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*Lawyers*

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## Canadian Tax Considerations for U.S. Residents Providing Services in Canada

By Greg Farano

Recently, a U.S. company based in Denver approached us for tax advice. For the past 6 months it had been sending two of its Denver-based employees (both U.S. citizens) every week (Monday to Friday) and one Denver-based employee (also a U.S. citizen) every other week (also Monday to Friday) to Canada to perform software development services for a Canadian client. It was expected that the services arrangement would be extended for another 6 months. The employees performed the services on behalf of the U.S. service provider entirely in the Canadian client's Canadian offices, and were paid by the U.S. service provider for their services in Canada. The services contract was concluded in the U.S. The U.S. service provider did not otherwise have an office, bank account, own property, or lease any space of its own in Canada.

The following article discusses the Canadian income tax, withholding tax and tax reporting issues which U.S. residents face when sending employees to Canada to work on short term assignments.

### United States Residents - Liability for Canadian Income Tax and Requirement to File Canadian Income Tax Return

Under paragraph 2(3)(b) and subparagraph 115(1)(a)(ii) of the *Income Tax Act* (Canada) ("ITA") a non-resident person is subject to tax in Canada on the income earned by it from "carrying on business" in Canada. However,

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these provisions of the ITA must be read subject to the Canada-United States Tax Convention (the "Canada-U.S. Convention"). The Canada-U.S. Convention has the force of law in Canada. The Canadian statute which brought the Convention into force provides that in the event of any inconsistency between the ITA and the Canada-U.S. Convention, the provisions of the Canada-U.S. Convention shall, to the extent of the inconsistency, prevail.

Article VII of the Canada-U.S. Convention provides that the business profits of a resident of a Contracting State (either of Canada or of the U.S.) shall be taxable in the other Contracting State to the extent that the business profits arose from the resident's carrying on business in the other State through a permanent establishment ("PE") in that other State. Accordingly, a U.S. resident is required to pay income tax in Canada from business profits derived from its carrying on business in Canada only where the business is carried on through a PE in Canada. Put another way, a U.S. resident which does not otherwise have a PE in Canada will not be subject to income tax in Canada on profits derived from its carrying on business in Canada.

Accordingly, in order to determine whether business profits earned by a U.S. resident are subject to income tax in Canada it is necessary to determine, first, whether the U.S. resident is carrying on business in Canada and, second, whether the business is carried on through a PE in Canada.

Clause 150(1)(a)(i)(B) of the ITA requires a corporation to file a tax return within 6 months after its fiscal year end if it carries on business in Canada. U.S. residents carrying on business in Canada through a PE must file a T2 return within this 6-month post year end time limit and report the income earned from such activity. And although the Canada-U.S. Convention exempts from Canadian tax income earned by a U.S. resident carrying on business in Canada other than through a Canadian PE, a U.S. resident with no PE in Canada is still required to file a T2 Schedule 91 where it is otherwise carrying on business in Canada. U.S. residents are subject to a penalty (up to \$2,500) under subsection 162(2.1) or (7) of the ITA for failing to file a T2 return (carrying on business through a Canadian PE) or T2 Schedule 91 (carrying on business other than through a Canadian PE), regardless of whether tax is owing.

### ***Background to Canada-U.S. Tax Convention - OECD Model Convention and Commentaries***

As a matter of background, the Canada-U.S. Convention is based upon the *Model Tax Convention on Income and on Capital* (the "OECD Model Convention") published by the Organization for Economic Co-Operation and Development ("OECD"). The main purpose of the OECD Model Convention is to provide its members (which include Canada and the U.S.) with a model set of rules for settling on a uniform basis the most common problems that arise in the field of international judicial double taxation. The OECD first published a draft model tax convention in 1963. This draft model tax convention was revised and replaced by the 1977 OECD Model Double Taxation Convention on Income and Capital (with Commentaries). Subsequently, the OECD published a revised and updated version of the Model (and Commentaries) in 1992 in a loose-leaf format in order to allow for updating on a regular basis.

The OECD Model Convention is accompanied by Commentaries issued by the OECD's Committee on Fiscal Affairs. Although not actually annexed to any particular tax Convention, and although not legally binding, the Commentaries are useful in the interpretation of tax treaties based on the OECD Model Convention and, in particular, in resolving disputes. A Commentary is given regarding the purpose and scope of each Article of the OECD Model Convention. Any reservations which a member country has entered with regard to a given Article of the Model are noted in the Commentary on the Article concerned.

The Canada Revenue Agency ("CRA") generally follows the Commentaries which accompany the OECD Model Convention for the purpose of interpreting the Canada-U.S. Convention, except where Canada has specifically entered a reservation. For example, in its Income Tax Technical News No. 33 released on September 16, 2005, the CRA states that the factors to be considered in determining whether or not a PE exists in Canada are outlined in the Commentary to the OECD Model Convention and derived from jurisprudence.

Canadian courts have generally accepted CRA's approach of following the Commentaries on the OECD Model Convention. See for example *The Queen v. Crown Forest Industries*, 95 DTC 5389 (SCC), and *Salt v. The Queen*, 2007 DTC 520 (TCC).

### **Meaning of “Carrying on Business” – Common Law Definition**

The terms “business” and “carrying on business” are not defined in the Canada-U.S. Convention. Article III:2 of the Canada-U.S. Convention states that any term not defined in the Convention shall, unless the context otherwise requires and subject to the provisions of Article XXVI (Mutual Agreement Procedure), have the meaning which the term otherwise has under the laws of that State concerning the taxes to which the Convention applies. Accordingly, in order to determine whether certain activities amount to “carrying on business” in Canada or the U.S., it is necessary to rely on the meaning of the term under the domestic laws of Canada or the U.S. where the activities take place.

“Business” is broadly defined in subsection 248(1) of the ITA as including a profession, calling, trade, manufacture or undertaking of any kind whatever, and for most purposes an adventure in the nature of trade, but as excluding an office or employment. In general, the purchase of a single property with the explicit intention of reselling the property may constitute an adventure in the nature of trade, and may therefore result in the carrying on of business for Canadian income tax purposes.

The term “carrying on business” is not exclusively defined in the ITA, and accordingly derives its meaning from the common law, subject to the extended definition of carrying on business in section 253 of the ITA, discussed below. Under the common law, a number of different tests have been used to determine whether or not a business is being carried on in Canada. These include the “facts-and-circumstances” test, the “general parameters” test, the “indirectly carrying on business” test, and the “place of contract” and “place where profits are earned” tests.

The facts and circumstances test focuses on the territorial situs of the business. The general parameters test takes into account whether there is a sufficient nexus with Canada to be carrying on business “in” Canada rather than “with” persons in Canada. The indirectly carrying on business test extends the meaning of carrying on business to include business activities carried on by an agent with authority to bind its principal.

The test most commonly used by Canadian courts in determining whether a business is carried on in

Canada has two key components: the place where the contract is made and the location of the operations from which the profits arise. In determining the place where the contract is made – the first component of the test – the courts generally consider only the place where the company’s profit-producing contracts are habitually entered into. Having said this, and although historically the place where the contract is made has had substantial importance in determining where a business is carried on, in *The Queen v. Gurd’s Products Company Limited*, 85 DTC 5314 (FCA), it was held that the taxpayer was carrying on business in Canada even though the contract was concluded outside of Canada. Further, paragraph 253(b) of the ITA discussed below has expressly modified this first component of the test.

In addressing the second component of the test – the location of the operations from which profits arise – the courts and the CRA<sup>1</sup> have considered the following factors relevant in determining whether a person is carrying on business: (i) the place where the goods are delivered or payments are made, (ii) the place where the business assets are located, (iii) the nature of the activities/transactions, (iv) the establishment of a bank account, listed telephone number or address, (v) whether the reason for compliance with a jurisdiction’s rules and relations is business - or legally – motivated, (vi) whether the taxpayer intended to do business in Canada, (vii) the place where the assets used in the business are purchased, (viii) the degree of supervisory or other activity in Canada, (ix) the substance or object of the transaction, (x) the presence of a representative or resident expert, (xi) whether activities in Canada are merely ancillary to the main business (e.g., the business of buying, storing, selling or manufacturing the product), (xii) whether individuals in Canada assist (or are available to assist) the taxpayer in his endeavour, (xiii) the reason for the taxpayer’s existence, and (xiv) how “the reasonable man” would answer this question. In addition, the CRA takes the position that the rendering of services to a resident Canadian or person otherwise carrying on business in Canada amounts to carrying on business in Canada.<sup>2</sup>

It is interesting to note the CRA’s policy on what

<sup>1</sup> The CRA has outlined its commonly used criteria in CRA document no. 9312986 dated May 31, 1993.

<sup>2</sup> See paragraph 1040 of the Canadian Master Tax Guide.

constitutes carrying on business for GST purposes. In example 18 in the CRA's GST/HST Policy Statement P-051R2 - Carrying on Business in Canada, dated April 29, 2005, the CRA concludes that the following facts involving a theoretical non-resident corporation would not amount to its carrying on business in Canada for GST/HST purposes. A large international non-resident corporation specializing in the provision of offshore services has contracted with a Canadian registrant to perform services on an oil rig stationed at a Canadian port. The contract is the non-resident corporation's only contract in Canada. The contract calls for an employee of the non-resident corporation to enter Canada and to perform services for a period of one week on board the rig. The non-resident corporation does not solicit business in Canada. The contract is concluded outside of Canada and payment for the supply is made outside of Canada. The non-resident corporation is not listed in any directories nor does it have any bank accounts or offices in Canada. And with the exception of the employee who temporarily enters Canada to perform the services, the non-resident corporation has no agents or employees in Canada. This administrative position appears to contradict the CRA's administrative position in its Canadian Master Tax Guide (footnote 2, above), which maintains that the provisions of any service, no matter how brief, amounts to carrying on business.

### ***Section 253 Extended Meaning of "Carrying on Business" – Solicitation***

In addition, section 253 of the ITA provides that if a non-resident person performs certain activities listed in that section, the person will be deemed to be carrying on business in Canada. Section 253 modifies the common law test of the place where the contract is made. Under paragraph 253(b), a non-resident person is deemed to be carrying on business in Canada if the person "solicits orders or offers anything for sale in Canada through an agent or servant, whether the contract or transaction is to be completed inside or outside Canada or partly in and partly outside Canada". Accordingly, the mere solicitation of business in Canada may amount to carrying on business in Canada even where the contract is otherwise concluded and performed outside of Canada. This is illustrated in *Maya Forestales S.A. v. The Queen*, 2005 DTC 51 (FCA). The court in that case determined that the non-resident's activity amounted to carrying on

business in Canada under paragraph 253(b) where the non-resident merely offered Costa Rican plantations for sale in Canada and otherwise concluded the sale contracts in Costa Rica. In that case, the "anything" offered for sale in Canada was Costa Rican real estate.

### ***Meaning of "Permanent Establishment"***

As stated above and under Article VII of the Canada-U.S. Convention, in order for a non-resident's business profits to be subject to tax in Canada they must be attributable to a business carried on through a PE in Canada. The rules for attributing profits to a particular PE in Canada are beyond the scope of this article.

There is an extended definition of permanent establishment in Article V of the Canada-U.S. Convention.

A PE is generally defined as a "fixed place of business" through which the business is wholly or partly carried on (Article V:1), including, (i) a place of management, (ii) a branch, (iii) an office, (iv) a factory, (v) a workshop, and (vi) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources (Article V:2). However, a PE is deemed not to include, (i) a building site or construction or installation project which lasts less than 12 months (Article V:3), nor (ii) the use of an installation or drilling rig or ship in a Contracting State to explore for or exploit natural resources where such use is for 3 months or less during any 12 month period (Article V:4). The Commentary to the OECD Model Convention provides detailed discussions of the 12-month rule.

However, and regardless whether a non-resident person of a Contracting State has a "fixed place of business" in the other Contracting State, the non-resident person will be deemed to have a PE in the other Contracting State where a third person (other than an independent agent) acting in the other Contracting State on behalf of the non-resident person has, and habitually exercises in the State, an authority to conclude contracts in the name of the non-resident (Article V:5) unless those activities are limited to certain preparatory or auxiliary activities listed in Article V:6.

Article V:6 contains certain exceptions to the fixed place of business and authority to conclude contract rules in Articles V:1, 2 and 5. Article V:6 provides that the term "permanent establishment" shall be deemed

not to include a “fixed place of business” used solely for, or a person referred to in Article V:5 engaged solely in, one or more of the following preparatory or auxiliary activities:

- (a) the use of facilities for the purpose of storage, display or delivery of goods or merchandise belonging to the resident;
- (b) the maintenance of a stock of goods or merchandise belonging to the resident for the purpose of storage, display or delivery;
- (c) the maintenance of a stock of goods or merchandise belonging to the resident for the purpose of processing by another person;
- (d) the purchase of goods or merchandise, or the collection of information, for the resident; and
- (e) advertising, the supply of information, scientific research or similar activities which have a preparatory or auxiliary character, for the resident.

Article V:7 contains an exception for independent agents. It provides that a resident of one Contracting State is deemed not to have a PE in the other Contracting State merely because such resident carries on business in that other State through a broker, general commission agent or any other agent of independent status, provided that such persons are acting in the ordinary course of their business.

Finally, Article V:8 provides that the fact that a company that is a resident of one Contracting State controls or is controlled by a company which is either a resident of the other Contracting State or which is carrying on business in the other Contracting State, does not automatically render either company a PE of the other.

Updates issued in 2003 and 2005 to the Commentary to Article 5 of the OECD Model Convention expanded the ambit of certain of the criteria for having a PE. Specifically, the Commentary on what constitutes a fixed place of business and whether an agency relationship creates a PE were revised and new guidelines were added for electronic commerce. The threshold for having a PE was lowered, resulting in certain taxpayers, who may have previously claimed Convention protection for business profits, now having

a PE and no longer qualifying for such protection.

The following are some of the changes brought about by the updates:

1. *No formal legal right required to use a premises in order to have a PE* – Paragraph 4.1 of the Commentary to Article 5 of the OECD Model Convention provides that no formal legal right is required to use a premises in order for the premises to constitute a place of business. The Commentary analyzes a number of examples, including that of a painter who, for two years, spends three days a week in a large office building of his main client. The presence of the painter in the building where he is performing the most important functions of his business (painting) constitutes a PE of the painter.
2. *Degree of permanency required for a PE* – Paragraph 6 of the Commentary to Article 5 notes that PEs have normally not been considered to exist in situations where a business has been carried on for less than 6 months. However, a place of business may be a PE although it exists only for a short period of time (less than 6 months) if the nature of the business is that it will be only carried on for a short period of time (paragraph 6.2). And once a PE exists, a temporary interruption in activities does not cause the PE to cease to exist.
3. *Multiple locations may constitute a single fixed place of business* – Paragraph 5.4 of the Commentary to Article 5 states that if a consultant provides services to several offices of the same company pursuant to a single consulting contract, each location should be considered separately in determining whether there is the necessary geographic coherence for a single place of business. Related locations may be considered a fixed place of business.
4. *Criteria for determining whether an agent is dependent or independent* – By virtue of Article V:5 and V5:7 of the Canada-U.S. Convention, a dependent agent in one Contracting State who regularly concludes contracts for a company in the other Contracting State may constitute a PE of the company in the dependent agent’s Contracting State. This will not result where the agent is independent and acting in the

ordinary course of its business. It is important therefore to determine whether an agent with authority to conclude contracts is dependent or independent of its principal. Dependence is based on whether an agent is subject to detailed instructions or comprehensive control, and whether such person has entrepreneurial risk (paragraph 28 of the Commentary to Article 5). Such persons may be individuals or companies and need not be residents of, nor have a place of business in, the Contracting State in which they act for the principal (paragraph 32 of the Commentary to Article 5). This provision is extended to agents who conclude contracts which are binding on the principal even if the contracts are actually in the name of the principal. Paragraphs 38.2 to 38.7 of the Commentary to Article 5 set out factors indicating that an agent is independent of its principal. And the authority to conclude contracts must be “habitually” exercised. The extent and frequency of activity necessary to conclude that an agent is “habitually exercising” contracting authority will depend on the nature of the contacts and business of the principal (paragraph 33.1 of the Commentary to Article 5).

### ***U.S. Service Provider Carrying on Business Through a Permanent Establishment in Canada***

In our view the U.S. service provider is carrying on business in Canada, even though the services contract was concluded in the U.S. and the U.S. service provider did not have an office or other physical presence in Canada.

Aside from the CRA’s view that the rendering of any services amounts to carrying on business (see footnote 2 above), this conclusion results from the application of the common-law “facts and circumstances” test and the “place where profits are earned” test. The nature of the U.S. service provider’s “business” from which it earned “profits” in this case was the provision of services, which services were performed solely in Canada. And the 6-month term of the services (with the likelihood that this work would be extended for another 6 months) were of a sufficient duration for a PE to exist (at the Canadian client’s offices).

The initial 6-month period of the work does not fall

within the less than 6-month experience threshold mentioned in paragraph 6 of the Commentary to Article V of the OECD Model Convention. And the work, in this case the provision of contract services, by its nature could have had a duration of less than 6 months, fitting within the inclusion language of paragraph 6.2. And the conclusion that the activity constitutes carrying on business results despite the fact that none of the three employees had the right to (nor did they in fact) habitually conclude contracts in Canada on behalf of their U.S. employer.

Accordingly, the U.S. service provider is liable to pay Canadian income tax (and file a Canadian income tax return) on its income (profit) earned from its three employees performing services in Canada.

### ***Avoiding Carrying on Business Through a PE and Resultant Canadian Income Tax Liability – Secondment Arrangement***

The U.S. Corporation could avoid the above results – that is a PE in Canada and the resultant liability for Canadian income tax in respect of income earned from the performance of services by its three employees in Canada - by entering into a qualifying secondment arrangement with the Canadian client.

The U.S. service provider could “loan” the three employees to the Canadian client for the duration of their presence in Canada performing services for the Canadian client. Under this lending arrangement, the employees would remain common-law employees of the U.S. service provider, who could continue to pay all of their remuneration and make all required employee withholdings in the U.S., although the Canadian client could assume this responsibility. Where the U.S. service provider continues to pay its employees’ remuneration, the Canadian client would reimburse the U.S. service provider for the portion of wages and benefits of the three employees attributable to the performance by them of the services in Canada. The U.S. service provider would not earn a profit on the services arrangement, as the Canadian client would pay the U.S. service provider nothing more than the three employees’ wages and benefits. In this way, the Canadian client would take full responsibility for the three employees in respect of their services performed in Canada and thus bear the risks and rewards associated with their assignment.

The criteria for secondment arrangements that satisfy the Regulation 105 exception requirements discussed below should be met.

Such a secondment arrangement would arguably result in the U.S. service provider not being regarded as carrying on business in Canada through a PE as a result of the activities carried out by its three employees. However, the U.S. service provider could not earn a profit from the services, which may make the arrangement undesirable. In such a case the U.S. service provider may decide to take the profit and report and pay tax on it in Canada. For this reason, secondment arrangements may be more appropriate where the U.S. employer has a Canadian subsidiary or affiliate to which it could loan its employees and keep the profit from their services (taxable in Canada) within the corporate group.

### **Requirement to Withhold and Remit Amounts on Account of Tax in Respect of Fees, Commissions or Other Amounts Paid to Non-Resident Contractors**

Notwithstanding that the Canada-U.S. Convention provides relief from Canadian income tax where a U.S. resident carrying on business in Canada does not do so through a PE in Canada, paragraph 153(1)(g) of the Act and section 105 of the *Income Tax Regulations* ("Regulation 105") requires that 15% of all fees, commissions or other amounts (but not reimbursed expenses) paid to a non-resident in respect of services rendered in Canada must be withheld and remitted to the CRA, regardless whether the non-resident has a PE in Canada or not. The Canadian payor must file a T4A-NR Information Return annually in respect of each non-resident payee, and issue a duplicate to the non-resident. The withheld amount must be paid by the 15th day of the month following the month of the payment. Where a non-resident is not otherwise liable to pay income tax in Canada (because it has no PE in Canada) and in the absence of a waiver (discussed below), the non-resident will have to file a Canadian tax return within the time required therefore under the Act on the basis that no business profits are attributable to a PE in Canada with the result that

the Canadian tax, previously withheld, should be refunded.

A bundled contract may include payments to non-residents of Canada for both services rendered in Canada and the use of property in Canada. The purchase of equipment or software may include installation or training. For example, royalties for use of computer software paid to a U.S. resident are exempt from Canadian withholding tax but could be subject to a Regulation 105 withholding requirement if a Canadian service component is included.<sup>3</sup> If the agreement with the non-resident does not have an allocation between services and property provided under the agreement, Regulation 105 requires a withholding on all payments. It is therefore important to separate the sale of goods or a license payment or a fee for services to be rendered outside of Canada from any fees for services to be provided in Canada. There can be a reasonable allocation in the agreement or preferably a separate agreement in respect of the Canadian services.

There may be an obligation to withhold on payments made to a non-resident where the non-resident does not itself perform services in Canada but subcontracts the services to be performed in Canada to a non-resident independent contractor. In *Ogden Palladium Services (Canada) Inc. et al. v. The Queen*, 2001 DTC 345 (TCC), aff'd 2007 DTC 7378 (FCA), a U.S. promoter/producer of the Elvis Stojko figure skating show was held to have provided "services", and the Canadian taxpayer owners of the stadiums in Canada where the shows were performed were subject to penalties for not withholding tax under Regulation 105 in respect of net ticket revenues from the Canadian performances paid to the U.S. promoter (payments "in respect of services" rendered in Canada). It was irrelevant that the U.S. promoter did not have a PE in Canada, and did not itself provide any services in Canada.

The CRA has in Information Circular IC 75-6R2 – *Required Withholding from Amounts Paid to Non-Resident Persons Performing Services in Canada*, dated February 28, 2005, ("IC 75-6R2") set out certain criteria for employee secondment arrangements which, if met, would result in the avoidance of a Regulation

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<sup>3</sup> See, however, *Weyerhaeuser Co. v. The Queen*, 2007 DTC 392 (TCC), where it was held that reimbursements of expenses by a Canadian client to a U.S. service provider were not subject to withholding tax.

105 withholding requirement. A copy of IC 75-6R2 can be obtained at the CRA's website at [www.cra.gc.ca](http://www.cra.gc.ca). Where the seconded non-resident employee continues on the payroll on the lending employer, a qualifying secondment arrangement exists if the non-resident employee can be considered to be "factually" an employee of the receiving employer and where the lending employer cannot be considered to be carrying on business in its own right. This occurs where the receiving employee's reimbursement of the lending employer is reasonable, that is where the reimbursement is limited to the cost of the loaned employee's remuneration, travel accommodation and per diem costs incurred in respect of the employment services that the employee provides in Canada. Any payment of a markup or unreasonable charges for overhead may result in the lending entity being subject to Regulation 105 withholding. The CRA indicates that it will consider an administrative charge of \$250 per month per employee to be a reasonable.

Factors that the CRA considers indicative of a qualifying secondment arrangement include the following (paragraph 37 of IC 75-6R2):

- the secondment and employment agreements are in writing, and are signed by the lending and receiving employers and the seconded employee(s);
- the legal terms of the secondment, such as the duration or project to be completed, the employee's and employer's responsibilities, the job description, the rate of pay, and any other benefits or payments are specified;
- the receiving employer is responsible for the employee's salary and benefits such as medical, pension, and possible tax payments, and, normally, any costs of the transfer including travel and relocation; and
- there is no element of profit included in the charge-back to the receiving employer by the lending employer.

Absent a waiver (discussed below), a non-resident may obtain a refund of the withholding tax only if it is otherwise not liable to pay income tax in Canada in respect of the services provided in Canada, that is if the profits arising from the services provided by the non-resident are not attributable to a PE in Canada. In order to obtain the refund, the non-resident must file

a Canadian tax return within the 6 month post-year end period required under the ITA on the basis that the Canadian service profits are not attributable to a Canadian PE.

In our example, and absent a qualifying secondment arrangement, the Canadian client would be required to withhold and remit 15% of all services fees paid to the U.S. service provider in respect of the three employees providing services in Canada. And since the U.S. service provider has a PE in Canada, it is not be entitled to a waiver (discussed below) or a refund of this withholding tax, but could claim the withholding tax as a credit against its Canadian income tax liability on its Canadian service profits.

### ***Application for Waiver of Withholding Tax Requirement***

Where a non-resident can demonstrate, based on Convention protection (such as a Convention provision exempting taxation of a non-resident who does not have a PE in Canada) or estimated income and expenses, that the normally required Regulation 105 withholding is in excess of the ultimate tax liability, the CRA may waive or reduce the withholding accordingly pursuant to the *Undue Hardship* provisions of subsection 153(1.1) of the Act. Again, the U.S. service provider in our example would not be entitled to a waiver because it has a PE in Canada.

The CRA has established two types of waiver procedures, which provide for the waiving or reduction of the Regulation 105 withholding which would otherwise be required. These procedures are found in two appendices to IC 75-6R2, namely Appendix A "*Guidelines for Treaty-Based Waivers Involving Regulation 105 Withholding*", and Appendix B "*Guidelines for Income and Expense Waivers Involving Regulation 105 Withholding*" (collectively, the "Guidelines").

If the non-resident service provider does not obtain a waiver, the Canadian payor must withhold in accordance with Regulation 105, regardless of whether the non-resident is entitled to an exemption from Canadian tax because it has no PE in Canada. The granting of a waiver does not affect the requirement that a non-resident providing services (that is carrying on business) in Canada file a Canadian tax return.

The Guidelines provide that Convention based waivers

will be granted in any of the following circumstances:

- (a) the applicant is a non-resident independent individual with income of less than \$5,000 for the current calendar year (including expenses reimbursed or paid on the applicant's behalf);
- (b) the applicant is a non-resident person whose presence in Canada is not "recurring" and who performs services in Canada for less than 180 days under the current contract or engagement; or
- (c) the applicant is a non-resident person whose presence in Canada is "recurring", but whose cumulative presence is less than 240 days during the period and less than 180 days under the current contract or engagement.

An applicant who otherwise satisfies the above criteria will be denied a waiver if their situation falls under one of the exceptions specified in the Guidelines.

A waiver application must be submitted at least 30 days before either services begin in Canada or the initial payment. A waiver application will be accepted after the start of payments, however, should a waiver be granted, it will only apply to payments made after the waiver is issued. A Regulation 105 waiver may be granted on annual contracts provided all information is provided and the conditions for a waiver are met. It is also possible to apply for an extension of a waiver.

The Guidelines set out the information required to be included in a Regulation 105 waiver application.

### **Requirement to Withhold and Remit Amounts on Account of Tax in Respect of Remuneration Paid to Non-Resident Employees – Waiver Application**

Paragraph 153(1)(a) of the Act and section 102 of the *Income Tax Regulations* ("Regulation 102") subject remuneration paid by both resident and non-resident employers to non-resident employees, who provide services in Canada, to the same withholding, remitting and reporting requirements as otherwise apply to Canadian resident employees. This could include income tax, Canada Pension Plan and Employment Insurance premiums. The non-resident employer requires a CRA business number account and must file a T4 Information Return in respect of each employee.

A non-resident individual engaged in employment in Canada should have a Canadian social insurance number and a valid work visa. The individual will have to file a Canadian tax return by April 30th of the following year.

A non-resident employee or an employer may apply for a waiver of the Regulation 102 withholding on salary 30 days before the earlier of the date employment services in Canada begin or the initial payment. A Convention-based waiver may be available to a U.S. employee who qualifies under Article XV of the Canada-U.S. Convention. The employee must earn \$10,000 or less in the calendar year or be present in Canada less than 183 days. In addition, the remuneration must not be deducted by an employer resident in Canada or by a Canadian branch of a non-resident employer.

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