Technical Amendments, Implementation of Tax Law Changes and Retroactive Tax Legislation

Issue

In 2009, the Auditor General of Canada looked at how the Department of Finance develops legislative amendments to address technical deficiencies in the *Income Tax Act* to more clearly convey the intent of the legislation or to make it easier for taxpayers to comply.

The Auditor General discovered that the Department of Finance has a backlog of some 400 technical amendments[1]—a backlog that continued to grow in the years that followed. It recommended that the government regularly develop and release draft technical amendments so that taxpayers and tax practitioners know what changes will be made and can provide input to the Department. Thus, any concerns they may have can be considered before a bill is tabled in Parliament.

It is important that technical amendments to the *Income Tax Act,* or legislative amendments that involve changes in tax policy, are set forth in proposed legislation in a timely fashion. Announcing proposed amendments and not enacting them within a reasonable short period creates uncertainty and makes it difficult for individuals and businesses to plan their affairs.

Background

One situation where technical amendments were necessary was to clarify the taxation of income arising from non-competition agreements.[2] In response to court decisions, the Minister of Finance issued a press release in October 2003 announcing the government's intention to propose amendments to the *Income Tax Act* that would generally treat payments received in consideration for the non-competition covenants as ordinary income for tax purposes (or in some important exceptions, as a capital gain).

In February 2004, the Department of Finance released draft legislation. A number of organization expressed concerns with the draft legislation, including the Joint Committee on Taxation of the Canadian Bar Association and the Canadian Institute of Chartered Accountants ("Joint Committee") which noted the proposed legislation was "significantly broader" than the Department of Finance originally described in its press release.

On July 18, 2005, the Department of Finance released a second round of amendments to the draft legislation. The Joint Committee reiterated many of its previous concerns and expressed additional concerns with respect to the redrafted legislation.

On November 9, 2006 the Department of Finance released a third set of amendments after making some minor changes. The proposed amendments were tabled in Parliament in Bill C-33 which died on the order paper when Parliament prorogued on September 14, 2007, and then in Bill C-10 (November 2007) when the next session of Parliament began sitting. Bill C-10 eventually died on the Senate floor in September 2008 when a federal election was called.

On October 24, 2012, the Minister of Finance released a detailed (close to a 1,000 page) Notice of Ways and Means Motion to implement a significant backlog of outstanding technical amendments, including those pertaining to non-competition agreements. These were contained in Bill C-48 which received Royal Assent on June 26, 2013. The scope of the newly enacted provisions extends well beyond non-competition payments made to a vendor of corporate shares and generally applies retroactively to amounts received or receivable after October 7, 2003, subject to certain limited exceptions.

[1] Technical amendments are changes made to correct anomalies that arise after the original measure was passed and to correct consequences that were not intended. These amendments are not intended to introduce new tax policy or change existing tax policy.

[2] When a taxpayer sells a business, part of the selling price may be linked to an agreement by the seller to not compete with the business carried on by the buyer. This type of agreement is referred to as a non-compete agreement, or restrictive covenant. It was commonly understood, and interpreted by the Canada Revenue Agency, that amounts received by a vendor in respect of a restrictive covenant on the sale of shares of a corporation were taxable. However, court decisions in 2000 and 2003 ruled that these amounts were generally not taxable.

The Canadian Chamber strongly urges the federal government to draw on the experience and advice of non-government experts to influence policy and assist in the development of legislation. Private-sector experts can provide policy makers and legislators with the knowledge required to understand how a policy or legislative change will impact business and the broader economy. Consulting prior to the development of legislation could avoid the overreaching, over-the-top, and unnecessarily complex response we saw with respect to the non-competition agreements. To its credit, Finance Canada has been trying recently to consult prior to going ahead and changing tax law—for example, with respect to treaty shopping changes and testamentary trust changes.

Additionally, the government should clarify its rationale for changing tax laws on a retroactive basis. The government has stated in the past that "retroactive clarifying amendments should only be made in exceptional circumstances". Due to the general nature of the government's rationale; however, it is open to interpretation which only serves to escalate the level of uncertainty regarding tax law. By allowing the least possible margin of different interpretations, taxpayers will have a higher degree of certainty about the effect of tax law. An atmosphere of mutual trust and confidence between business and government will promote the efficient, effective and equitable operation of the tax system.

Recommendations

That the federal government:

1. Provided that sufficient consultation has taken place, make announcements with respect to changes in tax law only if it intends to introduce enabling legislation within 6 months.
2. If the legislation is not issued until later, then make the change(s) effective at the later date and not the date on which the original announcement was made.
3. Clearly specify its rationale for adopting retroactive amendments to tax legislation. Define what constitutes "clarifying amendments" and "exceptional circumstances."
4. Actively expand opportunities to draw on the experience and advice of non-government experts from law, accounting firms and industry to assist in the development of legislation when either the government identifies a problem or the tax community identifies a problem. Where required, confidentiality agreements could be considered to ensure that the advice being sought and provided is treated with the level of sensitivity required.

SUBMITTED BY THE FORT SASKATCHEWAN & DISTRICT CHAMBER OF COMMERCE, CO-SPONSORED BY THE EDMONTON CHAMBER OF COMMERCE AND TAXATION COMMITTEE

Resolution 2011 falling off the book "Implementation of Tax Law Changes and Retroactive Tax Legislation".