

Section 116 Issues on Sales of Property by Non-Residents and an Overview of Alberta ULC's

Prepared for: Legal Education Society of Alberta

For Presentation In: Edmonton, Alberta
April 12, 2007

Calgary, Alberta
April 19, 2007

For Presentation by: Edmund A. Gill
Blake, Cassels & Graydon LLP
Calgary, Alberta

Section 116 Issues on Sales of Property by Non-Residents and an Overview of Alberta ULC's

I. INTRODUCTION

The purpose of this paper is to provide non-tax practitioners with a general overview of the requirements and procedures associated with obtaining a certificate of compliance under section 116 of the *Income Tax Act* (Canada) (the "**Tax Act**")¹ in connection with the disposition of certain property by non-resident persons. The provisions of section 116 are complex and their application may vary depending on a taxpayer's individual circumstance. There are a number of good reference materials available which should be consulted when dealing with the matters discussed herein.²

This paper also provides a general overview of the nature of Alberta unlimited liability companies (both in Canada and the United States) and discusses their distinguishing characteristics.³

II. SECTION 116

A. What is the Purpose of Section 116?

Generally, non-resident persons are subject to Canadian income taxes in respect of income from sources located in Canada. In particular, subsection 2(3) of the Tax Act imposes liability for Canadian income taxes on a non-resident who was employed in Canada, carried on a business in Canada or disposed of "taxable Canadian property". However, since a non-resident person, by definition, resides outside Canada there are obvious practical difficulties associated with the collection and enforcement of payment of, taxes owing by a non-resident that are not present when dealing with a resident taxpayer. These collection and enforcement issues are typically addressed in the Tax Act by requiring withholding at the income source.

¹ All statutory references contain herein unless otherwise provided are to the relevant provisions of the Tax Act.

² For example see CRA document IC 72-17R5 – Procedures concerning the Disposition of Taxable Canadian Property by Non-Residents of Canada – Section 116; David Moffat, France Marengère and Kevin Wickstrom, "Certificate of Compliance and Waivers," *2005 British Columbia Tax Conference*, (Vancouver: Canadian Tax Foundation, 2005), 19:1-9; and Sheldon Lerman, CA, "Hot Issues in Tax Compliance", *2002 Ontario Tax Conference*, (Toronto: Canadian Tax Foundation, 2002), 16:1-61.

³ For additional information regarding unlimited liability companies please see Don R. Sommerfeldt, "Alberta Unlimited Liability Corporations: A Corporate and Tax Overview," *Report of Proceedings of Fifty-Seventh Tax Conference*, 2005 Tax Conference (Toronto: Canadian Tax Foundation, 2006), 27:1-33.

A typical source withholding provision is not a taxing provision, in that its primary function is not to impose taxes. Rather, the provision imposes a requirement on the payor to withhold, and ultimately remit to the CRA, a portion of the funds otherwise payable to a non-resident recipient as an instalment against the non-residents tax liability for the year as otherwise determined under the Tax Act. Section 116 is a typical source withholding provision that provides procedures for collecting Canadian taxes from non-residents on the disposition of certain types of property. For ease of reference the provisions of section 116 have been attached hereto as Appendix A.

B. To Whom Does Section 116 Apply?

The potential application of Section 116 should be considered by counsel in all transactions involving the disposition of property since the provisions of the section impose obligations on both a purchaser and a vendor of certain types of property.

A precondition to the application of section 116 is that the vendor is a non-resident person, for the purposes of the Tax Act, at the time the property is disposed of to the purchaser. The term "person" is broadly defined in the Tax Act to include, in addition to an individual, any corporation, tax-exempt entity and the heirs, executors, liquidators, administrators and other legal representatives of such persons.⁴ This definition includes a trust (which is considered an individual for most purposes of the Tax Act)⁵ but not a partnership. Instead, for the purposes of applying section 116, a partnership is treated as a relationship existing between two or more persons. Therefore, where there is a disposition of partnership property, the partnership is treated as a disregarded entity and each of the partners is considered to have disposed of that partner's share of the partnership property. As a result, the application of section 116 must be considered on a partner by partner basis.

The term "non-resident" is defined in the Tax Act to mean not resident in Canada.⁶ A detailed discussion of all the rules and considerations relevant to determining whether a particular person is a non-resident for the purposes of the Tax Act is beyond the scope of this paper but some

⁴ See definition in subsection 248(1).

⁵ See subsection 104(2).

⁶ See definition of Non-resident in subsection 248(1).