

Eligibility for Foreign Tax Credits

Author : admin

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Eligibility for Foreign Tax Credits

Arsove v The Queen, [2016 TCC 172](#)

At issue was whether the taxpayer, who filed both Canadian and US tax returns by reason of being a Canadian resident and US citizen, was entitled to claim a foreign tax credit in respect of Canadian sources income.

ANALYSIS

[Income Tax Act](#) section 126 permits a foreign tax deduction in certain circumstances when calculating Canadian tax payable. Specifically, subsection 126(1) allows a deduction from TAX otherwise payable (not income) for part of any non-business-income tax paid by the taxpayer, for that year, to the government of a country other than Canada.

Subsection 126(7) defines "non-business-income tax" for purposes of section 126 as an amount actually paid for a taxation year to the government of a country other than Canada that is the portion of any income or profit tax so paid that:

- was not included in computing that taxpayers business-income tax for the year in respect of any business carried on by the taxpayer in any country other than Canada;
- that was not deductible (whether deducted or not) pursuant to subsection 20(11);
- that was not deducted pursuant to subsection 20(12); and
- does not include a tax or a portion thereof that fits under paragraphs (c.1) to (i).

The Court also referred to the [Canada-US Income Tax Convention](#) which provides specific rules for taxpayers who are citizens of the US and residents of Canada.

Here the taxpayer, in her US tax return calculated US tax but this was reduced to nil after deduction of a foreign tax credit and she was also refunded income tax that was withheld on a distribution (paras 6-7). She filed her US tax return as if she had filed tax on the income in Canada.

The Court noted that if she would have paid tax to the US government, then she would have been entitled to a foreign tax credit up to the amount of tax so paid (para 13). Where, however, not tax is payable in the US or paid in the US, it follows (one would think logically) that no tax

credit would be available in Canada. The tax payable is not the tax that is calculated as due but rather the amount that, by operation of US tax legislation, is ultimately imposed on a taxpayer - *Zhang v. The Queen*, [2007 TCC 634](#), aff'd [2008 FCA 198](#).

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