



# TaxNewsFlash

Canada

## CRA Offers Additional COVID-19 Travel Restriction Relief

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Individuals affected by international travel restrictions may benefit from updated CRA filing guidance and extended relief measures. The new CRA guidance, which was released April 1, 2021, provides details for certain cross-border employees on how to properly file their 2020 Canadian income tax filings. In addition, the CRA also extends its previous administrative relief for U.S. resident employees working in Canada, and for individuals who may otherwise meet Canada's individual residency test. While the CRA's past guidance on these issues generally expired on September 30, 2020, the new guidance extends certain aspects of the previous relief.

Note that, although the new guidance documents the CRA's views on certain permanent establishment issues, it does not extend the CRA's previous guidance for permanent establishments or corporate residency, which expired on September 30, 2020. Corporate taxpayers affected beyond this date should contact the CRA, according to the guidance.

### **Background**

As a result of COVID-19, countries around the world, including Canada, imposed restrictions on travel that have disrupted normal business operations. In response, the CRA released guidance in May 2020 to provide relief for employees and businesses affected by these restrictions. This guidance generally expired on September 30, 2020.

In the guidance, the CRA advised individuals who were visiting Canada at the time when travel restrictions were imposed—and who remained in Canada solely because of these restrictions—that they would not be deemed to be resident in Canada for tax purposes solely for that reason.

The CRA also noted that it would not consider certain non-resident entities that carry on a business in Canada and reside in a jurisdiction that Canada has a tax treaty with, to have a permanent establishment in Canada only because their employees performed their employment duties in Canada solely as a result of travel restrictions. The CRA also provided similar relief for non-resident entities that resided in treaty jurisdictions in respect of potential “agency permanent establishments” and “service permanent establishments” issues arising due to travel restrictions.

At that time, the CRA further stated that U.S. residents who were present in Canada for more than 183 days solely due to travel restrictions would not have those days counted towards the 183-day test in the Canada-U.S. income tax treaty to determine whether they are taxable in Canada on their employment income. The CRA also announced then that additional relief measures for non-resident persons who sought requests to waive certain withholding requirements under Regulation 102 and 105 of the *Income Tax Act*, and for non-resident vendors who disposed of certain taxable Canadian property but who were still awaiting a Section 116 certificate. The CRA also provided guidance on corporate residency, withholding obligations for non-resident entities, residency of foreign affiliates for surplus purposes and the status of “qualifying non-resident employees, which expired on September 30, 2020. For full details on the CRA’s guidance, see *TaxNewsFlash-Canada* 2020-50, “[COVID-19 — New CRA Relief Addresses Travel Restrictions](#)” and *TaxNewsFlash-Canada* 2020-70, “[CRA Further Extends Travel Restrictions Relief](#)”.

The CRA updated its guidance to clarify its interpretation of “travel restriction” and to provide certain withholding, remittance and reporting relief to certain non-resident employers, on October 15, 2020. This additional relief, which was not subject to the September 30, 2020 expiry date, could apply until December 31, 2020 at the latest. See *TaxNewsNow*, “[CRA offers additional relief for travel restrictions](#)”.

## Cross-border employment income — Filing guidance

### *Canadian resident employees*

In its latest guidance, the CRA advises that it will provide reporting relief for Canadian-resident individuals that performed their employment duties from their home in Canada instead of at the office of their United States employer because of the travel restrictions. Specifically, the CRA states that these individuals may file their 2020 Canadian tax returns as in prior years and claim a foreign tax credit for amounts paid in the United States or file in accordance with the income sourcing rules in the Canada-United States income tax treaty, depending on the facts and circumstances.

The CRA advises that, while it will soon provide additional guidance for affected individuals’ 2021 tax years, affected individuals should expect to apply the income sourcing rules in the

Canada-U.S. income tax treaty if their working arrangements change to allow them to work permanently from Canada.

#### *Previous-year approach*

Individuals whose taxes continued to be withheld in the United States as if the income was earned in the United States, may file their 2020 Canadian tax returns as in prior years and claim a foreign tax credit for the U.S. taxes withheld, and the CRA says it will consider that individual's employment income to be sourced from the United States for 2020. The CRA advises that these individuals must maintain records to confirm the amounts paid to the United States, and report income that was not subject to withholding in the United States as if it was sourced in Canada. Further, where these individuals receive refunds of amounts paid to the United States at a later time, they must file an amended return to adjust the amount of the foreign tax credit they claimed in Canada.

#### **KPMG observations**

In its previous guidance for the relief period ending September 30, 2020, the CRA specified that a CRA letter of authority to a non-resident employer allowing them to not remit Canadian withholdings would continue to apply. As a result, a non-resident employer's withholding obligations would not change in Canada, as long as there were no changes to the withholding obligation in the other jurisdiction. The CRA's new supplemental guidance does not address whether a U.S. employer needs to have a letter of authority in place for an employee to use the "previous-year approach". The new guidance also does not specify if the relief is intended for Canadian resident employees who were forced to perform their employment duties from their home in Canada instead of at the office of a location outside of Canada other than the United States.

#### *Treaty-based approach*

Alternatively, if the previous-year approach is not available, individuals must report their employment income as sourced from Canada in accordance with the Canada-U.S. treaty's income sourcing rules. This approach will apply to individuals whose 2020 income tax withholdings were changed to reflect these sourcing rules. In this case, the CRA advises individuals to treat the following 2020 amounts as follows:

- *Income tax paid to the United States* — Individuals may claim a foreign tax credit for U.S. taxes paid related to employment income that is taxable in the United States under the Canada-U.S. income tax treaty.
- *FICA contributions* — Individuals that made valid contributions in 2020 to the United States under the Federal Insurance Contributions Act (FICA) may claim a foreign tax credit in Canada for those contributions. To claim the FICA contributions as a foreign tax credit in Canada, individuals may include the entire

amount of the individual's employment income on which the contributions were based in their 2020 foreign non-business income.

- *U.S. retirement plan contributions* — Individuals must determine the deductible amount as if they continued to exercise their employment duties in the United States throughout all of 2020, and report this amount on form RC268, "Employee Contributions to a United States Retirement Plan — Cross-Border Commuters".
- *State income tax* — Individuals that paid state income tax in 2020 may claim a foreign tax credit in Canada for those taxes. For the purpose of claiming the foreign tax credit, the foreign non-business income of the individual consists only of the portion of the employment income that the individual would have earned in the state had they continued to commute to work in the United States in 2020. Individuals that later receive a refund of state tax must file an amended return to adjust their foreign tax credit claim.

The CRA acknowledges that individuals who use the treaty-based approach may have a larger-than-usual Canadian income tax payable for 2020. The CRA says that individuals are expected to take whatever actions are reasonably necessary to obtain any applicable refund of withholdings from the United States and pay their Canadian tax liability. Where these individuals are unable to pay the full Canadian tax amount owing until after they receive a refund of U.S. withholdings, the CRA indicates that it will cancel all or part of the resulting interest or late-payment penalties that arise as a result until the individual receives their U.S. refund and pays it towards the Canadian amount owing within a reasonable time. The CRA says it will also cancel instalment penalties and interest for individuals who are notified that they must remit income tax instalments in 2021 due to this amount.

Individuals can request penalty and interest relief through CRA My Account or by filing Form RC4288, "Request for Taxpayer Relief — Cancel or Waive Penalties or Interest". These individuals must also provide a detailed description of their employment arrangement and provide a copy of their:

- Form W-2
- U.S. 1040 return
- U.S. account transcript, and
- Any other document that confirms the receipt of the U.S. refund.

#### **KPMG observations**

Individuals should be aware of potential timing issues when filing a CRA relief request. For example, individuals must wait for the IRS to process their U.S. tax filing before they can request a U.S. account transcript, and it may be several more weeks before this transcript is received. As a result, individuals should ensure they file their U.S. tax returns on time.

Further, the CRA may take additional time to process RC4288 forms, since it must examine each employment arrangement on a case-by-case basis.

### *U.S. resident employees working in Canada*

The CRA guidance also extends relief from Canadian taxation and certain Canadian compliance for United States-resident individuals who continued to exercise their employment duties in Canada because of the travel restrictions until the end of 2020. The CRA says it will not consider days that these individuals are unable to return to their country of residence, solely because of travel restrictions, to count towards the 183-day test for employment income in the Canada-U.S. income tax treaty until December 31, 2020 (previously September 30, 2020). However, according to the CRA, where individuals in this situation remain in Canada after December 31, 2020, they must include each subsequent day present in Canada in calculating whether they meet the 183-day test for 2021.

Although non-resident employers will not be required to submit a T4 slip for the 2020 taxation year for these non-resident individuals, the CRA expects these non-resident employers to track and document, among other things:

- The days during which the non-resident employee is working or present in Canada and cannot return to their country of residence, due to travel restrictions, and
- The employment income that corresponds to these days of work in Canada.

The CRA also clarifies that an employer of an individual who continues to work remotely from Canada as of January 1, 2021, must meet their Canadian withholding and remittance obligations for 2021.

#### **KPMG observations**

The new CRA guidance does not directly address employees who are resident in countries other than the United States. Therefore, it is not yet clear whether resident employees of other countries may benefit from the extension of this guidance past September 30, 2020.

### **Individual residency test relief extended**

#### *Individual Canadian income tax residence*

In its guidance, the CRA says it will extend its administrative position that it will not consider days that an individual in Canada is unable to return to their country of residence, solely because of travel restrictions, to count towards the 183-day limit for deemed individual residency for Canadian domestic tax purposes. As a result, the CRA's position

will now apply until the travel restrictions are lifted or December 31, 2021, whichever comes first (extended from September 30, 2020).

The CRA notes that an individual may still be determined to be factually resident in Canada. In particular the individual may be considered to be resident in Canada if they have a permanent home in Canada or enroll in government programs intended for Canadian residents. Further, the CRA states that its extension applies only for individuals, and does not apply to its initial relief for corporate residency, which expired September 30, 2020.

### **Permanent establishment**

In its new guidance, the CRA did not extend its previous guidance for permanent establishments, which expired on September 30, 2020. However, the CRA confirms that non-resident entities should confirm whether they are eligible for relief under an income tax treaty. The CRA has advised that, administratively, it will not consider a non-resident entity to have a permanent establishment in Canada solely because of the travel restrictions. However, the CRA cautions that it will only determine whether administrative relief is appropriate on a case-by-case basis, and its conclusions could change, such as where employees continue to exercise their employment in Canada after the travel restrictions are lifted or if there are other factors indicating a permanent establishment.

Non-resident entities who are not eligible for treaty benefits are generally required to file a return in Canada if they carry on business in Canada. However, if these entities can demonstrate to the CRA that they carry on business in Canada only due to the travel restrictions, the CRA will consider administrative relief on a case-by-case basis.

### **We can help**

Your KPMG adviser can help you assess the effect of the CRA's guidance on cross-border tax issues caused by travel restrictions put in place because of COVID-19, and provide guidance on how your business might be affected in the future. We can also keep you abreast of any tax-related changes related to COVID-19 that you'll need to consider in the days and weeks ahead. For more details, contact your KPMG adviser.

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