



New rules may tax international employee benefit trusts

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International employee benefit trusts (EBTs) that hold assets for Canadian resident employees may be subject to tax in Canada under the recently [amended](#) non-resident trust rules (NRT Rules). A single employee in Canada could create Canadian tax obligations for the trust. The 31 March 2014 deadline for filing tax returns in relation to an EBT's 2013 taxation has passed. The next filing due date is in June 2014 for an EBT's 2007-2012 taxation years.

An EBT can elect to be taxed on income (and gains) on assets generally held for Canadian employees. However, if the election is not made on time, the entire trust fund (including assets held for non-residents) could become subject to tax in Canada. In a second election, a Canadian employer can elect to transfer the trust's tax liability to itself, which would reduce the applicable tax rate to Canadian corporate rates. The trustee, the Canadian employer and Canadian beneficiaries of foreign EBTs may also be required to file information returns in Canada with respect to the trust. The applicability of the NRT Rules and the deadlines for filing these elections and the tax and information returns should be reviewed based on the facts of each case.

Background

The NRT Rules apply to a foreign trust if either (i) a Canada resident has made a "contribution" (broadly defined) to the trust (the "resident contributor" test), or (ii) a trust has a Canadian resident beneficiary and a "connected contributor" (the "resident beneficiary" test). If the trust meets one of these two tests at the end of a taxation (i.e., calendar) year, the trust is deemed resident in Canada throughout that year and taxable in Canada on its worldwide income subject to the elections noted above. There are exemptions for trusts that qualify as an "exempt foreign trust". The amended NRT Rules came into force in June 2013 and generally apply retroactively from 1 January 2007.

As noted, contributions are widely defined. For example, a Canadian subsidiary in a multinational group is deemed to contribute property to a non-resident trust where a person (e.g., its foreign parent) transfers property (no matter its value) to the trust and a purpose or effect of the transfer may reasonably be considered to provide benefits in respect of services rendered by a person as an employee of the Canadian subsidiary or affiliate.

What types of trusts are caught?

Trusts that may be caught by the NRT Rules include:

1. ESOPs (employee share ownership plans), ESPPs (employee share purchase plans), Employee Benefit Trusts for deferred income, saving or health plans, cash or equity based, short or long term incentives, with or without sub-funds or classes of units;
2. Pension Trusts holding assets of pension, retirement, termination of service, disability or death plans, whether or not registered;
3. Trusts for funding or securing Supplemental Executive Retirement Plans (SERP);
4. Trusts for Individual Pension Plans (i.e. only one individual as plan member); and
5. Trusts holding assets as security of an obligation, for example an environmental trust.

Other types of trusts that may be caught include employee life and health trusts, employee trusts, health & welfare trusts, insurance segregated fund trusts, lifetime benefit trusts, master trusts, real estate investment trusts or unit trusts.

Exempt foreign trusts

Some EBTs that are trusts governed by an “employees profit sharing plan”, a “retirement compensation arrangement” or a “foreign retirement arrangement” may qualify as an exempt foreign trust not subject to NRT Rules. However, these exemptions are unlikely to be available to an EBT holding assets of:

- (a) foreign benefit plans in which long-term Canadian residents participate; or
- (b) foreign pension plans established in a jurisdiction that does not impose tax.

Accordingly, trustees of international EBTs with Canadian resident beneficiaries should take advice on the implications of the NRT Rules for the trust, the Canadian employer and beneficiaries in Canada.

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