Tax Insights
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Recent CRA practices deny Regulation 102 waiver requests

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In brief

Recent Canada Revenue Agency (CRA) practices have made it difficult for some non-resident employees working in Canada to obtain CRA waiver approval.

The CRA has acknowledged denying Regulation 102 waiver applications completed on Form R102-R, in respect of an employee's Canadian workdays, if there is a possibility that the foreign employer has a permanent establishment (PE) in Canada. In addition, when a Regulation 105 waiver is denied under the 'days threshold' test, any Regulation 102 waiver applications related to that project are likely to be denied too. The CRA has indicated that further guidance may be released late September 2013 on these matters.

In detail

General rules

Regulation 102

Payments to non-residents of Canada who provide employment services in Canada are subject to the same withholding, remitting and reporting obligations as those for Canadian-resident employees, as Regulation 102 requires.

Even if the employee's country of residence has an income tax treaty with Canada that exempts his or her income from tax in Canada, the employer must still withhold and remit applicable payroll taxes from the employee, unless the employee has received a Regulation 102 waiver from the CRA. If no waiver is obtained, the tax withheld may still be refundable after the employee files an income tax return.

Regulation 105

Payments to non-residents of Canada for services performed in Canada are subject to a 15% withholding, to be remitted to the CRA by the payer, under Regulation 105. This tax is refundable if the non-resident files an income tax return and does not have a PE in Canada.

To avoid the 15% withholding, the non-resident must obtain, in advance of the payment, a valid Regulation 105 waiver from the CRA. In determining if a waiver will be approved, the CRA applies a '240 days' test, which counts the calendar days on which the non-resident had at least one employee or subcontractor physically in Canada to render services over a seven-year span (starting three years before the current year). If that total exceeds 240 days, the Regulation 105 waiver typically will be denied.

Recent CRA Regulation 102 waiver denial practices

The CRA has stated that, generally, waiver officers in the Tax Services Offices will deny Form R102-R waiver applications if they suspect that a foreign employer has a PE in Canada in respect of the work the employee will be doing.

A field officer typically would not 'determine' whether a foreign employer actually had a PE in Canada. An assessment is normally made by the international audit group.

In this regard, the CRA has been linking the Regulation 105 '240 days' test to Regulation 102 waiver applications. For example, if an employer is a service provider and has had a Regulation 105 waiver application denied because it failed the '240 days' test, Regulation 102 waiver officers have tended to deny the R102-R applications for the employees working on that project.

The '240 days' test is a low threshold (an employer could fail with only 60 days each year) and is not representative of typical 'PE thresholds,' including in particular the 183-day test under the 'Services PE' rule in the Canada-US treaty. In some instances, CRA waiver officers have tried to apply the '240 days' test to R102-R applications when no Regulation 105 waiver had been requested.

These apparently recent waiver review practices are creating situations in which legitimate applications are being denied outright, without the officers raising their concerns to the employers so that these concerns can be addressed before denial letters are sent to the employee.

Another practice occurring at certain CRA offices is that, for Regulation 102 waivers to remain valid, some waiver officers are requiring employers and employees to update the CRA monthly with the employee's physical workdays in Canada.

None of these practices has been published. The CRA has advised us that it understands the concerns and that further guidance may be released (possibly by late September 2013).

PwC observations

These recent developments, particularly the CRA's use of the '240 days' test, make it difficult for some non-resident employees, such as those working for service providers, to obtain CRA waiver approval. As a result, some non-resident employers may no longer find it feasible for their employees to request Regulation 102 waivers. This has added unnecessary time and administrative costs for filing personal income tax returns for all non-resident employees in Canada that would otherwise be exempt under a tax treaty.

The CRA's implementation of an employer certification program to allow self-approval of Regulation 102 waivers would be welcome. It would allow the employer to assess the situation up front. Further, if legislative changes are required, the Department of Finance is urged to take the necessary steps.

The takeaway

Without any public announcement, the CRA has been applying guidelines (created in the early 2000s) for Regulation 105 waiver request reviews to those requested under Regulation 102. As a result, CRA field officers do not always approve Regulation 102 waiver requests that a non-resident would expect to be valid.

Applicants should be alert to these developments and perhaps be proactive with any pending waiver requests.

Let's talk

For a deeper discussion of what recent CRA practices regarding Regulation 102 waivers mean, please contact any of the following or your PwC HRS advisor.

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