Doing Business in Canada

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Daryl Maduke
Tax Partner, Corporate & International Tax

Daryl has over 20 years of experience in public practice. Daryl's practice is broad based, including domestic and international tax-planning. He advises on cross-border and domestic mergers and acquisitions, corporate reorganizations, spin-offs, and financings. Daryl has significant experience in advising Canadian and foreign multi-national corporations, private equity funds, venture capital funds, and privately owned businesses. Daryl manages his clients' Canadian tax compliance requirements and advises on the strategic development and execution of transactions from a tax perspective.

Daryl also has relevant experience with the preparation and review of income tax provisions and supporting documentation for both private and public company financial statement presentation. He also regularly manages due diligence projects, determining potential tax liabilities and exposure, and assisting with the tax aspect of purchase agreements, post-closing, and other transaction tax matters.

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Professional Designations & Education

Chartered Accountant, Institute of Chartered Accountants of British Columbia (2004)

Bachelor of Science - Physics, University of British Columbia (1998)

Professional Affiliations

Member, Institute of Chartered Accountants of British Columbia (ICABC)

Canadian Tax Foundation

International Fiscal Association

Contents

Glossary

Term	Definition
BEPS	Base erosion and profit shifting
BC	British Columbia
COB	Carrying on business
CRA	Canada Revenue Agency
FTE	Flow-through entity, or, fiscally transparent entity
GST	Goods and services tax
HST	Harmonized sales tax
ITA	*Income Tax Act (Canada)*
LLC	Limited liability company
MLI	Multilateral Instrument
MN	Manitoba
OECD	Organisation for Economic Co-operation and Development
PE	Permanent establishment
PST	Provincial sales tax
QST	Quebec sales tax
SK	Saskatchewan
Treaty	Canada- Netherland Income Tax Convention
ULC	Unlimited liability company
US	United States
VAT	Value-added tax

Tax Implications of Doing Business in Canada

OVERVIEW OF CANADIAN TAX

- Canada is a federation made up of 10 provinces and 3 territories
- Federal and provincial governments each have taxing jurisdiction
- Federal tax applies throughout Canada
- Provincial tax is imposed on activities within the province
- Most provinces have a collection agreement with the federal government who administers collection of tax
- Corporations are subject to the following taxes:
  - Canadian federal income tax;
  - Federal goods and services tax (GST or HST);
  - Social security tax; plus
  - Provincial taxes of varying nature
  - Non-resident withholding taxes on cross border payments.

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OPERATING LOSSES AND GROUP LOSS TRANSFERS

- No tax consolidation filing in Canada
- Loss utilization tax planning for a related group (*i.e.*, loss transfers via intercompany transactions, mergers, liquidations, etc.)
- No carryover of tax losses on incorporation of a Canadian branch
- Net operating losses can be used to offset against current year profits
  - 3 year carry back and 20 year carry forward period against profits of other years
- Capital losses may only be deducted against capital gains
  - Capital losses may be carried back 3 taxation years and forward indefinitely
- Special rules applicable on direct or indirect acquisition of control of a Canadian corporation that limit use of losses

Tax Implications of Doing Business in Canada

Carrying on Business:

- Under the ITA, a non-resident carrying on business in Canada is subject to income tax under Part I of the ITA on taxable income earned in Canada. It is a question of fact whether a company will be considered to be carrying on a business in Canada.
- However, subject to the provisions of the Treaty, the company may not be subject to income tax if it does not have a *permanent establishment* in Canada. Instead, the company would file a treaty-based return, disclosing its activities in Canada.
- Non-compliance penalty of $2,500 annually, possible relief through Voluntary Disclosure Program in Canada.

Tax Implications of Doing Business in Canada

Regulations 102 and 105:

Canada has strict regulations when it comes to hiring non-resident employees or engaging non-resident contractors for work in Canada. Very generally, where resident individuals or entities perform services in Canada, there maybe tax payable in Canada in respect of that service and reporting obligations to be met on behalf of the payer and payee. The Treaty may override the domestic tax provisions to exempt either an employee or contractor / service provider where certain criteria is met; however, this is a fact based determination and requires a full analysis.

Tax Implications of Doing Business in Canada

Regulation 102:

Where any person pays a non-resident for employment services *rendered in Canada, that payer is liable to comply with the general Canadian payroll withholding, social security, and compliance provisions of Regulation 102.*

- Foreign company with employees in Canada for any period of time (i.e. single day) are technically subject to Regulation 102.
- Even if the Foreign employees are not subject to tax under the Treaty, Regulation 102 applies unless a waiver is applied for and received prior to payment.
- Non-compliance penalties apply on late remittances and compliance (T4). Compliance is due by the end of February, regardless of the corporate tax year end.

Tax Implications of Doing Business in Canada

Regulation 105:

*Every person paying to a non-resident person a fee, commission or other amount in respect of services rendered in Canada, of any nature whatever, shall deduct or withhold **<u>15% of such payment</u>**.*

- Not a final tax but installment against possible income tax liability in Canada. Refundable if no PE in Canada when tax return is filed.
    - Can create substantial cash-flow issues based on timing of refunds
    - Foreign tax preparers inadvertently pick-up the 15% as a foreign tax credit
- Waiver application possible if applied for in advance.
- Also applies to Foreign companies paying non-resident sub-contractors for services in Canada.
- Non-compliance penalties apply on late remittances and compliance (T4A-NR). February due date for compliance.

Commodity Taxes in Canada

Current Landscape / General Rules

Federal Goods & Services Tax / Harmonized Sales Tax (GST/HST)

- Value-added tax
  - GST/HST generally collected on all transactions, unless zero-rated or exempt
  - Input tax credit (ITC) claimed to refund the tax to businesses engaged in commercial activity
  - Certain 'non-commercial' enterprises (universities, hospitals, public sector bodies, etc.) generally receive partial rebates, rather than ITCs
- 5% GST rate applies across the country, with the "harmonized" provincial component collected for a combined "HST" rate in the specific harmonized provinces being ON, NB, NF, NS and PEI.
- GST/HST not charged on exports or 'exempt' services, such as financial, insurance, medical, many public services, etc.

Current Landscape / General Rules
Provincial Sales Tax

Provincial Sales Tax (PST)

- BC, SK and MB are now the only provinces with their own PST regimes
  - PST applies to taxable tangible personal property (TPP) and carved-in services - software, services to TPP, etc.
  - Retail transaction - applies to the retail customer/purchaser
  - Not creditable, unlike the GST/HST which is fully refundable to commercial businesses
  - Some exemptions – food, medical, qualifying manufacturing, farming, etc.
- Provincial PST registration required even with relatively minimal levels of PST-taxable activity carried on
- Separate return filing requirements for PST provinces in addition to GST/HST

Current Landscape / General Rules
Quebec Sales Tax

Quebec Sales Tax (QST)

- QST is the provincial level of tax (in addition to the 5% GST) that applies in QC.
- QST legislation generally parallels federal GST/HST legislation, is also a value-added tax
  - QST generally collected on all transactions, unless zero-rated or exempt
  - Input tax rebate (ITR) claimed to refund the tax to businesses engaged in commercial activity
- 9.975% QST rate applies on taxable supplies in the province of Quebec, in addition to the 5% GST
- Suppliers usually file separate GST and QST return, unless the business a permanent establishment or is incorporated in Quebec, in which case a combined GST/QST return is filed

New Rules / Federal Digital Sales Tax (DST) and Simplified Quebec Sales Tax (QST)

New Digital Sales Tax (DST) and Simplified QST rules

- Recent response to the “Netflix Tax” found in other countries
- Quebec introduced the Simplified QST in 2019
- Federal government introduced DST effective July 1, 2021

- Response to non-resident vendors rendering various technology/services/Airbnb and other platform services to Canadian consumers, without having enough “nexus” to trigger GS/HST/QST registration under the normal rules.

New Rules - Federal Digital Sales Tax (DST)

Effective July 1, 2021, GST/HST legislation expands to capture:

- Sales of digital products and services provided to Canadian customers,
  - Transactions still taxable even if vendor is not carrying on business in Canada – simplified registration to collect tax only and not allowed to claim ITCs
- Goods supplied through fulfillment warehouses located in Canada and made by non-resident vendors directly through websites, and
  - Vendors generally required to register under the regular rules (to collect/remit tax and to claim ITCs)
- Supplies made via short-term accommodation platforms.
  - Platform operators required to register and tax collectible by the operator, if the non-resident property owner is not registered

New Rules – Simplified Quebec Sales Tax (QST)

Effective 2019, Simplified QST registration required for non-Quebec suppliers

Sales of digital products and services provided to Quebec-consumers

- Registration required under the simplified QST rules, requiring non-Quebec suppliers to register and collect simplified QST on services, digital/intangibles and taxable goods.
- Captures streaming services, SaaS, software apps and fulfillment warehouses.
- Some non-resident suppliers should voluntary register under the normal QST rules, rather than the simplified rules, depending on whether their customers are commercial business customers (entitled to claim an ITC for QST) or end-use consumers (not entitled to claim an ITC).
- Simplified QST is not creditable as an ITC, even if borne by a Quebec business customer
- $30,000 small supplier threshold for registration

New Rules – BC, SK and MB Provincial Sales Tax (PST)

The last 3 PST provinces (BC, SK and MB) are expanding their PST bases to "level the playing field" for PST purposes across the Provinces and to coordinate consumer taxation with GST/HST and QST rules

- BC: Effective April 1, 2021, new non-resident registration requirements for:
  - Digital services/intangibles, SaaS, accommodation platforms (Airbnb) and fulfillment warehouses
  - $10,000 small supplier threshold
- SK: Expanded its rules in 2019/2020, triggering PST registration for non-resident vendors without employees/inventory/place of business in the province.
- MB: Announced Fall 2021 non-resident vendor registration requirements.

2021 Canadian Sales Tax Landscape

Final Thoughts

- Non-resident suppliers selling services, goods, SaaS, digital, fulfillment and accommodations are - effectively - required to register in all jurisdictions across Canada, if selling into all jurisdictions in Canada.
- Differing GS/HST/QST vs. PST remittance threshold means different filing frequencies and compliance obligations.
- Increased audit / compliance requirements with up to 5 separate taxing jurisdictions

What BDO can offer

- Turn-key inbound diagnostic, planning, compliance and support services to non-resident vendors
- Returns preparation and audit support

Speaker's biography

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Partner

Darren is a tax partner in BDO's Vancouver office who has been in public practice since 1998 and has focused his expertise in sales and indirect tax since 2000. He helps clients to understand how sales and indirect tax impacts their business and works with them proactively to help them manage their sales tax risk as their business grows. Key firm and industry roles include:

- Member – CICA Commodity Tax Symposium Committee
- Instructor – Langara College
- BDO Canada LLP – Western Canada Commodity Tax Leader

Darren has presented extensively to public and private sector client groups and industry associations regarding GST/HST transitional issues since 2010 and de-harmonization issues in BC since 2013. He presented at the 2010 CICA Western Commodity Tax Symposium in Calgary on PST transition issues for oilfield services and transportation companies doing business on both sides of the BC/AB border and presented at the Canadian Tax Foundation Annual tax conference in 2010.

Questions?