CRA updates to COVID-19 relief guidelines and travel restrictions

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On April 1, 2021, the Canada Revenue Agency (CRA) updated its guidance and administrative relief relating to the impact of COVID-19 travel restrictions on residency and permanent establishment determinations.

Impact for individuals

Residency

An individual's tax residence is determined based on a factual assessment of their ties to Canada. Additionally, if an individual is physically present in Canada for 183 days or more during a tax year, the individual will be deemed a resident in Canada for the year. Where ordinarily non-resident individuals were in Canada at a time when travel restrictions were imposed and such restrictions prevented them from returning to their jurisdiction of residence, the CRA announced that they would not consider the individuals residents in Canada if the reason for their continued presence were solely due to travel restrictions. Further, the days of presence in Canada due to travel restrictions would not count towards the 183-day limit. Initially, the relief was to apply for the period from March 16, 2020 to September 30, 2020. The CRA has extended the relief period to the earlier of the lifting of travel restrictions and December 31, 2021. It is important to note an individual may still be considered to be a Canadian resident where other indicators of residency, such as having a permanent home in Canada or enrolling in government programs intended for Canadian residents, are present.

Cross-Border employment

Non-resident employees working in Canada

The CRA has provided relief for employees who are normally residents in the U.S., however, are working remotely from Canada. The time they spend in Canada due to travel restrictions will not be counted towards the 183-day test for employment in Canada under the Canada-US tax treaty. The CRA announced that this relief extends to Dec. 30, 2020. After that time, the 183-day test under the treaty will apply.

Where an employee works in Canada, the employer is subject to Canadian withholding and remitting obligations, unless these are waived by the CRA. The CRA had previously confirmed that it would not assess or penalize an employer for failing to withhold or remit as required in respect of a non-Canadian resident employee, if the conditions listed below are satisfied. The CRA has extended this relief to Dec. 30, 2020 and relieved the employer from their obligation of issuing a T4 slip for the 2020 tax year; provided the employer documents the days during which the employee was working while present in Canada due to travel restrictions and the income that corresponds to those days. The conditions are:

1. The non-resident employee is resident in a country with which Canada has a comprehensive tax treaty (the treaty);
2. The non-resident employee is not a resident in Canada for tax purposes in accordance with the relevant treaty;
3. The remuneration received by the non-resident employee for performing their duties of employment in Canada would otherwise be exempt from taxation in Canada in accordance with the relevant treaty;
4. The non-resident employee regularly and customarily performs their duties of employment outside of Canada and has not previously performed duties of employment in Canada, as a non-resident of Canada, for any employer;
5. There is no employer-employee relationship between the non-resident employee and any employer in Canada;
6. There has been no significant change to: the non-resident employee's duties of employment (other than working remotely) while working in Canada; or the employer-employee relationship that existed between the non-resident employer and the non-resident employee at the time the non-resident employee travelled to Canada; and
7. The non-resident employee travelled to Canada due to the COVID-19 crisis or for reasons not relating in any manner whatever to their employment, and could not return to their jurisdiction of residence solely due to COVID-19 travel restrictions.

Canadian resident employees working in the U.S.

In the instance a Canadian resident employee works in a foreign jurisdiction for a non-resident employer, the CRA may issue a "letter of authority" authorising the non-resident employer to reduce Canadian deductions at source to account for foreign taxes payable; which would generally be creditable against the employee's Canadian tax liability by a foreign tax credit. If the Canadian resident employee is forced to perform the work in Canada instead of at the employer's foreign office due to travel restrictions, the CRA had previously announced that the letter of authority would continue to apply for the period between March 16, 2020 and Sept. 30, 2020 provided there are no changes to the withholding obligations in the foreign jurisdiction.

By virtue of the application of the Canada-US tax treaty, Canadian resident employees who normally work for their U.S. employer in the U.S. may be subject to more Canadian tax and less U.S. tax on the employment income. To address this, the CRA has announced two options:

1. To simplify reporting, the CRA will administratively accept that the employment income from the U.S. employer paid to Canadian residents forced to work remotely in Canada because of travel restrictions is sourced in the U.S. for the

2020 tax year. Under this method, employees would file as they have in previous years. Employees will need to keep records of the taxes paid to the U.S. and file an adjustment to the extent they receive a U.S. tax refund.

2. Alternatively, employees can elect to file in 2020 based upon the tax treaty sourcing rules (which would source the income in Canada). Employees whose tax withholding was adjusted in 2020 to take into account the treaty sourcing rules are required to file on this basis. The CRA has provided additional guidance on the treatment and availability of foreign tax credits (including permitting a credit where US State taxes are not refunded), social security remittances, as well as U.S. retirement plan contributions. Employees are required to apply for all applicable U.S. tax refunds and pay the Canadian tax due, and may be subject to 2021 instalment obligations. In such cases, interest and late payment penalties will be cancelled in certain circumstances.

Further guidance will be released for 2021, however, where employees work permanently from Canada, the CRA notes that the income sourcing rules in the tax treaty would apply.

The CRA also issued several examples of how these administrative concessions apply to different cross-border employment working arrangements.

Impact on corporations

Residency

Where directors of a corporation are physically present in Canada and unable to travel to another jurisdiction to attend meetings, there is a possibility that the corporation could be considered resident in Canada. Where the corporation is also resident in a jurisdiction with which Canada has a tax treaty, often the tax treaty itself will address the issue. Where the tax treaty does not address the issue (by providing the corporate residence is determined based upon the “effective place of management”), the CRA will not consider the corporation to be resident in Canada solely because the director participates in a board meeting from Canada due solely to travel restrictions. Where Canada does not have a tax treaty with the other jurisdiction, the determination is made on a case-by-case basis. The CRA applies this approach to foreign entities, which are considered corporations under Canadian income tax law and to commercial trusts as well as to the calculation of surplus of a foreign affiliate of a Canadian corporation. This administrative relief has not been extended beyond September 30, 2020.

Permanent establishment

A permanent establishment can arise when an employee or agent performs certain duties in Canada on behalf of the non-resident. The CRA provided administrative relief during the period from March 16, 2020 to September 30, 2020. Although the CRA has not extended this relief, it has clarified its position in circumstances where a tax treaty applies. The CRA would generally not consider a home office or other workspace to constitute a fixed place of business in Canada unless there is a semblance of permanence to the site and the site is at the “disposal” of the employer. An individual working from their home or short-term residence in Canada while travel restrictions remain in place would not generally be sufficient to constitute a permanent

establishment. The CRA notes that after travel restrictions are lifted, the position could change if the employee continues working remotely and the site is at the disposal of the employer.

A permanent establishment can also arise where an employee has the right to conclude contracts on behalf of the employer and habitually exercises that right in Canada. The CRA confirmed that this requirement would not be met where the individual concludes contracts in Canada solely because of travel restrictions.

For more information on the new guidelines and travel restrictions, please reach out to one of the key contacts below.

By

Pamela L. Cross

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BLG Offices

Calgary

Centennial Place, East Tower
520 3rd Avenue S.W.
Calgary, AB, Canada
T2P 0R3

T 403.232.9500
F 403.266.1395

Ottawa

World Exchange Plaza
100 Queen Street
Ottawa, ON, Canada
K1P 1J9

T 613.237.5160
F 613.230.8842

Vancouver

1200 Waterfront Centre
200 Burrard Street
Vancouver, BC, Canada
V7X 1T2

T 604.687.5744
F 604.687.1415

Montréal

1000 De La Gauchetière Street West
Suite 900
Montréal, QC, Canada
H3B 5H4

T 514.954.2555
F 514.879.9015

Toronto

Bay Adelaide Centre, East Tower
22 Adelaide Street West
Toronto, ON, Canada
M5H 4E3

T 416.367.6000
F 416.367.6749

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