

Taxation Bulletin

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The Tax Information Exchange Agreement Era is Near!

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On May 21st, 2009, officials with the Department of Finance Canada announced that Canada was engaged in negotiations to conclude tax information exchange agreements (“TIEA”) with a number of countries that do not have an income tax treaty with Canada. Bermuda, Jersey, Guernsey, the Isle of Man and the Netherlands Antilles were specifically named. We understand that other unnamed countries are also negotiating a TIEA with Canada, and it is expected that the first TIEA will be signed before the end of 2009.

This announcement is significant, as dividends paid out of active business income (or on income that is deemed to be active business income) made by foreign affiliates resident in a country having a TIEA with Canada will generally be excluded from corporate income tax in Canada. Thus the Canadian parent can receive usually the dividend tax free.

Prior to the introduction of the TIEA regime, only foreign affiliates resident in a country with which Canada had a tax treaty could pay a dividend to its Canadian parent that could benefit from this exemption from Canadian income

tax. Taxpayers should consider these jurisdictions when reviewing new or existing structures.

The TIEA program was announced in *The Budget Plan 2007* to enhance Canada’s network for the sharing of tax information with countries that do not have a tax treaty with Canada. To encourage such countries to enter into a TIEA, the existing exemption for dividends received out of active business income earned by foreign affiliates resident in a treaty country will be extended to also include active business income earned by a foreign affiliate residing in a country that has a TIEA with Canada.

This announcement also has a significant effect on countries that do not have either a comprehensive income tax treaty or a TIEA with Canada. Recent Canadian legislation establishes that income earned by foreign affiliates in countries that do not have either a comprehensive income tax treaty or a TIEA would become taxable in Canada on an accrual basis even if no amount is ever paid back to the Canadian parent where, more than 60 months before that time, one of the following two conditions were fulfilled:

Vancouver

Calgary

Toronto

Ottawa

Montréal

Québec City

London

Johannesburg

(i) Canada began negotiations to enter into a TIEA, or (ii) Canada sought, by written invitation, to enter into negotiations for a TEIA with the particular country. For countries that were in the process of negotiating a TIEA with Canada at the time that the program was publicly announced, negotiations must be successfully completed before 2014.

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