign entities that are considered corporations for Canadian tax purposes (e.g., limited liability companies). Moreover, the CRA is also considering adopting a similar approach in determining the residency of a commercial trust.

B. Carrying on Business and Permanent Establishments

A non-resident carrying on business in Canada that benefits from an income tax treaty is subject to tax in Canada on the income from that business only if, and to the extent that, its business activities are carried on through a permanent establishment (PE) in Canada. In this regard, in the Guidance the CRA has confirmed the following:

- A non-resident entity will not be considered to have a PE in Canada if its employees perform their employment duties in Canada solely as a result of the travel restrictions.
- A non-resident entity will not be considered to have an "agency" PE solely due to a dependent agent entering into contracts in Canada on behalf of the non-resident principal. However, the agent's activities must be limited to the period during which travel restrictions are in place.
- The CRA will exclude from the computation of the 183-day presence test under the "services" PE provision of Canada's tax treaties any days of physical presence in Canada resulting *solely* from travel restrictions (e.g. article V(9)(a) of the Canada-U.S. treaty).

If the non-resident entity's business is not being carried on through a PE in Canada, it is required to file a treaty-based income tax return for that year in order to claim the treaty exemption from Canadian income tax. The CRA has indicated that this filing obligation *will continue to apply* for any taxation year of a non-resident entity that overlaps with the period affected by travel restrictions.

In the case of residents of *non-treaty countries*, provided the non-resident can demonstrate that it satisfied the threshold of "carrying on business in Canada" *solely* due to the travel restrictions, the CRA will consider on a case-by-case basis whether administrative relief from the obligation to file a Canadian income tax return is appropriate.

C. Cross-Border Employment

Non-Resident Employees

Under the Canada-U.S. treaty, U.S. residents that regularly perform employment duties in Canada, but would normally not be present in Canada for more than 183 days, are generally not subject to Canadian tax on their employment income (e.g. article XV(2) of the Canada-U.S. treaty). However, current travel restrictions may cause such U.S. employees to be present in Canada beyond the 183-day limit. The CRA has confirmed in the Guidance that if such individuals are physically present in Canada and are performing their employment duties from Canada *solely* as a result of current travel restrictions, those days will not be counted toward the 183-day limit provided for in the Canada-U.S. treaty. A similar administrative approach will be applied in computing the *days of presence test* in respect of employees that are resident in other countries with which Canada has a tax treaty.

Canadian Resident Employees

Non-resident employers paying Canadian resident employees salary or wages are generally required to deduct withholdings at source, regardless of where the employment services are being rendered. Nevertheless, the applicable Canadian deductions at source may be reduced in order to account for any foreign tax credits available to the Canadian employee by obtaining a "letter of authority" from the CRA. In the event that a Canadian employee is required to perform employment duties in Canada as a result of travel restrictions, and such employee has already been issued a letter of authority for the current taxation year, the CRA has indicated that the Canadian withholding obligations of the non-resident employer will not change, and the letter of authority will continue to apply, provided that the withholding obligations of the non-resident employer in the other jurisdiction remain unchanged.

D. Waiver Requests

The CRA acknowledges in the Guidance that the current pandemic has caused a temporary interruption in processing Regulation 102 or 105 waiver requests. To address the backlog resulting from this interruption, the CRA is currently developing a process that will enable applicants, on a temporary basis, to submit urgent waiver requests electronically.

Moreover, where a Regulation 102 or 105 waiver request was submitted to the CRA but, as a result of the interruption of service, such waiver request was not processed within 30 days, the payor will not be assessed for failure to deduct, withhold or remit any amount as required by Regulation 102 or 105 in respect of amounts paid to a non-resident person covered by the particular waiver request. This relief is available only if the non-resident person can demonstrate that (i) the applicable waiver could not be obtained because of the interruption of services; and (ii) reasonable steps have been taken to ascertain that the non-resident person was entitled to a reduction or elimination of Canadian withholding tax by virtue of an income tax treaty with Canada. Other situations in which a waiver request could not be submitted due to the travel restrictions (or other consequences stemming from the current pandemic) will be examined by the CRA on a case-by-case basis.

E. Dispositions of Taxable Canadian Property

Where a non-resident vendor has submitted a request for a certificate of compliance (section 116 of the *Income Tax Act*), and the certificate had not been issued by the time a purchaser's remittance was due (namely, within 30 days of the end of the month in which the property was sold), the parties may request that the CRA issue a *comfort letter*. This letter advises the parties to a transaction to retain amounts withheld from the purchase price until the CRA completes its review of the file and instructs the purchaser to remit the withheld amounts (if any). So long as the amount of tax payable is remitted when requested, the CRA will not assess penalties or interest on the amount remitted.

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