Paying Wages: Can CRA Collect Unpaid Remittances from a Related Company?



Employers are responsible for withholding and remitting source deductions on payments to their employees. This straightforward principle becomes tricky to apply when the employer is a complex corporate structure made up of multiple legal entities. Controversy over which entity is liable to deduct and remit source deductions to the CRA may arise when labour is shared among the group and the employer of record struggles while the others prosper. The CRA might seek to shift employer status to one of the other entities or principal of the group and assess it for the unpaid remittances. The following cases illustrate the factors that determine whether such assessments are legitimate.

NO SHIFTING EMPLOYER STATUS

SITUATION

A Newfoundland employer establishes 3 legal entities to house its separate business activities: logging, precision machining and metal working. Initially, the logging company is the employer of record for all employees. When logging company employees cross over and work for one of the other 2 entities, the logging company charges the other entity with the labour cost for the work. In 2002, the logging company runs into financial difficulty and is in arrears in CRA source deduction remittances. As a result, all crossover employees are transferred to the machining or metal working entity and the logging company retains employer status over only the employees who work solely in logging. The logging company still uses the crossover employees but now the billing arrangement is reversed and the logging company is charged by the other entity for the crossover employee’s labour. The CRA treats the machining and metal working companies as the employer and assesses them for the arrears on source deductions for payments to employees prior to 2002. The companies appeal.

DECISION

The Tax Court allows the appeals and squashes the assessments.

EXPLANATION

The CRA Collections Division had conducted a payroll audit of the 3 companies to determine which was responsible for the source deduction arrears from before 2002. But, the court noted, the CRA employees who did the audits didn’t actually look at

the employment agreements but relied almost entirely on a short verbal description of each employee's job duties. As a result, the Tax Court concluded that the payroll audits produced no evidence that the employment arrangements were not as the logging company had reported them before 2002 and how all 3 of the other companies described them after that date. So it found no basis for ruling that the machining and metal working companies were the employers responsible for source deductions on crossover employees prior to 2002.

Central Springs Ltd. v. Canada, [2010] TCC 543 (CanLII)

OK TO SHIFT EMPLOYER STATUS

SITUATION

A man and his wife create a group of high tech corporations made up of 5 related entities. Technology Equity Corporation (TEC) is the parent and sole shareholder of the other 4, each of which carries out separate business activities. One of these 4 other companies, LAN Technologies Inc. (LAN), is designated as the employer for the group. LAN charges the others for the use of any of its employees. Up to 1986, payroll is made out of a LAN bank account. But in 1987, the group's bank insists that all cheques be issued in the name of and from the account of the holding company, TEC. In 1988, TEC a payroll audit is conducted and TEC is assessed $82,500 in source deductions. TEC is unable to pay. So CRA assesses the founder in his role as director of the company. The founder appeals.

DECISION

The Tax Court denies the appeal and upholds the assessment against the founder.

EXPLANATION

Despite the founder's intentions, the Tax Court found that from 1987, payroll cheques had been issued to group employees by TEC, rather than LAN. Although LAN may have been the employer of record, it was TEC that had, in fact, paid their wages. Since the requirement to deduct at source is imposed on the person who actually pays employees their wages, CRA was right to assess TEC for the unpaid source deductions. And as an inside director, the group founder couldn't escape the liability for TEC's failure to remit the source deductions owing to the CRA.