

Tax Memo

Canada-U.S. Income Tax Treaty: Fifth Protocol Enters into Force

On December 15, 2008 after nearly 10 years of negotiation, the fifth Protocol (the Protocol) to the *Canada-U.S. Income Tax Convention* (Treaty) entered into force. On that date, Canada and the United States notified each other in writing, through diplomatic channels, that their respective applicable procedures have been satisfied.

This *Tax Memo* will consider the Protocol's entry into force under the following headings:

- Coming-into-force Dates
- Withholding Tax on Interest
- Accounting Implications

For a more detailed discussion of the provisions of the Protocol see the following PricewaterhouseCoopers publications, available on www.pwc.com/ca, that discuss the Protocol:

- *Tax Memo*, Canada-U.S. Income Tax Treaty: Fifth Protocol Makes Major Changes;
- *Tax Memo*, Fifth Protocol to the Canada-U.S. Income Tax Treaty – Reflections;
- *Estate Tax Update*, Cross-Border Estate Planning: Effect of Fifth Protocol to the Canada-U.S. Income Tax Treaty; and
- *Tax Memo*, Fifth Protocol to the Canada-U.S. Treaty: Technical Explanation.

Coming-into-force Dates

The entry-into-force provisions should be considered carefully because, in many cases, the effective date depends on the particular change to the Protocol. The provisions of the Protocol generally apply:

- for purposes of **non-resident withholding tax**, to amounts paid or credited on or after February 1, 2009 (i.e., the first day of the second month that begins after the Protocol's entry into force); and
- for **other taxes**, to taxable years beginning after 2008 (i.e., to taxable years beginning after the calendar year in which the Protocol enters into force).

Important exceptions to these dates follow.

		Effective Date	
Treaty Change	Withholding tax rate changes	Interest rate reductions	January 1, 2008
		Other rate changes	February 1, 2009
	Limited Liability Companies (LLCs) (and other fiscally transparent entities)	Payments subject to withholding (including interest, royalties and dividends)	Payments made on or after: February 1, 2009
		Capital gain and permanent establishment exemptions	Taxable years (presumably of the eligible member of the LLC) that begin after 2008
	Employee taxation	2009 and subsequent calendar years	
	Permanent establishment rules for service providers	The third taxable year that ends after December 15, 2008	
	Hybrid entity treaty denial rules	2010 and subsequent calendar years	
Limitation on benefit changes	Depends on the provision that would otherwise give rise to the treaty benefit		

Withholding Tax on Interest

Both Canada and the U.S. have confirmed that the reduced withholding tax rates on interest will apply retroactive to January 1, 2008. For more information, see our *Tax Memo*, "Withholding Tax on Interest – Welcome Changes for 2008 and Beyond," dated April 25, 2008.

The reduced withholding tax on interest paid to related parties will be phased in over three years, starting in 2008, as follows:

- before 2008 – 10%
- January 1, 2008 – 7%
- January 1, 2009 – 4%
- January 1, 2010 – Nil

If tax has been withheld at 10% on related-party interest payments made during 2008, consideration should be given to the options for recovering the excess withholding tax paid. These may include:

- adjusting future withholdings for the remainder of 2008;
- preparing NR4s, "Statement of Amounts Paid or Credited to Non-Residents of Canada," reflecting revised withholding tax amounts to request a refund using the NR4 Summary process; or
- having the non-resident file an NR7-R, "Application for Refund of Non-resident Part XIII Tax Withheld" request no later than December 31, 2010.

Accounting implications

The Protocol is considered substantively enacted for Canadian GAAP and enacted for U.S. GAAP purposes as of December 15, 2008. Therefore, the effects of the Protocol changes should be taken into account when calculating current and future income tax balances.

For More Information

Please contact any of the individuals listed on page 3 or page 4 for more information on this topic.

PricewaterhouseCoopers Contacts

International Tax			
Calgary	Murray Lee	403 509 7576	<i>murray.lee@ca.pwc.com</i>
	James Meadow	403 509 7353	<i>james.m.meadow@ca.pwc.com</i>
	Dale Meister	403 509 7584	<i>dale.s.meister@ca.pwc.com</i>
Vancouver	Michael Balaski	604 806 7073	<i>michael.e.balaski@ca.pwc.com</i>
	Paul Bush	604 806 7021	<i>paul.bush@ca.pwc.com</i>
	Bettina Charpentier	604 806 7026	<i>bettina.charpentier@ca.pwc.com</i>
	William Holms	604 806 7052	<i>william.holms@ca.pwc.com</i>
	Bruce McGregor	604 806 7079	<i>bruce.mcgregor@ca.pwc.com</i>
	Lincoln Schreiner	604 806 7713	<i>lincoln.schreiner@ca.pwc.com</i>
	Michael Shields	604 806 7802	<i>michael.shields@ca.pwc.com</i>
Montreal	Jay Black	514 205 5033	<i>jay.black@ca.pwc.com</i>
	Pierre Bourgeois	514 205 5139	<i>pierre.bourgeois@ca.pwc.com</i>
Toronto	Paul Barnicke	416 869 2369	<i>paul.l.barnicke@ca.pwc.com</i>
	Ken Buttenham	416 869 2600	<i>ken.buttenham@ca.pwc.com</i>
	Stephen Dunk	416 365 8239	<i>steve.dunk@ca.pwc.com</i>
	Melanie Huynh	416 869 2941	<i>melanie.huynh@ca.pwc.com</i>
	Eric Lockwood	416 365 8180	<i>eric.lockwood@ca.pwc.com</i>
	Mike Maikawa	416 365 2719	<i>mike.maikawa@ca.pwc.com</i>
	Andy McAskile	416 869 8725	<i>andrew.mcaskile@ca.pwc.com</i>
Gregory Papinko	416 869 8702	<i>gregory.j.papinko@ca.pwc.com</i>	
Toronto North	Arlene Cohen	416 228 1012	<i>arlene.cohen@ca.pwc.com</i>
Mississauga	Dan Fontaine	905 949 7313	<i>dan.g.fontaine@ca.pwc.com</i>
Transfer Pricing			
Toronto	Andy McCrodan	416 869 8726	<i>andrew.f.mccrodan@ca.pwc.com</i>
	Martin Skretkowicz	416 815 5027	<i>martin.p.skretkowicz@ca.pwc.com</i>
Personal Tax			
Calgary	Dave Peters	403 509 7481	<i>dave.peters@ca.pwc.com</i>
Vancouver	Diane Akelaitis	604 806 7011	<i>diane.akelaitis@ca.pwc.com</i>
Montreal	Jean Milot	514 205 5186	<i>jean.milot@ca.pwc.com</i>
Toronto	Jerry Alberton	416 365 2746	<i>jerry.alberton@ca.pwc.com</i>
Windsor	Loris Macor	519 985 8913	<i>loris.macor@ca.pwc.com</i>
Wilson & Partners LLP			
Toronto	David Glicksman ^{1,2}	416 947 8988	<i>david.glicksman@ca.pwc.com</i>
	Elizabeth Johnson ^{1,2}	416 869 2414	<i>elizabeth.j.johnson@ca.pwc.com</i>
	Jim Wilson ^{1,2}	416 869 2988	<i>james.r.wilson@ca.pwc.com</i>
Canadian National Technical Services			
Toronto	Wally Conway ¹	416 365 2710	<i>wallace.g.conway@ca.pwc.com</i>
	Bruce Harris ¹	416 218 1403	<i>bruce.harris@ca.pwc.com</i>
	Ewald Kacnik ¹	416 869 8720	<i>ewald.r.kacnik@ca.pwc.com</i>
	Nick Pantaleo ¹	416 365 2701	<i>nick.pantaleo@ca.pwc.com</i>
	Janice Russell ¹	416 365 8810	<i>janice.russell@ca.pwc.com</i>
Winnipeg	Jeffrey Johns ¹	204 926 2435	<i>jeffrey.c.johns@ca.pwc.com</i>

1. Member of PricewaterhouseCoopers Canadian National Technical Services (CNTS). CNTS comprises a multi-disciplinary group of tax accountants, lawyers and other specialists from a variety of professional backgrounds in taxation, including government, with the mandate to enhance the overall value and scope of tax services PricewaterhouseCoopers provides to its clients.
2. Wilson & Partners LLP is a law firm affiliated with PricewaterhouseCoopers whose partners advise on a broad range of corporate tax matters including domestic and cross-border mergers & acquisitions, capital markets transactions, corporate reorganizations, financial products and structures as well as the acquisition and restructuring of income funds and REITS.

Other PricewaterhouseCoopers Contacts across Canada

Alberta			
Calgary	Dale Meister	403 509 7584	<i>dale.s.meister@ca.pwc.com</i>
Edmonton	Dan Woodruff	780 441 6810	<i>daniel.a.woodruff@ca.pwc.com</i>
British Columbia			
Vancouver	Brad Sakich	604 806 7730	<i>brad.a.sakich@ca.pwc.com</i>
Manitoba			
Winnipeg	David Loewen	204 926 2428	<i>dave.loewen@ca.pwc.com</i>
Maritimes			
Saint John/Halifax	Dean Landry	506 653 9427	<i>dean.landry@ca.pwc.com</i>
Newfoundland and Labrador			
St. John's	Allison Saunders	709 722 3883	<i>allison.j.saunders@ca.pwc.com</i>
Quebec			
	Pierre Lessard	514 205 5034	<i>pierre.lessard@ca.pwc.com</i>
Ontario			
Hamilton	Jason Safar	905 972 4118	<i>jason.safar@ca.pwc.com</i>
Mississauga	Betty Ann Jarrett	905 949 7314	<i>betty.ann.jarrett@ca.pwc.com</i>
Ottawa	Lois McCarron-Mcguire	613 755 4345	<i>lois.a.mccarron-mcguire@ca.pwc.com</i>
South Western Ontario	Loris Macor	519 985 8913	<i>loris.macor@ca.pwc.com</i>
Toronto	Brenda Humphreys	416 814 5765	<i>brenda.j.humphreys@ca.pwc.com</i>
Toronto North	Louis Provenzano	416 218 1563	<i>louis.j.provenzano@ca.pwc.com</i>
Saskatchewan			
Saskatoon	Frank Baldry	306 668 5910	<i>frank.m.baldry@ca.pwc.com</i>

Tax News Network (TNN) provides subscribers with Canadian and international information, insight and analysis to support well informed tax and business decisions. Try it today at www.ca.taxnews.com.

© 2008 PricewaterhouseCoopers LLP. All rights reserved. "PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership, or, as the context requires, the PricewaterhouseCoopers global network or other member firms of the network, each of which is a separate and independent legal entity.

This publication is intended to inform readers of developments as of the date of publication, and is neither a definitive analysis of the law nor a substitute for professional advice. Readers should discuss with professional advisers how the information may apply to their specific situations.

This publication may be displayed or printed only if for personal non-commercial use and unchanged (with all copyright and other proprietary notices retained). Unauthorized reproduction is expressly prohibited.