OUTLOOK SERIES 2021
Tax Planning

Tax Perspectives

Review of 2020 & 2021 Outlook

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Tax Perspectives: Review of 2020 & 2021 Outlook

The year 2020 was an eventful year for developments in Canadian income tax and sales tax. This article provides an overview of the important legislative and judicial tax developments of 2020, and looks ahead to potential significant Canadian tax changes in 2021.

Income Tax Act

LEGISLATION

Because of the COVID-19 global pandemic, the Government of Canada ("**Government**") did not provide its usual federal budget in March 2020. Instead, the Government provided a myriad of federal relief measures aimed at alleviating financial hardship due to the COVID-19 pandemic, which resulted in certain legislative amendments to the *Income Tax Act* (Canada) ("**Tax Act**"). In addition, the Government provided the Fall Economic Statement 2020 on November 30, 2020, where it announced certain additional measures and that there will be a $382 billion deficit in 2020-2021. Québec also implemented new disclosure obligations for nominee agreements.

The Canada Emergency Wage Subsidy

On April 11, 2020, the Government passed Bill C-14, the *COVID-19 Emergency Response Act, No. 2*, to amend the Tax Act and thereby establish the statutory foundation for the Canada Emergency Wage Subsidy ("**CEWS**"). The Government passed further legislation throughout the course of the year, which redesigned and updated the CEWS program. The CEWS program forms part of the Government's economic response plan to support the Canadian economy during the COVID-19 global pandemic ("**Response Plan**").

The CEWS is intended to allow eligible employers who suffer significant declines in revenue to keep Canadian employees on the payroll, and to bring Canadian employees who are already on layoff back onto the payroll.

The CEWS is intended to allow eligible employers who suffer significant declines in revenue to keep Canadian employees on the payroll, and to bring Canadian employees who are already on layoff back onto the payroll. CEWS amounts are based on the employer's decline in revenue for the particular period. The CEWS is currently scheduled to end in June 2021, with details for periods following March 13, 2021, to be proposed at a later date. Commentary from our Firm on the CEWS can be found in publications on April 15, May 16, August 3, October 2, and November 20, 2020.

Other Relief Measures Under the Response Plan: CRB, CERB, CERS & T2200

On March 25, 2020, the Government passed Bill C-13, *An Act respecting certain measures in response to COVID-19*, to implement the first stage of the Response Plan.

One measure from the Response Plan that was enacted was the Canada Recovery Benefit ("**CRB**"), which was available from September 27, 2020, to September 25, 2021, to provide $500 per week to individuals for up to 26 weeks. The benefit is for workers who are not eligible for Employment Insurance ("**EI**"), so mainly the self-employed and those working in the "gig" economy.

The Response Plan also contains a Canada Emergency Response Benefit ("**CERB**") to support eligible workers, including seasonal workers and those who have exhausted their EI benefits and were unable to find employment or return to work due to the pandemic. The CERB provided $2,000 per four-week period for up to 28 weeks, from March 15, 2020, until September 26, 2020. The last date to apply was December 2, 2020. Payments under the CERB are a taxable benefit and must be reported in the individual's 2020 income tax return. Workers could not receive both EI and the CERB for the same period, and employees were not eligible for both the CEWS and CERB for the same period.

Employees who worked from home more than 50% of the time over a period of at least four consecutive weeks (a shorter qualifying period than the ordinary practice) in 2020 due to COVID-19 may be eligible to claim the home office expenses deduction for 2020. Employees may claim the deduction using either a new simplified flat rate for claims up to $400, or a detailed method for larger claims. Under the simplified flat rate, eligible employees may claim a deduction of $2 for each day they worked at home in the qualifying period, plus any other days they worked from home in 2020 due to COVID-19, up to a maximum of $400. The Canada Revenue Agency ("**CRA**") will not require a Form T2200 or Form T2200S completed and signed by their employer. Employees with larger claims may choose the existing method, using the new simplified forms (Form T2200S and Form T777S) or the regular Form T2200. To date, neither Revenu Québec nor the Québec Ministry of Finance has announced plans to ease the requirement for an employee to obtain form TP-64.3-V, "General Employment Conditions", which is the analogous form to Form T2200 for purposes of the Taxation Act (Québec). Further commentary from our Firm on the deduction can be found here.

The Canada Emergency Rent Subsidy ("CERS") program, enacted on November 19, 2020, under Bill C-9, *An Act to Amend the Income Tax Act (Canada Emergency Rent Subsidy and Canada Emergency Wage Subsidy)*, is intended to provide support to qualifying renters and property owners, retroactive to September 27, 2020. It is administered by the CRA, and provides direct rent and mortgage support on a sliding scale, covering up to a maximum of 65% of eligible expenses, with an additional 25% "lockdown support" top-up potentially available where public health restrictions apply. The Government's Fall Economic Statement 2020 proposed to extend this measure to March 13, 2021. Further commentary from our Firm on the CERS can be found in publications on November 20 and December 3, 2020.

Limits on Employee Stock Options

When a Canadian resident employee's stock option is cashed out or exercised, the employee has an employment benefit equal to the cash-out amount or, in the case where the option is exercised, the amount by which the fair market value of the share acquired on the exercise exceeds the exercise price paid by the employee. Where the options are issued by a corporation or a mutual fund trust and certain conditions are met, the employee is entitled to a deduction equal to 50% of such employment benefit ("**50% Deduction**") such that the employee is taxed at a rate equivalent to the Canadian capital gains rate.

The Fall Economic Statement 2020 indicated that the Government intends to move forward with previously announced rules to limit the amount of employee stock options that may be eligible for the 50% Deduction. The new rules will:

- Impose a $200,000 annual vesting limit (based on the value of an option's underlying shares at the date of grant) on options that can qualify for the 50% Deduction; and

- Provide the employer with a deduction for the amount of the stock option benefits that exceed the new annual vesting limit, subject to certain conditions.

Additionally, employers can elect to have this tax treatment apply for stock options, which are below the $200,000 threshold.

These rules will apply to options issued by an employer that:

- is a mutual fund trust or a corporation, other than a Canadian-controlled private corporation, and
- has consolidated group gross revenues greater than $500 million.

Employers that are not described above cannot elect into the new tax treatment.

Options granted before July 1, 2021 will remain subject to the existing rules, and only options granted after June 2021 will be subject to the new rules.

New Disclosure Requirements for Nominee Agreements in Québec

In Bulletin 2019-5, published on May 17, 2019, Revenu Québec announced proposed amendments that impose an obligation on parties to a nominee agreement made as part of a transaction, or a series of transactions, to disclose the nominee arrangement to Revenu Québec by filing a TP-1079.PN information return. The amendments were enacted in Bill-42, *An Act to give effect to fiscal measures announced in the Budget Speech delivered on 21 March 2019 and to various other measures*, which received assent on September 24, 2020.

Disclosure is mandatory for nominee agreements entered into after May 16, 2019, or agreements entered into prior to May 17, 2019, but in respect of which the tax consequences continue after May 16, 2019.

Under a nominee agreement, the nominee enters into an agreement to act as agent for a principal – for example, a nominee arrangement is often used in circumstances where the nominee holds legal title to a property for the owner of the property, and the owner retains beneficial ownership of the property.

Disclosure is mandatory for nominee agreements entered into after May 16, 2019, or agreements entered into prior to May 17, 2019, but in respect of which the tax consequences continue after May 16, 2019. Disclosure made by one of the parties to the nominee agreement would be deemed to have been made by the other party as well. However, if a partnership is party to the agreement, the partners must make the disclosure, except in the case of a limited partnership wherein only the general partner is required to make the disclosure.

The TP-1079.PN return must be filed on the later of: (i) 90 days after the date on which the nominee agreement was concluded; and (ii) December 23, 2020. Failure to file may attract penalties of up to $5,000, for which the parties are jointly liable and the suspension of the normal reassessment period in respect of the transaction or series of transactions. The nominee agreement must be attached to the form.

INCOME TAX CASES

To go along with the plethora of legislative changes, 2020 brought us a number of important decisions, including from the Supreme Court of Canada ("**SCC**") and the Federal Court of Appeal ("**FCA**"). The following is a summary of some of the notable cases from 2020.

Is a Forward Contract a Hedge (MacDonald, SCC)?

On March 13, 2020, the SCC released its decision in *MacDonald v. The Queen*,[1] which addressed the test for whether a derivative contract constitutes a hedge of a capital asset.

The taxpayer held common shares of the Bank of Nova Scotia ("**BNS**"). The taxpayer borrowed an amount under a credit facility with Toronto-Dominion Bank and pledged a portion of the BNS shares as collateral. The terms of the credit facility required the taxpayer to enter into a cash-settled forward contract ("**Forward Contract**") with an affiliate of Toronto-Dominion Bank as part of the pledge. The Forward Contract was structured so that the taxpayer would receive cash settlement payments if the BNS share price decreased, and the taxpayer would pay cash settlement payments if the BNS share price increased. The BNS share price appreciated during the life of the Forward Contract such that the taxpayer made cash settlement payments.

The taxpayer took the position that the Forward Contract was speculative and not entered into as a hedge, and that the cash settlement payments were losses on income account such that they were deductible against income from other sources. The CRA reassessed the taxpayer on the basis that the Forward Contract was a hedge against the BNS shares, characterizing the cash settlement payments as capital losses for the years in issue, which could only be deducted against capital gains.

In the decision, the SCC dismissed the taxpayer's appeal, finding that the Forward Contract was a hedge and not speculative. A derivative contract's purpose, ascertained objectively, is what determines the proper characterization. The primary source for determining such purpose is the linkage between the derivative contract and the underlying risk. The linkage analysis begins by identifying the source of a particular financial risk (e.g., an asset, liability or transaction) and then considering the extent the derivative contract mitigates or neutralizes such risk. Perfect linkage is not required, but the more effective the mitigation and the more closely connected the derivative contract is to the item purported to be hedged, the stronger the inference that the purpose of the derivative contract was to hedge.

In this case, there was a substantial link between the taxpayer's BNS shares and the Forward Contract. Considering the whole context of the Forward Contract and the credit facility, the SCC found it was clear that the purpose of the forward contract was to hedge against the risk that the taxpayer's BNS shares were exposed to.

Of note, evidence attempting to establish the taxpayer's subjective intention in entering into the derivative contract was not determinative. The SCC stated that whether a derivative contract is a hedge is mainly decided by the objective purpose of the contract, as determined by examining the link between the derivative contract and any underlying asset using a two-step linkage analysis:

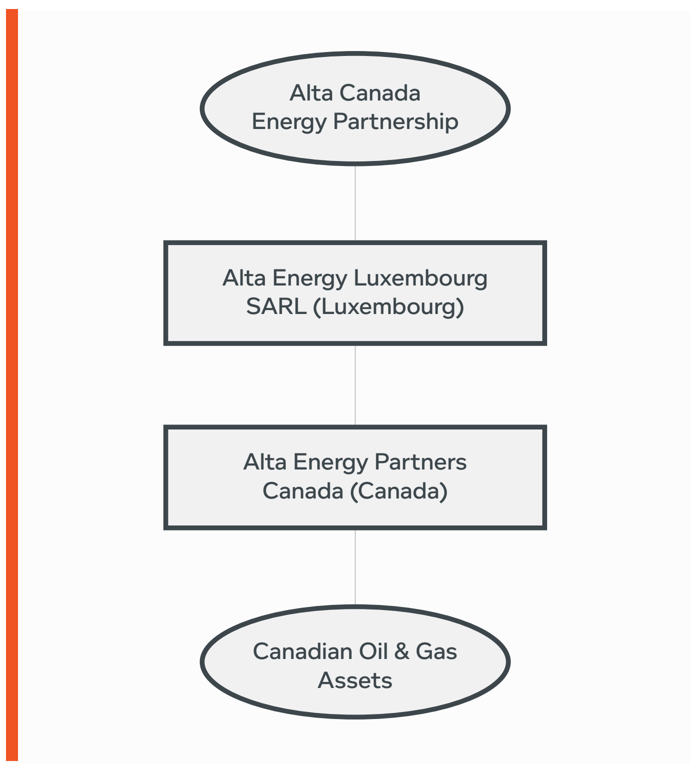
- identify an underlying asset, liability or transaction that exposes the taxpayer to financial risk; and
- assess the extent to which the derivative contract mitigates or neutralizes the risk identified in first step.

A more detailed discussion of this case can be found here.

Is Treaty Shopping Abusive (Alta Energy, FCA)?

The FCA released its decision in The Queen v. Alta Energy Luxembourg S.A.R.L.,[2] in early February 2020, which held that the General Anti-Avoidance Rule ("**GAAR**") did not apply to the sale of shares that were "taxable Canadian property" that met an exemption from Canadian tax under the Canada-Luxembourg Tax Treaty ("**Treaty**").

The taxpayer, a resident of Luxembourg ("**Alta Luxemberg**"), sold its shares of its wholly-owned Canadian resident subsidiary, Alta Energy Partners Canada Ltd. ("**Alta Canada**"), realizing a capital gain in excess of $380 million. The taxpayer claimed that this capital gain was exempt from Canadian income tax, pursuant to Article 13 of the Treaty. While the Treaty generally provides Canada with the right to tax gains on the disposition of immovable property situated in Canada (which includes shares, partnership interests, and interests in trusts that principally derive their value from immovable property situated in Canada), the definition of immovable property in the Treaty is defined to exclude property (other than rental property) in which the business of the company, partnership, or trust was carried on ("**Exemption**").



On appeal, the Crown conceded that the Exemption did apply, but argued that the transactions in issue were abusive such that the GAAR should apply. The Crown's argument was that the object, spirit, and purpose of the relevant provisions of the Treaty were intended to benefit: (i) Luxembourg investors (i.e., not simply residents), (ii) entities that have the potential to earn income in Luxembourg, and (iii) entities that have commercial or economic ties to Luxembourg. Essentially, the Crown was attempting to use the GAAR to create two classes of residents – those that could rely on the Exemption and those that could not. The FCA rejected these arguments, finding that the object, spirit, and purpose was reflected in the words of the provisions themselves. The Exemption applies to residents of Luxembourg, and the GAAR could not be used to justify adding a requirement that was not present in the provisions of the Treaty.

The FCA also dismissed the Crown's argument that the "treaty shopping" by Alta Luxembourg was abusive, with reference to the Tax Court of Canada's ("**TCC**") decision in *MIL (Investments) S.A.*, 2006 TCC 460, which stated that the shopping or selection of treaties to minimize taxes cannot on its own be considered abusive. Although steps taken by the Department of Finance subsequent to the transactions in this appeal to curb treaty shopping were not relevant, the Court did indicate that they may be relevant with respect to future transactions.

The Court was referring to the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Sharing* ("**MLI**"), which entered into force for Canada on December 1, 2019, and, as a result, entered into effect for some of Canada's tax treaties which would apply for withholding taxes on January 1, 2020, and for other taxes (including capital gains taxes) for tax years beginning on or after June 1, 2020, (which for calendar year taxpayers would be January 1, 2021). The MLI will need to be contemplated when considering international structures that rely on treaty exemptions going forward. The onus under the principal purpose test in the MLI appears to flip to the taxpayer the burden to establish that the tax benefit is in accordance with the object and purpose of the applicable tax treaty. In addition, the Crown was successful in obtaining leave to appeal the FCA decision to the SCC, which is currently scheduled to be heard in early 2021.

Transfer Pricing (Cameco, FCA)

In June 2020, the FCA unanimously dismissed the Crown's appeal in The Queen v. Cameco Corporation.[3] The case involved the interpretation of the transfer pricing substitution rules in paragraphs 247(2)(b) and (d) of the Tax Act ("**Substitution Rules**"), and provides helpful guidance on the scope of such rules.

The taxpayer entered into contracts to sell a substantial portion of its uranium to its Swiss subsidiary ("**Uranium Contracts**"), and also guaranteed long-term contracts entered into by the Swiss subsidiary to purchase uranium from third parties. The Swiss subsidiary earned substantial profits under the Uranium Contracts, due to an increase in the price of uranium. The Minister reassessed the taxpayer, reallocating the profits earned by the Swiss subsidiary to the taxpayer pursuant to the Substitution Rules.

The Substitution Rules provide a mechanism for the Minister to make transfer pricing adjustments where a non-arm's length transaction or series

of transactions: (i) would not have been entered into between persons dealing at arm's length, and (ii) it can reasonably be considered not to have been entered into primarily for bona fide purposes other than to obtain a tax benefit. Where this is the case, the transaction or series is substituted with the transaction or series that would have been entered into between persons dealing at arm's length, under terms and conditions that would have been made between persons dealing at arm's length.

The decision focused on whether or not the test for the Substitution Rules to apply is subjective or objective. The Crown's argument was that the test is subjective – *the taxpayer* would not have entered into the transactions undertaken with the Swiss subsidiary with an arm's length person. In opposition, the taxpayer argued that the test is objective and could only be met if *no person dealing at arm's length* would have entered into the transaction or series in issue.

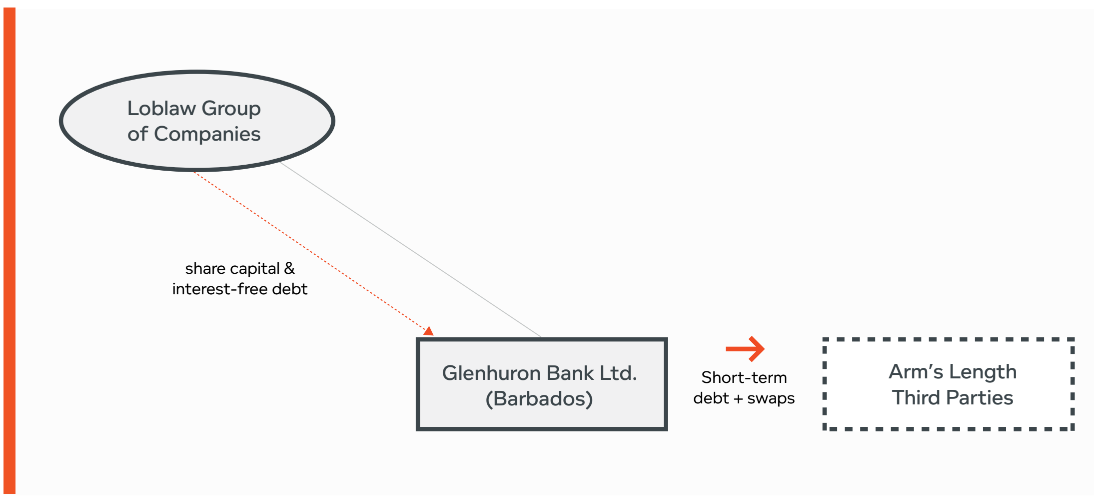
The Court conducted a textual, contextual and purposive analysis. The textual analysis determined that the wording of the provisions made it clear that Parliament intended it to be an objective test – satisfied only when no arm's length parties would enter into the transaction in question. The transfer pricing rules were intended to allow an adjustment of the pricing in a relevant transaction, not to allow the CRA to effectively ignore the separate existence of a foreign subsidiary and reallocate its profits back to its Canadian resident parent.

In deciding in favour of the taxpayer, the Court noted that the economic benefit of participating in the uranium purchase agreements at the time the contracts were entered into was negligible. The profit that was proposed to be reallocated to the taxpayer resulted from the increase in the price of uranium, which the parties could not forecast. This was an inappropriate use of hindsight and after applying the objective test, the Court held that the Substitution Rules did not apply, because there was no evidence that parties dealing with each other at arm's length would not have entered into the contracts in question.

The Crown sought leave from the SCC to appeal this decision on October 30, 2020.

Interpretation to Regulated Banking Exception to the Definition of "Investment Business" in FA Rules (Loblaw, FCA)

In Loblaw Financial Holdings Inc. v. The Queen,[4] the FCA considered the arm's length regulated bank exclusion from the definition of an "investment business" in subsection 95(1) of the Tax Act. At issue was whether income earned by a controlled foreign affiliate of the taxpayer resident in Barbados was from an "investment business". If so, it would be considered income from property and included in the taxpayer's foreign accrual property income ("**FAPI**") (i.e., the income of the foreign affiliate would be included in the income of and taxed in the hands of the taxpayer on an accrual basis). The decision is particularly important to Canadian financial institutions with subsidiaries carrying on banking and other financial businesses outside of Canada.



The taxpayer was the sole shareholder of Glenhuron Bank Limited ("**Glenhuron**"), a Barbados corporation that was registered as a bank in Barbados. Glenhuron was a controlled foreign affiliate of the taxpayer and was largely capitalized with equity and interest-free loans from the taxpayer and other members of the group. In the taxpayer's view, Glenhuron qualified for the regulated financial institution exception from being an "investment business" under subsection 95(1) ("**Foreign Bank Exclusion**") and the income of Glenhuron was active business income for the purposes of the foreign affiliate rules. The Foreign Bank Exception required that Glenhuron was a regulated foreign

bank conducting its business principally with arm's-length persons and that it had more than five full-time employees. The CRA subsequently reassessed the taxpayer for several taxation years, on the basis that Glenhuron conducted its business principally with non-arm's length corporations (i.e., the entities that capitalized and directed it), so the income earned by Glenhuron constituted income from an investment business and FAPI to the taxpayer. It is worth noting that pursuant to a 2014 amendment (subsequent to the years in question) the Foreign Bank Exception was narrowed to only apply to foreign affiliates of Canadian financial institutions.

The question in this case was who Glenhuron conducted its business with, which necessarily required an analysis of what business Glenhuron conducted. Central to this determination was whether funds received by Glenhuron for use in its business were part of the conduct of Glenhuron's business for purposes of the definition of "investment business".

The Court held that the business conducted by Glenhuron consisted of entering into contracts with respect to short-term debt securities and swap transactions. All of these transactions were entered into with arm's length persons. Although the taxpayer provided "direction, support and oversight" with respect to these arm's length transactions, this was not the business Glenhuron conducted. Glenhuron's predominant business activity was to decide what areas of business to pursue and what specific income-earning contracts to enter into, and then to implement those transactions. The Court looked to the purpose of the Foreign Bank Exclusion and found that Parliament could not have intended that it should be denied as a result of support and oversight provided by a parent corporation, because the provisions were intended to encourage Canadians to carry on business outside of Canada. Other than the supporting role provided by the taxpayer, Glenhuron's business activity was conducted entirely with arm's length persons.

Investment in Glenhuron was a shareholder decision and the Court was not convinced that such inflow of funds involved business conducted by Glenhuron (e.g., the receipts did not occupy the time, attention, and labour of Glenhuron employees). As such, Glenhuron met the Foreign Bank Exclusion and its income was not included in the FAPI of the taxpayer.

As indicated above, the impact of this decision has been narrowed by the enactment of subsection 95(2.11) of the Tax Act in 2014, which restricts the Foreign Bank Exclusion to controlled foreign affiliates of financial institutions..

The Crown sought leave to appeal to the SCC, which was granted on October 29, 2020, so there will be more to come on this.

What is Debt for the Purposes of the Tax Act (Barejo, FCA[5])?

At issue in this case was whether two contracts, labelled "Notes", were debt for purposes of paragraphs 94.1(1)(a), despite the amounts under the Notes being unknown and unascertainable until the Notes would come to term.

The Notes were purchased by a controlled foreign affiliate ("**CFA**") of the taxpayer in 2001 for USD 498 million, representing the net asset value of the underlying reference assets ("**Reference Assets**") at the time. The Reference Assets comprised interests in a group of professionally managed hedge fund investments. The net asset value of the Reference Assets grew to over $1.7 billion by the end of 2009. The value of the Notes, which was derived from the value of the Reference Assets, was in constant flux. Thus any amounts to be paid under the Notes would remain unknown until maturity or early termination.

The offshore investment property rules ("**OFIP**") in paragraph 94.1(1)(a) could only apply to the taxpayer to include amounts in the taxpayer's income in respect of the Notes held by the CFA prior to maturity or disposition if the Notes were "debt". The term "debt" is not defined for the purposes of the Tax Act. Given this, the taxpayer argued that the term debt should be given its ordinary legal meaning. The Court disagreed and stated that the term "debt" was capable of a variety of meanings and that a textual, contextual and purposive analysis of paragraph 94.1(1)(a) was necessary to determine the meaning of the term debt for the purposes of that provision.

The FCA stated that a term can have a different meaning depending on the context in which it is used and this is particularly so with the Tax Act given that it is a statute known for its specificity and complexity. The FCA, in referring to case law in respect of the meaning of the term "partnership" for the purposes of section 96 of the Tax Act, suggested that even the term partnership could have a different meaning for other sections of the Tax Act.

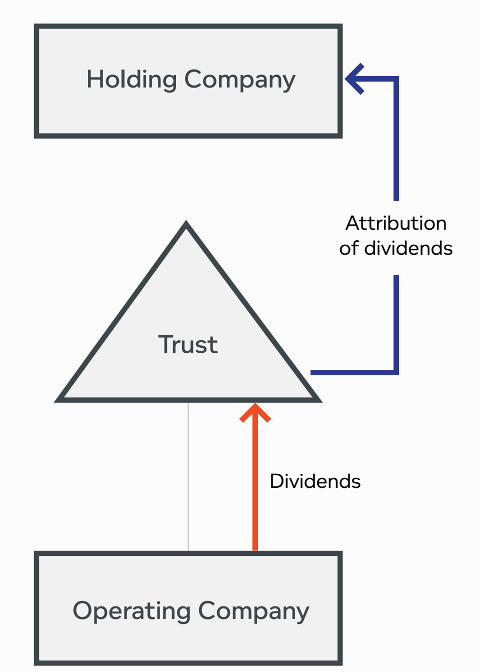
The FCA held that debt existed for the purposes of paragraph 94.1(1)(a) when (i) an amount or credit is advanced by one party to another party; (ii) an amount is to be paid or repaid by that other party at some point in the future in satisfaction of the advance; and (iii) this amount is fixed or determinable or will be ascertainable when payment is due.

This is an important decision because it discusses the hallmarks of debt, but more importantly it states that an undefined term could have different meanings under different sections of the Tax Act, depending on the text, context and purpose of the particular provision.

Rescission to Fix Tax Mistakes (Collins Family Trust, British Columbia Court of Appeal)

The transactions considered by the Court in Collins Family Trust v. Canada,[6] involved a well-known tax plan that purported to protect corporate assets from creditors without incurring income tax liability. The plan was devised to use the attribution rule in subsection 75(2) of the Tax Act, and the intercorporate dividend deduction under subsection 112(1).

Simplified, the plan involved the creation of a family trust with a holding company as a beneficiary, a loan from the holding company to the trust that was used to purchase shares in an operating company from the holding company, and the payment of dividends on the purchased shares from the operating company to the trust. No income tax would be payable by the trust on dividends from the operating company, as the dividend income would be attributed to the holding company under subsection 75(2) of the Tax Act, and the holding company would receive a deduction under subsection 112(1).



The accounting firm that devised the plan was relying on the CRA's administrative policy that the mode of transferring property (i.e., by way of a sale or gift) was irrelevant for the purposes of applying the attribution rule in subsection 75(2). Following the implementation of the plan, the TCC decision in *Sommerer*, 2011 TCC 212 adopted a narrower interpretation of subsection 75(2), and the FCA affirmed this decision (2012 FCA 207). Under this narrower interpretation, the attribution rule in subsection 75(2) did not apply where the property in question was sold to a trust, as opposed to gifted to the trust, or used to settle the trust. This had a significant effect on the plan that was implemented, and the CRA contacted the taxpayers asserting that the dividends were to be included in the income of the trust and, as an alternative position, that the GAAR would apply to include the dividends in the trust's income for tax purposes. Notices of reassessment were issued against the taxpayers, and the taxpayers petitioned the Court seeking to rescind the transactions.

The British Columbia Court of Appeal had previously decided a case involving near identical facts in *Pallen Trust*, 2015 BCCA 222, finding that rescission was an appropriate remedy in the circumstances.

In this case, the Crown was arguing that the chambers judge had failed to properly consider the Supreme Court of Canada decisions in *Fairmont*, 2016 SCC 56 and *Jean Coutu* 2016 SCC 55, which dealt specifically with rectification (i.e., not rescission). The Court held that neither *Fairmont* nor *Jean Coutu* undermined the principles expressed and applied in *Pallen Trust*. Although rectification and rescission are both equitable remedies, each has its own legal test. The Court effectively distinguished the test for rescission from the narrowed test for rectification and confirmed that rescission remains available in circumstances involving a "causative mistake of sufficient gravity", which is a mistake as to either the legal character or nature of a transaction or some matter of fact or law which is basic to the transaction. Rescission may be a viable solution for fixing a mistake, even in light of the narrowing of rectification.

Sales Tax - Legislation

LEGISLATION

Legislative developments from a Canadian sales tax perspective (goods and services tax ("**GST**"), harmonized sales tax ("**HST**), Québec sales tax ("**QST**"), and the provincial sales tax ("**PST**") of British Columbia, Manitoba and Saskatchewan) were somewhat limited throughout the year, at least until November 30, 2020, when the Government, in its Fall Economic Statement 2020, announced its intention to implement new GST/HST registration and collection requirements for non-resident vendors and digital platform operators, which the Government referred to as measures to provide "A Fair Tax System for the Digital Economy".

With the exception of the government of Saskatchewan, which has adopted new retroactive registration and collection requirements for e-commerce providers, the Government and most provincial governments were reluctant to adopt new tax measures from a Canadian sales tax perspective in 2020 (both the British Columbia and the federal government announced measures to address the digital economy that would become effective in 2021). It is not surprising that governments for the first half of the year focused on adopting temporary relief measures aimed at deferring the filing of sales tax returns and the remittance of all Canadian sales tax that became owing during specific periods of time, all of which have now ended. Businesses that continue to encounter financial difficulties in remitting sales tax could request flexible payment arrangements with the relevant tax authorities under certain circumstances.

New PST Registration and Collection Requirements in Saskatchewan for E-Commerce Businesses

On July 3, 2020, Bill No. 211, *An Act to amend The Provincial Sales Tax Act*, which broadens the application of the Saskatchewan PST by enacting new registration and collection requirements for e-commerce platforms, received royal assent. These new rules apply with retroactive effect to January 1, 2020.

Under the new rules, operators of "electronic distribution platforms" and "online accommodation platforms", as well as "marketplace facilitators", whether they carry on business in Saskatchewan or not, may now be required to register as "vendors" under the expanded definition of such term, for the purposes of collecting and remitting applicable Saskatchewan PST on sales to consumers or users in Saskatchewan generated through their platforms.

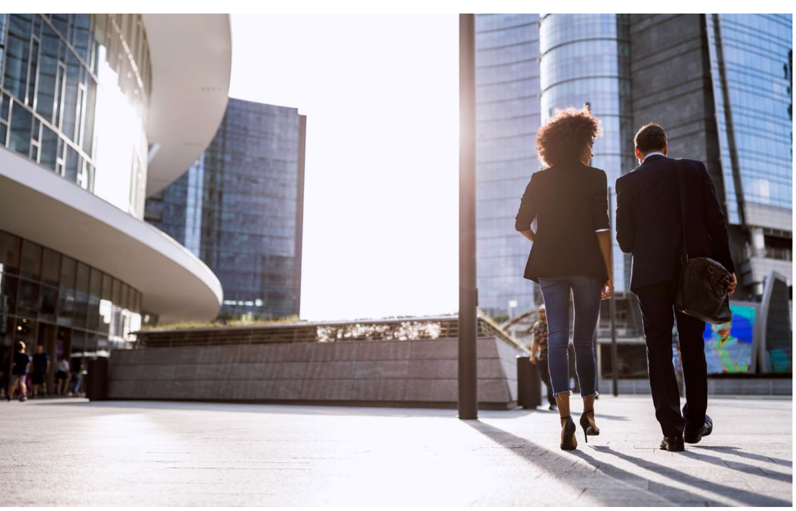
A more comprehensive summary of applicable rules can be found here.

These new rules are part of a broader global trend to tax digital platforms across the world, including in Canada. For now, and although very limited guidance has been issued by the Saskatchewan Ministry of Finance, we assume that these new requirements are intended to pass on the burden to account for the collection and remittance of the PST to platform and marketplace operators, but such assumptions remain subject to further clarifications.

Proposed New PST Registration and Collection Requirements in British Columbia for Canadian and Foreign Sellers

In its 2020 Budget (released on February 18, 2020), the government of British Columbia announced changes to the PST legislation, including new registration and collection requirements for Canadian sellers of goods, and Canadian and foreign sellers of software and telecommunication services. The implementation of these measures was postponed to provide relief in response to COVID-19.

On September 2, 2020, the government of British Columbia confirmed that effective April 1, 2021, Canadian sellers of goods and Canadian and foreign sellers of software and telecommunication services will be required to register to collect BC PST if their "specified BC revenues" exceed $10,000. At the time of publication, the expression "specified BC revenues" was not defined, but the assumption is that it is intended to include revenues earned from taxable sales made to consumers or users in the province. Accordingly, registration and collection requirements should be assessed and monitored closely by Canadian sellers of goods and Canadian and foreign sellers of software and telecommunication services, with the objective of bringing their activities and systems within compliance by April 1, 2021.



New GST/HST Registration and Collection Requirements for E-Commerce Businesses

As part of the global trend to tax digital economy and with the increasing importance of e-commerce, especially since the beginning of the COVID-19 pandemic, the Government announced in its Fall Economic Statement 2020, its intention to enact new GST/HST registration and collection requirements for non-resident vendors and digital platform operators effective July 1, 2021. The new proposed rules virtually mirror those adopted in Québec almost two years ago for QST purposes regarding supplies made to Québec consumers by foreign suppliers and operators of digital accommodation platforms. Further details on the Québec regime can be found here.

The Government announced in its Fall Economic Statement 2020, its intention to enact new GST/HST registration and collection requirements for non-resident vendors and digital platform operators effective July 1, 2021.

To level the playing field between Canadian and non-resident vendors, and to ensure that GST/HST applies to all goods and services consumed in Canada, non-resident vendors and distribution platform operators would be required to register, collect, and remit applicable GST/HST on all taxable supplies of digital products and services made or facilitated to Canadian consumers to the extent the total of such taxable supplies exceeds, or is expected to exceed, $30,000 over a 12-month period.

A similar set of rules is proposed for any accommodation platform operator who facilitates or expects to facilitate over a 12-month period more than $30,000 in taxable supplies of short-term accommodations[7] in Canada where the underlying third-party suppliers/owners of the accommodations are not registered for the GST/HST under the usual GST/HST regime. Under the new measures, discretionary authority is granted to the CRA to disclose, in any manner that the CRA considers appropriate, the name of any person registered under this new simplified GST/HST registration regime, including their effective date of registration. Although similar to the QST, such discretionary authority is quite unusual in the context of the GST/HST. It is also noteworthy that the proposed new rules provide, in certain circumstances, new disclosure and record keeping obligations, including the obligation to file with the CRA an annual information return in certain cases.

Finally, as part the new GST/HST measures, the Government also proposes to require distribution platform operators to register under the normal GST/HST rules, and to collect and remit the GST/HST in respect of sales of goods that are located in fulfillment warehouses in Canada, or shipped from a place in Canada to a purchaser in Canada, where those sales are made by non-registered vendors through distribution platforms. Non-resident vendors would also be required to register under the normal GST/HST rules and to collect and remit the GST/HST in respect of sales of goods that are located in fulfillment warehouses in Canada or shipped from a place in Canada to a purchaser in Canada, where those sales are made by the non-resident vendors on their own behalf.

To Come in 2021

In 2021, there may be significant federal tax measures including rules affecting interest deductibility, both income tax and GST/HST measures in respect of the digital economy, and possibly a number of new revenue raising measures given the federal deficit is expected to be approximately $382 billion in 2020-21. The Government may also launch consultations in respect of Canada's anti-avoidance rules and there may be decisions in key tax cases from the SCC.

LIMIT ON ALLOWABLE INTEREST DEDUCTIONS

In its October 2019 campaign, the Liberal party announced two significant proposals to limit the deduction of interest. Since the Liberal party only formed a minority government, it is not clear whether they will proceed with these proposals in 2021. As described below, both proposals would be consistent with recommendations from the Organisation for Economic Co-operation and Development ("**OECD**").

30% EBITDA Limitation

The first proposal would limit the amount of interest that a corporation could deduct against its income for a taxation year to no more than 30% of earnings before interest, taxes, depreciation and amortization ("**EBITDA**"), subject to certain exceptions. Corporations would be allowed to carry back three years, or carry forward twenty years, any denied interest deductions. The limitation would apply to corporations with an annual net interest expense exceeding $250,000. Corporations that are part of a multinational group would be able to deduct above the 30% ratio, up to the group's worldwide ratio.

The Government's proposal, which has not proceeded beyond the 2019 announcement, aligns with the OECD's report, "Limiting Base Erosion Involving Interest Deductions and Other Financial Payments, Action 4 - 2016 Update", under the *OECD/G20 Base Erosion and Profit Shifting Project* ("**BEPS**"). The report recommended a benchmark net interest/EBITDA ratio within a corridor of 10% to 30%.

Anti-Hybrid Rules

The second proposal would implement anti-hybrid rules that would deny the deduction of interest on hybrid debt arrangements (arrangements or instruments that are debt for Canadian tax purposes but treated otherwise for foreign tax purposes).

Many countries have enacted legislation that addresses the OECD's recommendations on hybrid debt mismatch arrangements. The Government's proposal aligns with the OECD's report, "Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 - 2015 Final Report", under the BEPS. The report recommended that countries deny the taxpayer's deduction for payments to the extent that such deduction is not included in the taxable income of the recipient in the counterparty jurisdiction, or if it is also deductible in the counterparty jurisdiction.

In addition, the United States has enacted its own anti-hybrid rules and released final regulations in respect of these rules on April 7, 2020.

COMBATTING INTERNATIONAL TAX EVASION AND AGGRESSIVE TAX AVOIDANCE

In the Fall Economic Statement 2020, the Government proposed to provide an increase of $606.2 million over five years for additional auditors and upgraded tools to combat international tax evasion and tax crimes such as money laundering and terrorist funding. These budgetary increases are to begin in 2021-2022.

In addition, the Government stated that taxpayers have been able to create increasingly complex structures to artificially lower their tax obligations in a manner that does not serve an economic purpose, including by shifting profits offshore and creating artificial tax deductions. To address this, the Government stated it will launch consultations in early 2021 in respect of the modernization of Canada's anti-avoidance rules, in particular the general anti-avoidance rule.

INCOME TAX MEASURES FOR THE TAXATION OF THE DIGITAL ECONOMY

In the Fall Economic Statement 2020, the Government stated it is supportive of the OECD's project to develop a coordinated multilateral approach to the taxation of the digital economy, but is concerned about a delay in arriving at consensus. The Government therefore proposes to implement a tax on corporations providing digital services, with effect from January 1, 2022, which would apply until such time as an acceptable common OECD approach comes into effect. The Government indicated that further details on its proposed approach will be announced in Budget 2021.

EXPANDED FOREIGN AFFILIATE REPORTING FOR MULTINATIONAL CORPORATIONS

On November 27, 2020, the CRA released a preview of the revised Form T1134, "Information Return Relating to Controlled and Non-Controlled Foreign Affiliates". The revised form, which must be filed by all Canadian resident taxpayers and partnerships for any year in which the taxpayer or partnership has an interest in a foreign affiliate at any time in the year, will be officially released in January 2021. The new form will be effective for taxation years or fiscal periods that begin after 2020, and must be filed within 10 months of the year end, as opposed

to the old form, which must be filed within 15 months of the year end (or 12 months for fiscal periods that start in 2020 only). No legislative amendments to section 233.4 of the Tax Act, which provides for reporting requirements in respect of foreign affiliates, accompany the revised form.

The additional reporting requirements will include information relating to the reporting entity's activities, involvement in certain transactions or arrangements, and dividend elections, as well as information relating to the foreign affiliates' gross revenue, adjusted cost base of directly owned shares, reorganizations, and foreign accrual property losses and foreign accrual capital losses. The revised form will also include relieving measures such as joint filing options and easing the criteria for certain filings.

GLOBAL TREND OF THE DIGITAL ECONOMY TAXATION AND NEXT STEPS ANTICIPATED FROM A GST/HST PERSPECTIVE, AS WELL AS ELIMINATION OF THE ITR RESTRICTIONS ON CERTAIN RESTRICTED EXPENSES

While the Government invited interested parties to submit comments and concerns on the new GST/HST measures by February 1, 2021, it is reasonable to expect the enactment of such new GST/HST registration and collection measures within the time frame provided in the Fall Economic Statement 2020 and legislative proposals (i.e., July 1, 2021). The Government estimated that these proposed measures combined together will increase federal revenues by over $2.5 billion over 5 years, starting in 2021- 2022.

With the increasing importance of e-commerce transactions and the new measures proposed or enacted by the provincial governments of British Columbia and Saskatchewan in their PST regime, it would not be surprising that such new PST rules also be enacted by the government of Manitoba in the upcoming year.

As previously announced by the Québec Minister of Finance, the phasing out of the input tax refunds ("**ITRs**") for large businesses will be complete as of January 1, 2021, essentially meaning that large businesses will be, as of this date, entitled to claim 100% of the QST paid or that became payable on or after January 1, 2021,[8] in respect of the acquisition of restricted goods and services to which the ITR restrictions would have otherwise applied to. This will also alleviate compliance concerns related to the complexity of these measures.

CASES GOING UP TO THE SUPREME COURT OF CANADA

Despite the SCC's usual hesitance to grant leave to tax law cases, leave was granted in *Alta Energy* and *Loblaw Financial Holdings* and the leave application in *Cameco* is still pending. These cases could have important implications.

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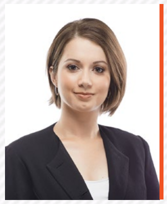

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Endnotes

1 2020 SCC 6.

2 2020 FCA 43.

3 2020 FCA 112.

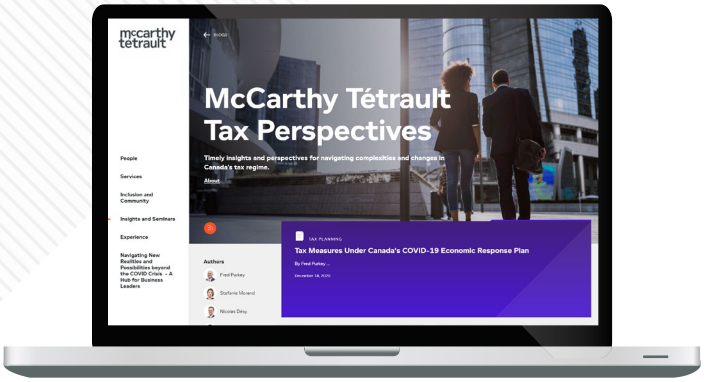
4 2020 FCA 79.

5 2020 D.T.C. 5023 (FCA).

6 2020 BCCA 196.

7 Generally including a rental of a residential complex or a residential unit to a person for a period of less than one month where the price is more than $20 per day.

8 The phasing out of the ITR restrictions started in 2018, and as a result, large businesses have been entitled to claim ITRs on restricted expenses at the rate of: 25% for 2018, 50% for 2019 and 75% for 2020.



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