Canada — TaxMatters@EY

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In this issue

TaxMatters@EY is a monthly Canadian bulletin that summarizes recent tax news, case developments, publications and more. For more information, please contact your EY advisor.

Advanced life deferred annuities: the latest tool in retirement planning

Krista Fox and Maureen De Lisser, Toronto

Retirement planning is becoming complex as Canadians are living longer than ever before. Many people are increasingly concerned about the value of their registered plans and the possibility of outliving their savings. Often, those concerned are working well past the traditional retirement age of 65 and would like to defer when they begin receiving a retirement income and paying tax on that income.

The federal government has made modest tax policy changes over the years to provide improved flexibility to individuals looking to delay the withdrawal of retirement income from their registered plans, or to reduce the taxable amount required to be withdrawn.

For example, the 2007 federal budget increased the age at which an individual must stop contributing to his or her registered retirement savings plan (RRSP) and begin receiving retirement income, from the end of the year an individual turns 69 to the end of the year an individual turns 71. In addition, in the 2015 federal budget, the government reduced the annual minimum amount required to be withdrawn from registered retirement income funds (RRIFs) in respect of individuals aged 71 to 94.

Leading up to the 2019 federal budget, there were calls by the financial industry for the government to further defer the age at which minimum withdrawals from a RRIF must begin. In response, the federal government announced in its 2019 budget the introduction of advanced life deferred annuities (ALDAs), a new type of annuity for certain registered plans. ALDAs are a retirement planning tool intended to provide greater flexibility for individuals who wish to defer the withdrawal of a portion of their retirement income until a later age by reducing the amount that is required to be withdrawn annually beginning at age 71.[1]

Current registered plan annuity rules

Under the current tax rules, individuals can use funds from certain registered plans to purchase a fixed-term annuity, a life annuity, or a joint life annuity with a spouse or common-law partner, provided certain conditions are met. A life annuity provides periodic payments to the annuitant for their life (or for the joint lives of the annuitant and their spouse or common-law partner) and payments are taxed as they are received. Currently, an annuity purchased with registered funds must begin by the end of the year in which the annuitant turns 71, and therefore is a common option on the maturity of an individual's RRSP.

Advanced life deferred annuities

Beginning in 2020, the tax rules will allow an ALDA to be a qualifying annuity purchase under RRSPs, RRIFs, deferred profit sharing plans (DPSPs), pooled registered pension plans (PRPPs) and defined contribution registered pension plans (RPPs), as well as a qualified investment for a trust governed by an RRSP or RRIF. The terms of a qualifying plan may need to be amended to permit the purchase of an ALDA under the plan.

An ALDA is a life annuity, the commencement of which can be deferred until the end of the year in which the annuitant turns 85. An ALDA's value will not be included in the calculation of the minimum amount required to be withdrawn in a year from a RRIF, PRPP or defined contribution RPP after the year in which the ALDA is purchased.

As a result, an ALDA will allow an individual to benefit from keeping their savings in a tax-sheltered investment vehicle for longer. Furthermore, depending on the person's circumstances, having retirement income spread out over a longer period of time (as a result of the ALDA reducing the annual minimum amounts to be withdrawn beginning at age 71) may result in the person being taxed at a lower marginal income tax rate, and therefore allowing them to keep more of their income on an after-tax basis. These benefits may also offer the person peace of mind, in that they will not be expected to outlive their retirement savings.

A brief summary of the proposed rules announced in the federal government's 2019 budget document is provided below. It should be noted that the government has indicated that additional rules may be introduced, as necessary, when the draft legislation for these rules is released for public comment.

Qualifications

To qualify as an ALDA under the proposed rules, the annuity contract must:

- Explicitly state its intention to qualify as an ALDA
- Provide annual or more frequent periodic payments for the life of the annuitant, or for the joint lives of the annuitant and their spouse or common-law partner, beginning no later than the end of the year the annuitant turns 85
- Provide periodic payments that are equal (except to the extent they are subject to annual adjustments reflecting CPI changes or a specified fixed rate no larger than 2% per year, or are reduced on the annuitant's death or the death of their spouse or common-law partner)
- Allow for a refund to the annuitant of any portion of premiums paid for the contract, to the extent that the premiums paid exceeded the annuitant's ALDA limit (described below)
- Provide for no other payments (e.g., commutation or cash surrender payments, or payments under a guarantee period)

Additional requirements, which are outlined under *Tax treatment of ALDA payments on death* (see below), must also be met. If these annuity contract requirements are not met, the existing rules for non-qualifying annuity purchases or non-qualified investments will apply.[2]

[1] The 2019 federal budget also introduced variable payment life annuities (VPLAs) for pooled registered pension plans and defined contribution registered pension plans. Also beginning in 2020, VPLAs will provide payments that vary based on the investment performance of the underlying annuities fund and on the mortality experience of VPLA annuitants.

[2] For example, under Part XI.01 of the *Income Tax Act*, a non-qualified investment held in an RRSP or RRIF will be subject to a 50% penalty tax (unless certain conditions are met to have the tax refunded or waived).

ALDA limits

Individuals will be subject to two ALDA limits:

- A lifetime ALDA limit in respect of a particular qualifying plan, equal to 25% of the sum of the value of all property (other than most annuities, including ALDAs) held in the qualifying plan as at the end of the previous year, and any amounts from the qualifying plan used to purchase ALDAs in previous years (this limit applies only at the time an ALDA is purchased or an additional amount is added to an existing ALDA)
- A comprehensive lifetime ALDA dollar limit of $150,000 from all qualifying plans (indexed to inflation for taxation years after 2020, rounded to the nearest $10,000).

If you purchase an ALDA contract in excess of your ALDA limit, you'll be subject to a tax of 1% per month on the excess portion. All or part of the excess tax can be waived or cancelled, however, if you can demonstrate that the portion in excess of the limit was paid as a result of a reasonable error, and the excess amount is returned to the annuitant's registered plan by the end of the year following the year in which the excess portion was paid.

Tax treatment of ALDA payments on death

In addition to the qualification criteria outlined above, to qualify as an ALDA the annuity contract must provide that:

- When an annuitant under a joint-life contract dies prior to commencement of the contract, payments to the surviving spouse or common-law partner will begin no later than the time the payments would have begun for the annuitant (provided the value of payments commencing before that time are required to be adjusted in accordance with generally accepted actuarial principles).

- Following the annuitant's death, a lump-sum death benefit[3] (if any) to a beneficiary will not exceed the premium paid for the annuity less the total of all payments received by the annuitant or, in the case of a joint-life contract, the total of all payments received by the annuitant and the annuitant's spouse or common-law partner prior to death.

Annuity payments made to a deceased annuitant's surviving spouse or common-law partner under a joint-life contract must be included in the surviving spouse's or common-law partner's income for tax purposes. Similarly, a lump-sum death benefit paid to a beneficiary who is a surviving spouse or common-law partner, or a financially dependent child or grandchild of the deceased annuitant, must also be included in the beneficiary's income for tax purposes. However, all or a portion of the lump-sum death benefit may qualify for a tax-deferred transfer (i.e., rollover) to the beneficiary's RRSP, RRIF or other qualifying registered plan. For example, to qualify for a rollover, a beneficiary who is a child or grandchild must be dependent on the deceased annuitant due to a physical or mental infirmity.

Lump-sum death benefits paid to a beneficiary who is not a surviving spouse or common-law partner, or a financially dependent child or grandchild, will be included in the income of the deceased annuitant for tax purposes in the year of death.

Conclusion

Annuities provide individuals with a predictable and guaranteed income stream, and are particularly appealing to those who have no workplace pension plan or other income source.

The introduction of ALDAs offers more flexibility in managing your retirement savings and can offer you an opportunity to keep more money in your registered plan for longer. This may be particularly beneficial if you have other sources of income during your early retirement years and you wish to defer some of your income to later years when you may be in a lower income tax bracket.

However, you need to consider this tax deferral opportunity in the context of your overall financial goals and whether an annuity will meet those goals. Such considerations include, for example, the effects of prolonged periods of low interest rates, which will result in lower annuity payments.

For more information, consult your tax advisor.

[3] In general terms, a lump-sum death benefit is a return of all or a portion of the premium paid to purchase the annuity.

How tax is transforming in the digital age

Originally published on ey.com

The digital age is changing the relationship between tax authorities and taxpayers. Learn the impact and ways to rise to the challenge.

Driven by a desire for more revenue, greater efficiency and improved compliance in an atmosphere of shrinking resources, tax authorities are increasingly relying on digital tax data gathering and analysis – using digital platforms to facilitate real-time or near-real-time collection and assessment of taxpayer data.

This move toward tax "digitalization" is allowing tax authorities to collect tax data in real time or near real time; they can then use the information to respond quickly and in more targeted ways to perceived compliance risks. Digitalization is, in some cases, allowing taxpayer information to be cross-referenced and shared among governments and agencies.

Some countries are leading the digital revolution, others are forming a second wave and still others are years away from embracing digitalization. Some Latin American countries, such as Brazil, are among the more advanced, while the United States is not as far along in its efforts.

As countries move toward digitalizing their tax administration, their efforts can often follow a similar pattern. Of course, the move to digitalization is not necessarily linear, nor should higher levels of digitalization be viewed as the ultimate goal of either taxpayers or tax authorities.

Business impact

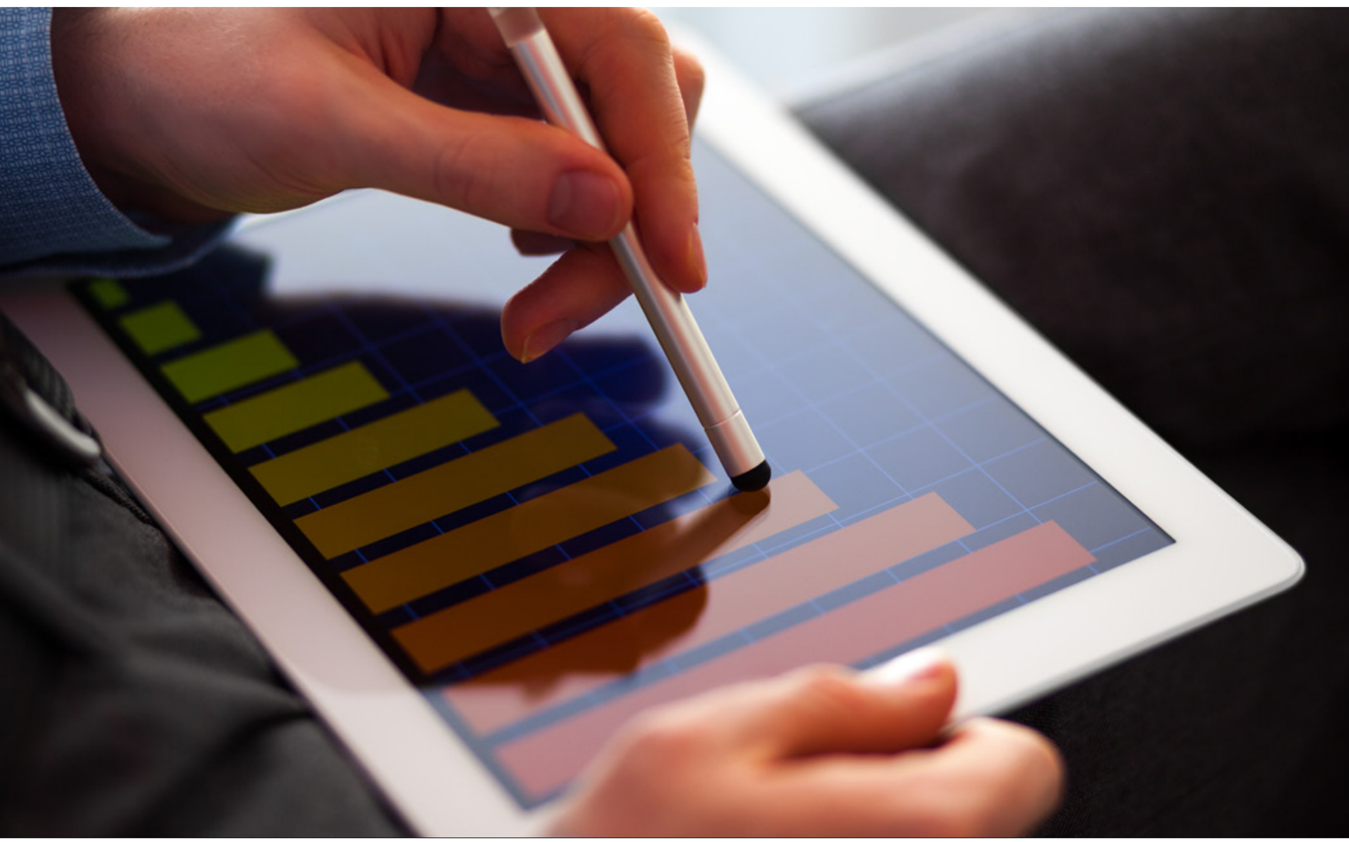
The data businesses are being asked to submit under tax digitalization reaches far beyond tax forms, and often includes accounting and sales data. Legacy systems and processes may not be able to support these and other government requirements.

Challenges may include:

- Lack of data available in the required formats
- Difficulty submitting data
- Inefficient processes for transforming data
- Lack of process support for new data requirements
- Outdated tax operating models
- More frequent need for more comprehensive analytics, in advance of submission to tax authorities
- Inability to respond to audit notices in a timely or effective manner
- Inability to respond quickly when there is disagreement with a tax assessment

A detailed review and possible re-engineering of the processes companies use to record and report their data may be required. Businesses that outsource these and related functions need to make sure that their third-party solutions are flexible and updated frequently.

Businesses will also experience a financial impact as tax administration is digitalized — more complex data requirements, delayed refunds, construction of new systems, retooling of processes and more time spent on compliance could negatively affect cash flow. Data security will also be a major concern as governments share data and BEPS reports.



Meeting the challenge

As tax authorities move at varying speeds toward greater digitalization of tax information, businesses need to develop a detailed understanding of digital tax requirements in their markets.

Following developments closely and engaging in conversations can help businesses better meet the challenges as governments expand their digital capabilities.

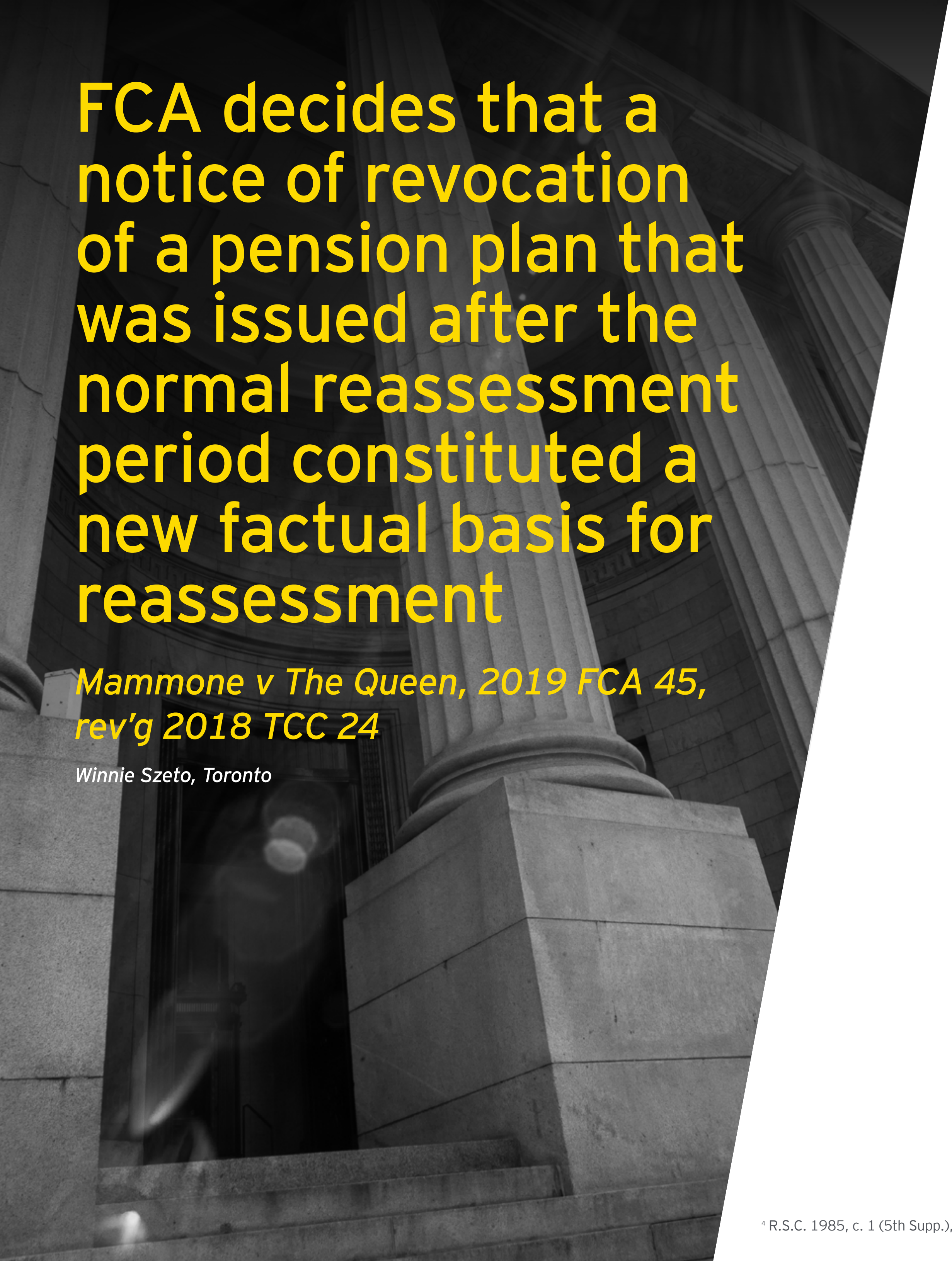
They must also determine whether their tax function is able to meet digital data and filing obligations in operating jurisdictions and is prepared to defend audits in real time or near real time.

Businesses will need to implement digital solutions that can work within and across countries and that can respond to evolving compliance and controversy requirements. They should explore the use of real-time data analytics for tax planning and compliance purposes, to measure and mitigate risk, to better target controversy interventions and to resolve issues as they occur.

Businesses should consider what investment may be needed to respond to the increasing demand for digital tax information and how to manage the risks inherent in the expansion of electronic data submission. Taking the time to understand these issues and explore forward-looking solutions today — and conveying these options to policymakers — may help avoid more costly and time-consuming remedies tomorrow.

Summary

Tax authorities are increasingly relying on digital tax data gathering and analysis, though countries are progressing at varying speeds.



FCA decides that a notice of revocation of a pension plan that was issued after the normal reassessment period constituted a new factual basis for reassessment

Mammone v The Queen, 2019 FCA 45, rev'g 2018 TCC 24

Winnie Szeto, Toronto

In this case, the Federal Court of Appeal (FCA) considered whether subsection 152(9) of the *Income Tax Act*[4] (the Act) permitted the Minister of National Revenue (the Minister) to correct a timeline error in respect of a reassessment issued after the expiry of the limitation period for reassessing under subsection 152(4) of the Act.

Facts

The taxpayer worked as a mechanic for the Toronto Fire Services from 1981 until his retirement in 2009. Throughout his employment, he was a member of a public sector pension plan.

On his retirement, the taxpayer established a new pension plan of which he was the sole member. The new plan was registered as a pension plan under the Act effective 1 January 2009.

On 23 June 2009, the taxpayer transferred the commuted value of his pension benefits under the old plan, $640,080.91, to the new plan.

In 2013, the Minister decided that the new plan did not qualify for registration as a pension plan under the Act. To revoke a pension plan's registration under section 147.1, a two-step process is required. First, the Minister must provide to the plan administrator a notice of intention to revoke, including the effective date of revocation, which may be on a retroactive basis. Second, the Minister must issue to the plan administrator an actual notice of revocation after 30 days after the day the notice of intent to revoke is mailed.

[4] R.S.C. 1985, c. 1 (5th Supp.), as amended.

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On 14 November 2013, the Minister mailed a notice of intention to revoke the new plan's registration, to be effective retroactively as of 1 January 2009.

On 12 December 2013, the Minister issued a notice of revocation, which revoked the new plan's registration effective 1 January 2009. It is important to note that the notice of revocation was issued only **28 days** after the mailing of the notice of intention to revoke.

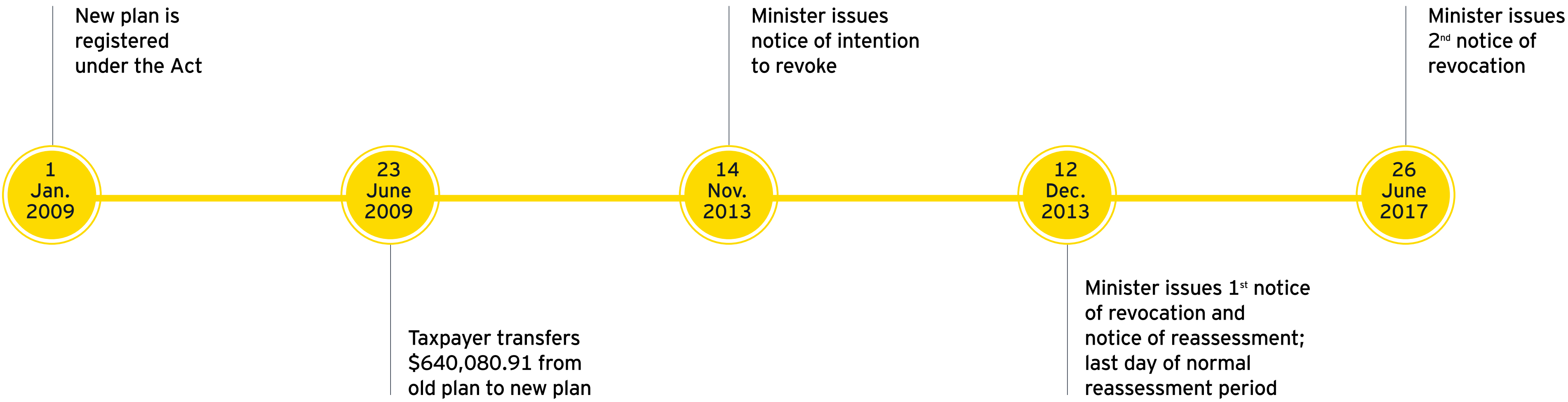
On the same day, the Minister also issued a notice of reassessment, by which the taxpayer's 2009 taxation year was reassessed to include the commuted value of the old plan in his income pursuant to paragraph 56(1)(a). The notice of reassessment was issued on the last day before the expiry of the time period that the Minister could reassess the taxpayer's 2009 taxation year.

The taxpayer pursued his rights to appeal, which included an appeal to the Tax Court of Canada (TCC) that was instituted in July 2016.

In 2017, and in the course of that appeal, the Minister realized that the notice of revocation that was sent to the taxpayer on 12 December 2013 was defective, because it was sent two days before the **30-day** requirement in the Act. In an effort to remedy that mistake, the Minister issued a second notice of revocation on 26 June 2017. The second notice stated that it superseded the earlier one, and was being issued to correct a timing error. Like the first notice, the second notice stated it would be effective retroactive to 1 January 2009.

On 22 September 2017, the Minister also amended her reply to the notice of appeal filed in the TCC to reflect the issuance of the second notice. In the amended reply, the Minister stated that she was relying on the second revocation notice for purposes of the reassessment issued on 12 December 2013.

The following is a timeline of the relevant dates in this appeal:



TCC decision

The TCC first considered whether the reassessment should be vacated, because the factual basis for the reassessment that the Minister relied on (i.e., the second notice of revocation) did not exist at the time the reassessment was issued. The TCC determined that "the facts necessary to support the reassessment did exist when the reassessment was issued because subsection 147.1(12) caused them to exist retroactively."

The TCC then considered whether the Minister's reliance on the second revocation notice was prohibited, because it was a new basis of reassessment that was raised after the limitation period had expired. The TCC determined that there was no change to the factual basis of the reassessment, because the basis for reassessment had always been that the commuted value of the old plan was transferred to a non-registered pension plan. Consequently, subsection 152(9) of the Act permitted the Minister to rely on the second revocation notice.

Based on the above, the TCC dismissed the taxpayer's appeal.

The parties' positions

The taxpayer appealed to the FCA.

At the FCA, the taxpayer argued that the factual basis for the reassessment changed in 2017 when the Minister no longer relied on the defective first revocation notice issued in 2013, and instead relied on the second revocation notice issued in 2017.

The Minister argued that the TCC made no reviewable error, and that the retroactive effect of the revocation meant that the factual basis of the reassessment did not change.

FCA decision

The FCA distinguished between the legal and factual bases for the assessment.

According to the FCA, the legal basis for the reassessment was that the amount transferred to the new plan was required to be included in the taxpayer's income because the new plan was never registered. In this regard, the FCA agreed with the lower court that the legal basis did not change over time due to the retroactive nature of the revocation.

On the other hand, the FCA determined that the factual basis underlying the reassessment did change. Initially, the reassessment was based on the first notice of revocation issued on 12 December 2013. But by 2017, this initial basis was abandoned, because the first notice of revocation was of no effect. The Minister then relied on the second notice of revocation.

According to the FCA,

> [i]t is clear from the legislative scheme [...], and subsection 147.1(13) in particular, that a revocation notice is a necessary step which must be taken to revoke a pension plan's registration. Without the notice, the new pension plan would be a "registered pension plan" that qualifies for a tax-free transfer of funds between plans. Therefore, a revocation notice was a factual element that was necessary in order to support the legal basis of the income inclusion, namely that the amount transferred from the [old plan] should be included in [the taxpayer's] income because it was transferred to an unregistered plan.
>
> In this case, the applicable revocation notice was sent in 2017, which is long after the limitation period had expired. Clearly, this was not a factual basis on which the reassessment was based when it was issued, or when the limitation period expired.

The FCA therefore concluded that the TCC made an error of mixed fact and law which attracts the palpable and overriding error standard of review,[5] and that the error made met that standard. In the FCA's view, subsection 152(9) of the Act simply could not apply to permit an out-of-time reassessment in the circumstances.

In allowing the appeal, the FCA had strong words of caution as follows:

> ...the taxpayer was entitled to rely on the expiry of the normal reassessment period to finalize his tax payable for the 2009 taxation year. In issuing the second notice of revocation, and relying on it for purposes of reassessment, the Minister was in effect seeking to do away with the limitation period.

Lessons learned

In its conclusion, the FCA stressed the importance of limitation periods. First, they promote accuracy and certainty in the adjudication of claims. Second, they provide fairness to those who might be required to defend against claims based on stale evidence. Third, they encourage those who might wish to commence claims to be diligent in pursuing them in a timely fashion. Together, these three purposes of limitation periods are known as the certainty, evidentiary and diligence rationales.[6]

In our view, this case once again confirms the importance of limitation periods and demonstrates the courts' unwillingness to permit any attempts to circumvent or frustrate this legal concept.

A word to the wise: mind your dates!

[5] See *Housen v Nikolaisen*, 2002 SCC 33, [2002] 2 SCR 235 at para. 37.
[6] *Canadian Imperial Bank of Commerce v Green*, 2015 SCC 60, at para. 57.

Publications and articles

Tax Alerts - Canada

Tax Alert 2019 No. 14 – Federal budget 2019-20 proposes changes to stock option deduction

On 19 March 2019, federal Finance Minister Bill Morneau tabled his fourth budget. The budget proposes significant changes to the tax treatment of employee stock options.

Tax Alert 2019 No. 15 - CCA acceleration measures substantively enacted as part of 2019 budget implementation bill

On 8 April 2019, Bill C-97, *Budget Implementation Act, 2019 No. 1*, which implements certain tax measures announced in the 2019 federal budget and the 21 November 2018 federal fall economic statement (as well as other previously announced measures), received first reading in the House of Commons. Bill C-97 contains the tax measures that were included in the notice of ways and means motion tabled on 4 April 2019.

As a result, the business income tax measures contained in Bill C-97 are now substantively enacted for financial reporting purposes. Most notably, the capital cost allowance (CCA) acceleration measures that were first announced in the 21 November 2018 federal fall economic statement, including some modifications since their initial release, are now substantively enacted.

Tax Alert 2019 No. 16 – Ontario budget 2019-20

Tax Alert 2019 No. 17 – CITT releases safeguard inquiry report

On 3 April 2019, the Canadian International Trade Tribunal (CITT) submitted to the Governor in Council its safeguard inquiry concerning the future importation into Canada of steel goods that have been subject to a provisional safeguard surtax since 25 October 2018.

Tax Alert 2019 No. 18 – Newfoundland and Labrador budget 2019-20

Tax Alert 2019 No. 19 – BC LOTA receives first reading

On 2 April 2019, Bill 23, the *Land Owner Transparency Act* (LOTA), received first reading in the British Columbia legislative assembly. If enacted, the LOTA would establish a registry of beneficial ownership of real property in British Columbia to be administered by the Land Title and Survey Authority. Although the LOTA is not a tax statute, the information contained in the registry it establishes would be publicly available and could be shared with tax and law enforcement officials.

Publications and articles

Publications and articles

EY's Global Capital Confidence Barometer

The 19th edition of EY's *Global Capital Confidence Barometer* describes how Canada's executives are optimistic about the strength of the Canadian and global economies but are dialing back their merger and acquisition intentions.

EY's Worldwide Personal Tax and Immigration Guide 2018-19

This guide summarizes personal tax systems and immigration rules in more than 160 jurisdictions, including Australia, Brazil, Canada, France, Germany, Mexico, the Netherlands, the Russian Federation, the UK and the US.

EY's Worldwide Capital and Fixed Assets Guide 2018

The *Worldwide Capital and Fixed Assets Guide* helps our clients navigate the rules relating to fixed assets and depreciation. It summarizes the complex rules relating to tax relief on capital expenditures in 29 jurisdictions and territories.

EY's Worldwide Estate and Inheritance Tax Guide 2018

EY's Worldwide Estate and Inheritance Tax Guide summarizes the estate tax planning systems and describes wealth transfer planning considerations in 39 jurisdictions around the world, including Australia, Canada, China, France, Germany, Italy, the Netherlands, the UK and the US.

Worldwide Corporate Tax Guide 2018

Governments worldwide continue to reform their tax codes at a historically rapid rate. Chapter by chapter, from Afghanistan to Zimbabwe, this EY guide summarizes corporate tax systems in 166 jurisdictions.

Worldwide VAT, GST and Sales Tax Guide 2018

This guide summarizes the value-added tax (VAT), goods and services tax (GST) and sales tax systems in 122 jurisdictions, including the European Union.

Worldwide R&D Incentives Reference Guide 2018

The pace at which countries are reforming their R&D incentives regimes is unprecedented. This EY guide summarizes key R&D incentives in 44 countries, and provides an overview of the European Union's Horizon 2020 program.

2017-18 Worldwide Transfer Pricing Reference Guide

The proliferation of transfer pricing rules and regulations around the world, and the huge increase in focus on the subject by the world's tax authorities, require practitioners to have knowledge of a complex web of country tax laws, regulations, rulings, methods and requirements. This guide summarizes the transfer pricing rules and regulations adopted by 119 countries and territories.

Board Matters Quarterly

The January 2019 issue of Board Matters Quarterly includes four articles from the EY Center for Board Matters. Topics include: the board's role in confronting crisis, cybersecurity disclosure benchmarking, improving board performance through effective evaluation, and today's independent board leadership landscape.

EY Trade Watch

EY Trade Watch is a quarterly communication prepared by EY's Customs & International Trade Practice. This edition includes Argentina's temporary duties on exports of services, Brazil's single-window product database and Costa Rica's draft resolution regulating inclusion of royalty payments in an import's customs value.

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The Worldwide Indirect Tax Developments Map

Updated monthly, our interactive map highlights where and when changes in VAT, global trade and excise duties are happening around the world. The map can be filtered by tax type, country and topic (e.g., VAT rate changes, compliance obligations and digital tax).

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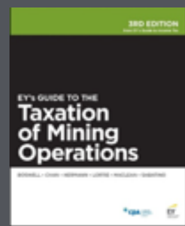


EY's Guide to the Taxation of Mining Operations

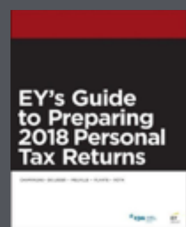
Editors: Lee Boswell, Irene Chan, Craig Hermann, André Lortie, Jim MacLean, Michael Sabatino

This guide is designed to help Canadian mining businesses interpret and apply the rules under the federal *Income Tax Act*, as well as under provincial and territorial legislation.

EY's Guide to Capital Cost Allowance, 6th Edition

Editors: Allan Bonvie, Susan Bishop, Brett Copeland, Krista Robinson

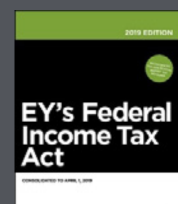
Takes you through the capital cost allowance and eligible capital expenditure rules in Canada with commentary and illustrative examples. Unique CCA lookup tables (by class and by item) are included.



EY's Guide to Preparing 2018 Personal Tax Returns

Editors: Lucie Champagne, Maureen De Lisser, Gael Melville, Yves Plante, Alan Roth

This is the line-by-line guide busy tax professionals rely on throughout the tax season. The guide includes a summary of what's new for the 2018 taxation year as well as tips, suggestions and reminders to consider when preparing 2018 personal tax returns. Available as an easy-to-use and searchable internet collection (includes access to four years of previous internet editions).



EY's Federal Income Tax Act, 2019 Edition

Editors: Albert Anelli, Warren Pashkowich and Murray Pearson

Complete coverage of Canada's *Income Tax Act* and Regulations. Included with this edition: interactive online features and purpose notes for selected provisions. Purchase of a print book includes access to an online updated and searchable copy of the federal Income Tax Act as well as the PDF eBook. This edition contains amendments and proposals from the 19 March 2019 federal budget, the 15 January 2019 proposed amendments to the *Income Tax Act* (salary overpayments) and 2018 legislation as passed and proposed.

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