

Global Tax Alert

News from EY Americas Tax

Canada Revenue Agency releases preview of revised T1134 form

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Executive summary

On 27 November 2020, the Canada Revenue Agency (CRA) released a preview of the revised Form T1134, *Information Return Relating to Controlled and Non-Controlled Foreign Affiliates*, accompanied by a notice to tax professionals.

While the revised form will be officially released and published on Canada.ca in January 2021 and is applicable to taxation years that begin after 2020, no actual legislative changes to section 233.4 of the *Income Tax Act* (the Act), the provision that establishes reporting requirements in respect of foreign affiliates, have been proposed to accompany such changes. The overhaul of the T1134 form thus stems from the CRA's policy of reviewing and updating its forms and administrative guidelines to clarify and enhance compliance requirements.

A copy of the draft revised form can be accessed [here](#).

Detailed discussion

Background

The 27 February 1995 federal budget proposed that Canadian individuals and corporations holding investments outside Canada be required to disclose additional information regarding their interests in such investments. In general terms, these requirements were intended to provide the CRA with sufficient

information regarding offshore investment made by Canadian taxpayers to determine compliance with the Canadian taxation of foreign-based income and help ensure that Canadian taxpayers pay an appropriate amount of Canadian tax on income accruing with respect to their foreign holdings.

The original T1134 form comprised two separate forms distinguishing between the reporting requirements in respect of controlled and non-controlled foreign affiliates (T1134A and T1134B). The current T1134 form combines the former T1134A and T1134B forms in a Summary form (the T1134 Summary) and Supplements (the T1134 Supplement(s)). The revised T1134 form that is due to be released in early 2021 will continue to include the T1134 Summary and the T1134 Supplements. It should be noted that taxpayers will also continue to have the option of e-filing the T1134 form.

A reporting entity is generally required to file the foreign information return annually with respect to each of its foreign affiliates. The draft legislative proposals released on 27 July 2018 following the 2018 federal budget amended subsection 233.4(4) of the Act to shorten the T1134 filing deadline from 15 months after the end of the taxpayer's taxation year (or fiscal period, if the reporting entity is a partnership) to:

- ▶ 12 months for filings related to taxation years (or fiscal periods) beginning in 2020
- ▶ 10 months for filings related to taxation years (or fiscal periods) beginning after 2020

The following provides an overview of the key changes to the reporting requirements currently applicable. The changes are described from the taxpayer's point of view and grouped into three categories: relieving changes, additional disclosure requirements and additional challenges.

Relieving changes

- ▶ **New joint filing option** - Instead of filing several sets of T1134 forms (T1134 Summary and T1134 Supplements), only one set may need to be filed for a group of reporting entities that are related to each other, that share the same taxation year-end, and that report in the same currency (Canadian dollar or functional currency).
- ▶ **Dormant/inactive foreign affiliate exemption** - The criteria to qualify for a filing exemption, including the requirement that the total cost amount to the reporting entity of the interest in all foreign affiliates must be less than CA\$100,000, has been revised to be applied at the individual legal entity level (i.e., to the interest in

the dormant/inactive foreign affiliate only). In addition, the CA\$25,000 gross receipt threshold to qualify as a dormant/inactive foreign affiliate has been increased to CA\$100,000. Although the T1134 Supplement is not required to be filed when the filing exemption conditions are met, there will be a (new) requirement to provide base-level information in respect of all dormant/inactive foreign affiliates on the T1134 Summary (in new Table D of Section 3).

- ▶ **Organizational chart** - Although in practice the CRA is generally willing to accept a detailed organizational chart for the purpose of Part I, Section 3, the CRA will make this administrative policy official by providing the reporting entities with the option of submitting a comprehensive and fully descriptive organizational chart instead of completing the organizational structure questions on the T1134 Summary (in Table C of Part I, Section 3).
- ▶ **Unconsolidated financial statements** - The requirement to provide unconsolidated financial statements for each foreign affiliate will be limited to situations where the foreign affiliate is a controlled foreign affiliate of the reporting entity or where the reporting entity owns, directly or indirectly, at least 20% of the voting shares of the foreign affiliate. However, where a reporting entity (or any member of the related Canadian group) is deemed under the "tracking arrangement" rules to own shares of a separate corporation that is a controlled foreign affiliate, unconsolidated financial statements will have to be provided in respect of each separate corporation.
- ▶ **Book cost** - The requirement to disclose the "book cost" of shares of lower-tiered affiliates in Part II, Section 2B, Question (ii) will be removed.

Additional disclosure requirements

Additional information will need to be disclosed in relation to various rules enacted since the last major revision to the form. The following summarizes highlights of certain key additional disclosure requirements, many of which may significantly increase the time and effort that may be required on the part of each reporting entity to complete the T1134 forms:

- ▶ **Gross revenue breakdown** - Not only must the gross revenue amounts, grouped into categories of traditional passive-type income sources (such as interest, dividends, rents, etc.), be reported, those amounts must be further categorized to disclose the gross revenue amounts in each category earned from arm's-length sources versus non-arm's length sources.

- **Lower-tier non-controlled foreign affiliates** - Specific information on lower-tier non-controlled foreign affiliates indirectly held through one or more non-controlled foreign affiliates will now require additional disclosure in the new Table E of Section 3 of the T1134 Summary; however, a separate T1134 Supplement will not be required to be filed in respect of these foreign affiliates.
- **Direct common and preferred share investments** - The adjusted cost base (ACB) in a directly owned foreign affiliate's shares is now required to be broken down between common share investments and preferred share investments, including changes during the year. The ACB is required to be provided for each reporting entity (or any member of the related Canadian group, if applicable) that directly owns shares in the foreign affiliate.
- **Foreign accrual property income (FAPI), foreign accrual property losses (FAPL) and foreign accrual capital losses (FACL)** - More detailed disclosure around FAPI, FAPL and FACL for controlled foreign affiliates is required in the revised T1134 form. In previous versions of the T1134 form, disclosure was only required on FAPI for the year; therefore, if a controlled foreign affiliate incurred a net FAPI loss for the year, no additional disclosure in respect of FAPI was required. The revised T1134 form now requires disclosure of various forms of FAPI for the year, regardless of whether net FAPI is nil, as well as details of any FAPL and FACL, and FAPI/FAPL/FACL information in respect of each of the members of the related Canadian group (in the case of a group filing).
- **Foreign affiliate dumping (FAD) rules** - If the reporting entity or any member of the related Canadian group (where applicable) was involved in a transaction(s) to which the FAD rules apply, additional disclosure is required with respect to the specific provisions of section 212.3 of the Act, including confirmation of whether a pertinent loan or indebtedness (PLOI) election has been made under subsection 212.3(11) of the Act.
- **Upstream loans** - Details relating to any upstream loans owed by a "specified debtor" (as defined in subsection 90(15) of the Act) in respect of the reporting entity or any member of the related Canadian group (if applicable) to a foreign affiliate are required to be disclosed.
- **Tracking arrangement rules** - As introduced in the 2018 federal budget, the tracking arrangement rules were aimed at preventing the avoidance of accrual-based taxation of FAPI. If the reporting entity or a member of the related

Canadian group, where applicable, holds a "tracking interest" (as defined in subsection 95(8) of the Act) in respect of a foreign affiliate, additional disclosures are required.

- **Surplus accounts and reorganizations** - A detailed section relating to the surplus accounts and share transactions of controlled foreign affiliates is required to be completed as part of the revised T1134 form. This section includes the requirement of disclosure of any transactions entered into during the year to which section 51 - *Convertible property*, subsection 88(3) - *Liquidation and dissolution of foreign affiliate*, or paragraphs 95(2)(c) to (e) in respect of foreign affiliate reorganization transactions, the stub-period FAPI rules or relevant cost base elections apply.

Additional challenges

More disclosure around the number of employees

In Section 1 of Part III, the revised T1134 form now asks for more detail in respect of the number of full-time employees or employee equivalents (as defined in subparagraphs (c)(i) and (ii) of the "investment business" definition in subsection 95(1) of the Act) employed by the foreign affiliate throughout the year.

While it no longer requires the breakdown of employees on a business-by-business basis, it now has four more categories, requiring selection of one of the following options:

- i. 0 employees
- ii. 1 to 5 employees
- iii. 6 to 15 employees
- iv. 16 to 25 employees
- v. 26 to 100 employees
- vi. 100+ employees

There is also an additional question confirming whether the foreign affiliate or the partnership of which the foreign affiliate is a qualifying member relied on the services of the qualifying employer (i.e., a corporation related to the foreign affiliate, a designated corporation or a designated partnership).

As the definition of "investment business" solely captures those businesses that do not have more than five employees, it is unclear what the relevance of having options for anything other than (i) fewer than five employees and (ii) more than five employees in this case. No other FAPI

or surplus rules test the number of employees employed by the foreign affiliate. It is not clear how the CRA will view those taxpayers that select zero employees. If these foreign affiliates are automatically flagged, this could mean higher risk of audit for holding companies and those entities with a low number of employees.

Which members of the “related Canadian group”?

Practitioners/taxpayers will undoubtedly need to pay close attention to the disclosures for each of the members of the related group in each of the sections in the case of this elective group filing option, particularly as each reporting entity remains responsible for providing the correct information on, and timely filing of, each information return.

Where the reporting entity is completing the revised form on behalf of a related Canadian group, additional information/disclosures are to be included:

1. Requirements (i) to (iv) of Part I, Section 3 - for the organizational structure.
2. Requirement D of Part II, Section 1 - disclosures of the transactions to which the FAD rules apply (which is only required for members of the related group that are Canadians resident in Canada).
3. Requirement (iii) of Part III, Section 3 - for the FAPI information of the affiliate (this should only be applicable for those members with participating percentages in the foreign affiliate).
4. Requirement B, Part II, Section 3 - for the surplus accounts of the foreign affiliate (this should only be applicable for the members that must maintain summary calculations of the various surplus accounts of the foreign affiliate).

Disclosures of details pertaining to complex transactions

As described earlier, the revised form now requires disclosures of transactions to which various complex rules may apply, including the FAD rules, the upstream loan rules, tracking arrangement rules, and the various internal reorganization provisions. The complexity of the questions asked and the level of detail required will surely pose challenges for even the most experienced tax professionals and may make the automation of the preparation of certain sections of the form impractical.

As noted above, any FAPI amounts and upstream loans that taxpayers have are now reportable on the revised form in significant detail. Where taxpayers have previously taken a practical approach and chosen to report only net FAPI or the upstream loan amounts not covered by various deductions under section 90 (e.g., the downstream surplus of underlying foreign affiliates), additional details will now be made available to the CRA, which may be used as part of their audit assessments related to prior years as well as future years.

Filing deadline

With the revised T1134 form and the added complexity and detailed information/disclosures required, taxpayers and tax practitioners will face significant challenges in compiling all of the necessary information in the already-shortened time frame. With the various COVID-19 relief programs provided by tax authorities in many foreign jurisdictions in the past year, this has meant many foreign tax filings were completed later than usual and may mean more delays for taxpayers and practitioners in gathering the requisite information for the FY2021 T1134 form filings.

Implications

As stated in the Notice to Tax Professionals, the purported objective of the proposed changes to the T1134 information return is to balance the CRA's needs and requirements to use the T1134 for audit risk assessment purposes and to address taxpayers' concerns on compliance burden. The changes to the T1134 form thus attempt to take into account the latest legislative amendments enacted in respect of the foreign affiliate regime and target areas that may be of particular audit concern for the CRA while also reducing redundant information.

However, as outlined above, the changes appear to trend toward requiring greater disclosure of foreign affiliate information for the purposes of the CRA's audit assessment requirements more so than they do toward reducing cost, time and efforts for taxpayers to comply. Additional information and disclosures in the revised T1134 form will require taxpayers to devote more resources to meeting their compliance obligations.

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