

Implementation of Tax Law Changes and Retroactive Tax Legislation

Implementation of tax legislation within a reasonable period of time and the certainty that government will not change tax rules retroactively to increase the tax burden are of paramount importance to business planning.

There are a number of examples where the federal government has announced changes to tax law without implementing legislation within a reasonable period of time and/or enacted changes retroactively. One example pertains to the taxation of non-resident trusts and foreign investment entities.

Proposed changes affecting the taxation of non-resident trusts and foreign investment entities were contained in the 1999 federal budget. On November 30, 1999, the Finance Minister announced a number of revisions to the proposals. On June 22, 2000, the Department of Finance released initial draft legislation and invited the public to submit comments by September 1, 2000. On September 7, 2000, the Finance Minister announced that the period of consultation on draft legislation would be extended to December 31, 2000 and that the implementation date will be delayed by one year, to taxation years beginning after 2001.

On August 2, 2001, the Department of Finance released a revised draft reflecting comments received by the Department. On October 11, 2002, a third draft of the legislation was released as a *Notice of Ways and Means Motion*. On October 30, 2003, a fourth draft of the legislation was released as a *Detailed Notice of Ways and Means Motion* and stated that “generally, the proposals would take effect for taxation years that begin after 2002”.

On July 18, 2005, Finance Canada released revised legislative proposals – based on the Motion tabled in 2003 and reflecting comments received by Finance since that time – to provide guidance to taxpayers in anticipation of the amendments to be tabled in Parliament in the fall of 2005.

On January 1, 2006, Finance released a *Notice of Ways and Means Motion* which included changes to the taxation of income from foreign investment entities and non-resident trusts. Legislation (Bill C-33) was tabled in Parliament on November 9, 2006. Bill C-33 passed third reading in the House of Commons on June 15, 2007. When Parliament prorogued on September 14, 2007, Bill C-33 died on the order paper. It was re-introduced as Bill C-10 in November 2007 when the next session of Parliament began sitting. The legislation included in Bill C-10 – *Income Tax Amendments Act, 2006* – would generally apply to tax years that begin after 2006, instead of for taxation years that begin after 2002. However, provisions have been made to allow taxpayers to elect an earlier application of the rules as far back as their first tax year beginning after 2002 (or for certain non-resident trust, beginning after 2000). Bill C-10 passed all the stages in the House of Commons on October 29, 2007 and received second reading in the Senate on December 4, 2007. The Bill is currently being held up by the Senate Committee on Banking, Trade and Commerce pending further hearings on a number of aspects of the non-resident trust provisions.

The announcement of tax rule changes with no legislation makes it difficult for individuals and businesses to plan their affairs when they have no assurance as to what form the law will take, whether it will be implemented and how it will apply. The government must refrain from making announcements with respect to changes in tax law if it does not intend to introduce legislation within six months.

The government must also 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, corporations 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. Assuming that sufficient consultation has taken place, make announcements with respect to changes in tax law only if it proposes to introduce enabling legislation within 6 months, and 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.
2. Clearly specify its rationale for adopting retroactive amendments to tax legislation. Define what constitutes “clarifying amendments” and “exceptional circumstances”.