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Tax Filing Obligations for Non-Resident Canadian Partnerships (2019) 27:7 Canadian Tax Highlights: Canadian Tax Foundation

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A section 116 clearance certificate must be obtained by a non-resident vendor where there is a disposition of taxable Canadian property (TCP). Section 248 defines TCP as a direct interest in real or immovable property situated in Canada, and an indirect interest held through private partnerships, corporations, or trusts where more than 50 percent of the value of its units, shares, or interests was derived within the past 60 months from real or immovable property situated in Canada.

Since Canada's tax treaties are based on the OECD model treaty, gain from the disposition of TCP is taxed by Canada, and treaty relief is not provided to a non-resident. A non-resident seller that is not in possession of a section 116 clearance certificate will be subject to 25 percent withholding on the gross proceeds from the sale. The purchaser must remit the withholding to the CRA; if it doesn't, the purchaser will be liable to the CRA for this amount. A non-resident seller is exempt from withholding if it obtains a section 116 clearance certificate from the CRA prior to the sale. Security has to be posted, or the tax on the gain must be prepaid, in order to obtain the clearance certificate.

A partnership is a common vehicle used to invest in and to purchase TCP. However, the section 116 withholding provisions pose an administrative burden on such partnerships. A partnership is generally not treated as a person for the purposes of the Act. Although income and losses are computed at the partnership level, tax is imposed on its partners and not on the partnership itself. However, as previous commentators have mentioned, there are provisions in the Act under which a partnership is treated as a separate person from its partners—for example, paragraph 212(13.1)(b). It is the author's opinion that similar treatment should be extended to a widely held partnership investing in TCP by treating a partnership as a person for the purposes of section 116 and subsection 150(5).

At the 2012 IFA round table, the CRA was asked whether it would provide relief to a non-resident partner of a partnership disposing of a TCP interest, allowing it to obtain a clearance certificate at the partnership level (CRA document no. 2012-0444081C6, May 17, 2012). Relief was requested because security was provided to the CRA by the partnership in its application for a section 116 clearance certificate. The request for this relief was driven by the administrative burden on a multitiered, widely held partnership to ensure that every non-resident partner had obtained the certificate. The CRA appeared to recognize the administrative burden and cited its current policy, which is set out in paragraph 10 of IC 72-17R6. This policy relieves individual non-resident partners from having to each obtain a separate clearance certificate. The CRA will accept one notification of disposition filed on behalf of all partners by the partnership, on the condition that sufficient information about each individual partner is provided. Sufficient information consists of a complete listing of the non-resident partners, their Canadian and foreign addresses, their tax identification numbers, their ownership percentages, and their respective portion of the security. Where there is no tax identification number available, the CRA will assign a number to the partner.

For practitioners, this was a relief, but it was still unclear whether a tax-filing obligation remained for a non-resident partner. This was addressed at the recent 2019 IFA meeting in May, where the CRA was asked whether a non-resident partner in possession of a section 116 clearance certificate had an obligation to file a tax return where there were no taxes payable, owing to the prepayment of tax when the partnership applied for the certificate.

The focus of the question to the CRA was specifically with regard to paragraph 150(5)(b). Section 150 states the conditions under which a tax return does not have to be filed. A tax return does not have to be filed pursuant to subsection 150(5) where a non-resident person meets the following four conditions: (a) the taxpayer is a non-resident at that time; (b) no tax is payable under part I by the taxpayer for the taxation year; (c) the taxpayer is, at the time, not liable to pay any amount under the Act in respect of any previous taxation year; and (d) each TCP disposed of by the taxpayer in the taxation year is excluded property within the meaning assigned by subsection 116(6) or a property for which the minister has granted a clearance certificate pursuant to subsection 116 (2), (4), or (5.2). Practitioners have interpreted the possession of a section 116 clearance certificate with the prepayment of the tax to meet the requirements of subsection 150(5). See Melody Chiu, "Taxation of Non-Resident Investors in

Canadian Investment Funds," International Tax Planning feature (2010) 58:1 *Canadian Tax Journal* 117-43; and Rita Trowbridge and James Witty, "Investing in Canadian Real Estate by Non-Residents," in 2017 *Ontario Tax Conference* (Toronto: Canadian Tax Foundation, 2017), 11:1-28.

At the May IFA meeting, the CRA stated that regardless of whether the tax was prepaid and no tax would be owing on the filing of the tax return, a return nevertheless had to be filed because the requirement of paragraph 150(5)(b) is that there not be part I tax payable. The CRA's interpretation is correct. The requirement is not centred on tax payable *at the time the tax return is filed*.

From a policy perspective, it does not make sense to enforce a filing obligation on a non-resident partner of a widely held partnership where there are no taxes owing and where the CRA has the necessary information on the non-resident partner from the partnership's section 116 certificate application. To insist on an income tax filing obligation is to deter investments by non-resident partners directly into funds operating as partnerships in Canada. Given that relief is provided pursuant to an application for a section 116 certificate, similar relief could be provided at the partnership level by waiving the requirement for a partner to file an income tax return where a certificate has been issued to the partnership, or by requiring an information return at the partnership level.