

## LEGISLATIVE PROPOSALS RELATING TO INCOME TAX

### INCOME TAX ACT

**1. (1) Subsection 90(8) of the *Income Tax Act* is amended by striking out “and” at the end of paragraph (b), by adding “and” at the end of paragraph (c) and by adding the following after paragraph (c):**

(d) subject to subsection (8.1), an upstream deposit owing to an eligible bank affiliate.

**(2) Section 90 of the Act is amended by adding the following after subsection (8):**

Upstream  
deposit —  
eligible bank  
affiliate

(8.1) For the purposes of this section, if a taxpayer is an eligible Canadian bank and an eligible bank affiliate of the taxpayer is owed, at any time in a particular taxation year of the affiliate or the immediately preceding taxation year, an upstream deposit,

(a) the affiliate is deemed to make a loan to the taxpayer immediately before the end of the particular year equal to the amount determined by the following formula, where all amounts referred to in the formula are to be determined using Canadian currency:

$$A - B - C$$

where

A is 90% of the average of all amounts each of which is, in respect of a calendar month that ends in the particular year, the greatest total amount at any time in the month of the upstream deposits owing to the affiliate,

B is the lesser of

(i) the amount, if any, by which the affiliate’s excess liquidity for the particular year exceeds the average of all amounts each of which is, in respect of a calendar month that ends in the particular year, the greatest total amount at any time in the month of eligible Canadian indebtedness owing to the affiliate, and

(ii) the amount determined for A, and

C is the amount, if any, by which the amount determined for A for the immediately preceding year exceeds the amount determined for B for the immediately preceding year; and

(b) if the formula in paragraph (a) would, in the absence of section 257, result in a negative amount for the particular year,

(i) the taxpayer is deemed to repay immediately before the end of the particular year — in an amount equal to the absolute value of the negative amount and in the order in which they arose — loans made by the affiliate under paragraph (a) in a prior taxation year and not previously repaid, and

(ii) the repayment is deemed to not be part of a series of loans or other transactions and repayments.

**(3) Subsection 90(15) of the Act is amended by adding the following definitions in alphabetical order:**

“eligible bank affiliate” « <i>filiale bancaire admissible</i> »	“eligible bank affiliate” has the same meaning as in subsection 95(2.43).
“eligible Canadian bank” « <i>banque canadienne admissible</i> »	“eligible Canadian bank” has the same meaning as in subsection 95(2.43).
“eligible Canadian indebtedness” « <i>dettes canadiennes admissibles</i> »	“eligible Canadian indebtedness” has the same meaning as in subsection 95(2.43).
“excess liquidity” « <i>liquidités excédentaires</i> »	“excess liquidity” has the same meaning as in subsection 95(2.43).
“upstream deposit” « <i>dépôt en amont</i> »	“upstream deposit” has the same meaning as in subsection 95(2.43).

**(4) Subsections (1) to (3) apply in respect of taxation years of a foreign affiliate of a taxpayer that begin after Announcement Date.**

**2. (1) The portion of subparagraph 95(2)(a.1)(ii) of the English version of the Act before clause (A) is replaced by the following:**

(ii) the property was not

**(2) Subparagraph 95(2)(a.1)(ii) of the Act is amended by striking out “nor” at the end of clause (A), by adding “or” at the end of clause (B) and by adding the following after clause (B):**

(C) an indebtedness, or a lease obligation, of a person resident in Canada or in respect of a business carried on in Canada, that was purchased and sold by the affiliate on its own account,

**(3) The portion of paragraph 95(2)(a.1) of the Act after subparagraph (ii) and before subparagraph (iii) is replaced by the following:**

unless more than 90% of the gross revenue of the affiliate for the year from the sale of property is derived from the sale of such property (other than a property described in subparagraph (ii) the cost of which to any person is a cost referred to in subparagraph (i) or a property the income from the sale of which is not included in computing the income from a business other than an active business of the affiliate under this paragraph because of subsection (2.31)) to persons with whom the affiliate deals at arm’s length (which, for this purpose, includes a sale of property to a non-resident corporation with which the

affiliate does not deal at arm's length for sale to persons with whom the affiliate deals at arm's length) and, where this paragraph applies to include income of the affiliate from the sale of property in the income of the affiliate from a business other than an active business,

**(4) Paragraph 95(2)(a.3) of the Act is amended by replacing the portion after subparagraph (ii) and before subparagraph (iii) by the following:**

unless more than 90% of the gross revenue of the affiliate derived directly or indirectly from indebtedness and lease obligations (other than excluded revenue or revenue that is not included in computing the income from a business other than an active business of the affiliate under this paragraph because of subsection (2.31)) was derived directly or indirectly from indebtedness and lease obligations of non-resident persons with whom the affiliate deals at arm's length and, where this paragraph applies to include income of the affiliate for the year in the income of the affiliate from a business other than an active business,

**(5) Section 95 of the Act is amended by adding the following after subsection (2.3):**

Application of paragraphs (2)(a.1) and (a.3)

(2.31) Paragraphs (2)(a.1) and (a.3) do not apply to a controlled foreign affiliate (for the purposes of section 17) of an eligible Canadian bank (as defined in subsection (2.43)) in respect of activities carried out to earn income from a property, other than a specified property of the affiliate, if

(a) the affiliate sells the property, or performs services as an agent in relation to a purchase or sale of the property, and it is reasonable to conclude that the cost to any person of the property is relevant in computing the income from

(i) a business carried on by the bank or a person resident in Canada with whom the bank does not deal at arm's length, or

(ii) a business carried on in Canada by a non-resident person with whom the bank does not deal at arm's length;

(b) the property has a readily available fair market value and

(i) is listed on a recognized stock exchange, or

(ii) would be a mark-to-market property (as defined in subsection 142.2(1)) of the bank if it were owned by the bank;

(c) the purchase and sale of the property by the affiliate, or services performed by the affiliate as agent in respect of the purchase or sale, are made

(i) on terms and conditions that are substantially the same as the terms and conditions of similar purchases or sales of, or services performed in respect of the purchase or sale of, such property by persons dealing at arm's length,

(ii) in the course of a business

(A) that regularly includes trading or dealing in securities principally with persons with whom the affiliate deals at arm's length, and

(B) that is principally carried on through a permanent establishment in a country other than Canada, and

(iii) for the purpose of enabling the purchase or sale of the property by a particular person who deals at arm's length with the affiliate and the bank; and

(d) the affiliate is a foreign bank or a trader or dealer in securities and the activities of the business are regulated

(i) under the laws of the country under whose laws the affiliate is governed and any of exists, was (unless the affiliate was continued in any jurisdiction) formed or organized, or was last continued, and under the laws of each country in which the business is carried on through a permanent establishment in that country,

(ii) under the laws of the country (other than Canada) in which the business is principally carried on, or

(iii) if the affiliate is related to a corporation, under the laws of the country under whose laws that related corporation is governed and any of exists, was (unless that related corporation was continued in any jurisdiction) formed or organized, or was last continued, if those regulating laws are recognized under the laws of the country in which the business is principally carried on and all those countries are members of the European Union.

Specified  
property

(2.32) For purposes of subsection (2.31), "specified property", of a foreign affiliate, means a property that is owned by the affiliate for more than ten days and that is

(a) a share of the capital stock of a corporation resident in Canada;

(b) a property traded on a stock exchange located in Canada and not traded on a stock exchange located in the jurisdiction in which the affiliate is resident; or

(c) a debt obligation

(i) of a corporation resident in Canada,

(ii) of a trust or partnership, units of which are traded on a stock exchange located in Canada, or

(iii) of, or guaranteed by, the Government of Canada, the government of a province, an agent of a province, a municipality in Canada or a municipal or public body performing a function of government in Canada.

**(6) The portion of subsection 95(2.4) of the French version of the Act before subparagraph (a)(i) is replaced by the following:**

Application de  
l'alinéa (2)a.3)

(2.4) L'alinéa (2)a.3) ne s'applique pas à une société étrangère affiliée d'un contribuable pour ce qui est du revenu qu'elle tire directement ou indirectement de dettes, dans la mesure où, à la fois :

a) elle a tiré ce revenu dans le cours des activités d'une entreprise menée principalement avec des personnes avec lesquelles elle n'a aucun lien de dépendance et qu'elle exploite à titre de banque étrangère, de société de fiducie, de caisse de crédit, de compagnie d'as-

surance ou de négociateur ou courtier en valeurs mobilières ou en marchandises, dont les activités sont régies par les lois des pays suivants, selon le cas :

**(7) Paragraph 95(2.4)(b) of the Act is replaced by the following:**

(b) all the following conditions are satisfied:

(i) the income is derived by the affiliate from trading or dealing in the indebtedness (which, for this purpose, consists of income from the actual trading or dealing in the indebtedness and interest earned by the affiliate during a short term holding period on indebtedness acquired by it for the purpose of the trading or dealing) directly or indirectly with persons (in this subsection referred to as “regular customers”) that

(A) deal at arm’s length with the affiliate, and

(B) are resident, or carry on business through a permanent establishment, in a country other than Canada,

(ii) the affiliate has a substantial market presence in the country, and

(iii) one or more persons that deal at arm’s length with the affiliate and are resident, or carry on business through a permanent establishment, in the country

(A) carry on a business

(I) that competes in the country with the business of the affiliate, and

(II) the activities of which are regulated under the laws of the country or, where the country is a member of the European Union, any country that is a member of the European Union, in the same manner as are the activities of the business of the affiliate, and

(B) have a substantial market presence in the country,

**(8) Section 95 of the Act is amended by adding the following after subsection (2.42):**

(2.43) The following definitions apply in this subsection and subsections (2.44) to (2.46).

Definitions —  
subsections  
(2.43) to (2.46)

“Canadian  
indebtedness”  
« dettes  
canadiennes »

“Canadian indebtedness” means indebtedness (other than upstream deposits) owed by persons resident in Canada or in respect of businesses carried on in Canada.

“eligible bank  
affiliate”  
« filiale  
bancaire  
admissible »

“eligible bank affiliate”, of an eligible Canadian bank at any time, means a foreign bank that, at that time, is a controlled foreign affiliate (for the purposes of section 17) of the eligible Canadian bank and is described in subparagraph (a)(i) of the definition “investment business” in subsection (1).

“eligible  
Canadian  
bank”  
« banque  
canadienne  
admissible »

“eligible Canadian bank” means a bank listed in Schedule I to the *Bank Act*.

<p>“eligible Canadian indebtedness” « <i>dettes canadiennes admissibles</i> »</p>	<p>“eligible Canadian indebtedness”, owing to an eligible bank affiliate of an eligible Canadian bank, means bonds, debentures, notes or similar obligations of the Government of Canada, the government of a province, an agent of a province, a municipality in Canada or a municipal or public body performing a function of government in Canada, that are owing to the affiliate, other than property in respect of which paragraph (2)(a.3) does not apply because of subsection (2.31).</p>
<p>“eligible currency hedge” « <i>couverture de change admissible</i> »</p>	<p>“eligible currency hedge”, of an eligible bank affiliate of an eligible Canadian bank, means an agreement that provides for the purchase, sale or exchange of currency and that</p> <p>(a) can reasonably be considered to have been made by the affiliate to reduce its risk of fluctuations in the value of currency with respect to eligible Canadian indebtedness and upstream deposits owing to the affiliate; and</p> <p>(b) cannot reasonably be considered to have been made by the affiliate to reduce its risk with respect to property other than eligible Canadian indebtedness and upstream deposits owing to the affiliate.</p>
<p>“excess liquidity” « <i>liquidités excédentaires</i> »</p>	<p>“excess liquidity”, of an eligible bank affiliate of an eligible Canadian bank for a taxation year of the affiliate, means the amount, if any, by which</p> <p>(a) the average of all amounts each of which is, in respect of a month that ends in the twelve-month period that begins 60 days prior to the beginning of the year — or, if the affiliate was formed after the beginning of the period, in respect of a month that ends in the year — the amount of the affiliate’s relationship deposits for the month, expressed in the affiliate’s calculating currency for the year unless the context requires otherwise,</p> <p>exceeds</p> <p>(b) the average of all amounts each of which is, in respect of a month that ends in the period — or, if the affiliate was formed after the beginning of the period, in respect of a month that ends in the year — the amount of the affiliate’s organic assets for the month, expressed in the affiliate’s calculating currency for the year unless the context requires otherwise.</p>
<p>“organic assets” « <i>actif organique</i> »</p>	<p>“organic assets”, of an eligible bank affiliate of an eligible Canadian bank for a month, means the total of all amounts in respect of the affiliate each of which is</p> <p>(a) included in the amounts reported as loans in the assets section of the consolidated monthly balance sheet accepted by the Superintendent of Financial Institutions that is filed for the month by the bank, or another corporation resident in Canada that is related to the bank at the end of the month, or</p> <p>(b) an amount owing to the affiliate by a person that is related to the affiliate (other than an amount described in paragraph (a))</p>

<p>“qualifying indebtedness” « dettes déterminées »</p>	<p>but does not include the amount of an eligible Canadian indebtedness or upstream deposit owing to the affiliate.</p> <p>“qualifying indebtedness”, owing to an eligible bank affiliate of an eligible Canadian bank, means an upstream deposit owing to, or an eligible Canadian indebtedness of, the affiliate, to the extent that it can reasonably be considered that</p> <ul style="list-style-type: none"> <li>(a) the upstream deposit or the acquisition of eligible Canadian indebtedness, as the case may be, is funded by <ul style="list-style-type: none"> <li>(i) property transferred or lent by a person other than the bank or a person resident in Canada that was not, at the time of the transfer or loan, dealing at arm’s length with the bank,</li> <li>(ii) a repayment of all or part of an upstream deposit owing to the affiliate, or</li> <li>(iii) the purchase of eligible Canadian indebtedness by the bank or a person resident in Canada that was not, at the time of the transfer or loan, dealing at arm’s length with the bank; and</li> </ul> </li> <li>(b) the proceeds of the upstream deposit or the proceeds received by the vendor of the eligible Canadian indebtedness, as the case may be, are used for a purpose other than to fund a transfer or loan of property by the bank — or another person resident in Canada that was not, at the time of the transfer or loan, dealing at arm’s length with the bank — to the affiliate or another foreign affiliate of the bank or of the other person.</li> </ul>
<p>“relationship deposits” « dépôts apparentés »</p>	<p>“relationship deposits”, of an eligible bank affiliate of an eligible Canadian bank for a month, means the total of all amounts included in the amounts reported as demand and notice deposits, and fixed-term deposits in the liabilities section of the consolidated monthly balance sheet accepted by the Superintendent of Financial Institutions that is filed for the month by the bank, or another corporation resident in Canada that is related to the bank at the end of the month, that are deposits (other than of a temporary nature) of the affiliate made by a person who at the end of the month</p> <ul style="list-style-type: none"> <li>(a) deals at arm’s length with the affiliate; and</li> <li>(b) is not resident in Canada.</li> </ul>
<p>“total specified indebtedness” « dettes désignées totales »</p>	<p>“total specified indebtedness”, owing to an eligible bank affiliate of an eligible Canadian bank for a taxation year of the affiliate, means the average of all amounts each of which is, in respect of a month that ends in the year, the greatest total amount at any time in the month that is the total of all amounts each of which is</p> <ul style="list-style-type: none"> <li>(a) the amount of an upstream deposit owing to the affiliate;</li> <li>(b) the amount of an eligible Canadian indebtedness owing to the affiliate; or</li> <li>(c) the positive or negative fair market value of an eligible currency hedge of the affiliate.</li> </ul>
<p>“upstream deposit” « dépôt en amont »</p>	<p>“upstream deposit”, owing to an eligible bank affiliate of an eligible Canadian bank, means indebtedness owing by the bank to the affiliate.</p>

FAPI  
adjustment —  
eligible bank  
affiliate

(2.44) If a non-resident corporation (in this subsection referred to as the “affiliate”) is, throughout a taxation year of the affiliate, an eligible bank affiliate of an eligible Canadian bank, and the bank elects in writing under this subsection, in respect of the affiliate for the year, and files the election with the Minister on or before the filing-due date of the bank for the particular taxation year of the bank in which the year ends,

(a) there is to be deducted in computing the amount determined for A in the definition “foreign accrual property income” in subsection (1) in respect of the affiliate for the year, the lesser of

(i) the amount determined, without reference to this paragraph, for A in the definition “foreign accrual property income” in subsection (1) in respect of the affiliate for the year, and

(ii) the amount determined by the following formula, where each amount referred to in the formula is to be determined using Canadian currency:

$$A - B - C - D$$

where

A is the total of all amounts each of which is the affiliate’s income for the year that is from a qualifying indebtedness owing to, or an eligible currency hedge of, the affiliate and that would, in the absence of this subsection, be included in computing the income of the affiliate from a business other than an active business of the affiliate,

B is the total of all amounts each of which is the affiliate’s loss for the year that is from a qualifying indebtedness owing to, or an eligible currency hedge of, the affiliate and that would, in the absence of this subsection, be deducted in computing the income of the affiliate from a business other than an active business of the affiliate,

C is the total of all amounts each of which is the amount, if any, by which an amount included in computing A or B in respect of an upstream deposit exceeds the amount that would be the affiliate’s income, or is less than the amount that would be the affiliate’s loss, as the case may be, for the year from the upstream deposit if the interest received or receivable by the affiliate in respect of the upstream deposit were computed at an interest rate equal to the lesser of

(A) the rate of interest in respect of the upstream deposit, and

(B) the benchmark rate of interest, acceptable to the Minister, that is

(I) if the upstream deposit is denominated in a qualifying currency (as defined in subsection 261(1)) that is the affiliate’s calculating currency, the average, for the year, of a daily inter-bank offered rate for loans denominated in that currency with a term to maturity of three months, or

(II) in any other case, the average, for the year, of a daily rate for Canadian dollar denominated bankers' acceptances with a term to maturity of three months,

D is the amount determined by the formula

$$E \times F/G$$

where

E is the amount, if any, by which the amount determined for A exceeds the total of the amounts determined for B and C,

F is the amount, if any, by which the total specified indebtedness owing to the affiliate for the year exceeds the affiliate's excess liquidity for the year, and

G is the total specified indebtedness owing to the affiliate for the year, and

(b) there is to be included, in computing the income of the affiliate from an active business for the year, an amount equal to the proportion of the amount computed under the formula in subparagraph (a)(ii), computed as if each amount referred to in that formula were determined using the affiliate's calculating currency, that the amount that is required to be deducted under paragraph (a) for the year is of the amount described in subparagraph (a)(ii).

Investment  
business and  
excluded  
property

(2.45) If an election is made under subsection (2.44) in respect of an eligible bank affiliate of an eligible Canadian bank for a taxation year of the affiliate,

(a) for the purposes of the definition "investment business" in subsection (1), the bank, and any other person resident in Canada that does not deal at arm's length with the bank, are deemed to deal at arm's length with the affiliate in respect of the making of upstream deposits, and acquisitions of Canadian indebtedness from the bank or the other person, by the affiliate in the course of a business carried on by the affiliate in the year if the affiliate's excess liquidity for the year is at least 90% of the total specified indebtedness owing to the affiliate for the year; and

(b) for the purposes of paragraph (b) of the definition "excluded property" in subsection (1),

(i) the fair market value of each upstream deposit and Canadian indebtedness owing to, and eligible currency hedge of, the affiliate is deemed to be nil,

(ii) at any particular time, the lesser of the following amounts is deemed to be the fair market value of a property of the affiliate that is excluded property at that particular time,

(A) the total of all amounts each of which is the fair market value of an upstream deposit or Canadian indebtedness owing to, or an eligible currency hedge of, the affiliate, and

(B) the amount, if any, by which

(I) the affiliate's relationship deposits for the calendar month that is two months prior to the particular time (or if the affiliate was formed less than two months prior to the particular time, for the calendar month that includes the particular time)

exceeds

(II) the amount of the affiliate's organic assets for the calendar month that is two months prior to the particular time (or if the affiliate was formed less than two months prior to the particular time, for the calendar month that includes the particular time); and

(iii) the amount, if any, by which the amount in clause (ii)(A) exceeds the amount in subparagraph (ii) is deemed to be the fair market value of a property of the eligible bank affiliate that is not excluded property at that time.

**(9) The definition “specified deposit” in subsection 95(2.5) of the Act is replaced by the following:**

“specified deposit”  
« dépôt déterminé »

“specified deposit”, of a foreign affiliate of a taxpayer, means a deposit of the affiliate made with a permanent establishment in a country other than Canada of a prescribed financial institution resident in Canada if the income from the deposit is income of the affiliate for the year that would, in the absence of paragraph (2)(a.3), be income from an active business carried on by the affiliate in a country other than Canada, other than a business the principal purpose of which is to derive income from property (including interest, dividends, rents, royalties or any similar returns, or substitutes therefor) or profits from the disposition of investment property.

**(10) Section 95 of the Act is amended by adding the following after subsection (3):**

Application of paragraph (2)(b) — eligible Canadian bank

(3.01) Paragraph (2)(b) does not apply to a controlled foreign affiliate (for the purposes of section 17) of an eligible Canadian bank (as defined in subsection (2.43)) in respect of services performed in connection with the purchase or sale of a property described in paragraph (2.31)(b) if

(a) the services have been performed by the affiliate

(i) under terms and conditions that are substantially the same as the terms and conditions that would have been made between persons who deal at arm's length with each other,

(ii) in the course of a business

(A) that regularly includes trading or dealing in securities principally with persons with whom the affiliate deals at arm's length, and

(B) that is principally carried on through a permanent establishment in a country other than Canada, and

(iii) for the purpose of enabling the acquisition or disposition of the property by a person who, at the time of the acquisition or disposition, deals at arm's length with the affiliate and the eligible Canadian bank; and

(b) the affiliate is a foreign bank or a trader or dealer in securities and the activities of the business are regulated

(i) under the laws of the country under whose laws the affiliate is governed and any of exists, was (unless the affiliate was continued in any jurisdiction) formed or organized, or was last continued, and under the laws of each country in which the business is carried on through a permanent establishment in that country,

(ii) under the laws of the country (other than Canada) in which the business is principally carried on, or

(iii) if the affiliate is related to a corporation, under the laws of the country under whose laws that related corporation is governed and any of exists, was (unless that related corporation was continued in any jurisdiction) formed or organized, or was last continued, if those regulating laws are recognized under the laws of the country in which the business is principally carried on and all those countries are members of the European Union.

**(11) Subsections (1) to (10) apply in respect of taxation years of a foreign affiliate of a taxpayer that begin after October 2012.**

**3. (1) The Act is amended by adding the following after section 125.2:**

Part XIII tax  
— eligible  
bank affiliate

**125.21** There may be deducted in computing the tax payable under this Part for a taxation year by a particular corporation that is throughout the year an eligible Canadian bank (as defined in subsection 95(2.43)) the total of all amounts, each of which is the amount, if any, by which

(a) an amount paid under paragraph 212(1)(b) in respect of interest paid or credited in the year by the particular corporation in respect of an upstream deposit (as defined in subsection 95(2.43)) owing to a non-resident corporation that is, throughout the year, an eligible bank affiliate (as defined in subsection 95(2.43)) of the particular corporation

exceeds

(b) the total of all amounts each of which is a portion of the amount described in paragraph (a) that is available to the non-resident corporation or any other person or partnership at any time as a credit or reduction of, or deduction from, any amount otherwise payable to the government of a country other than Canada, or a political subdivision of that country, having regard to all available provisions of the laws of that country, or political subdivision, as the case may be, any tax treaty with that country and any other agreements entered into by that country or political subdivision.

**(2) Subsection (1) applies in respect of taxation years that begin after October 2012.**

#### INCOME TAX REGULATIONS

**4. (1) Paragraph (b) of the definition “earnings” in subsection 5907(1) of the *Income Tax Regulations* is replaced by the following:**

(b) in any other case, the total of all amounts each of which is an amount of income that would be required under paragraph 95(2)(a) or subsection 95(2.44) of the Act to be included in computing the affiliate's income or loss from an active business for the year if that income were computed taking into account the rules in subsection (2.03); (*gains*)

**(2) Subparagraph (d)(ii) of the definition "exempt earnings" in subsection 5907(1) of the Regulations is amended by striking out "or" at the end of clause (H) and by adding the following after clause (I):**

(J) an amount that is required to be included in computing the particular affiliate's income from an active business for the year under subsection 95(2.44) of the Act if the amount is in respect of income that would, in the absence of paragraph 95(2)(a.3) of the Act, be income from an active business carried on by the particular affiliate in a designated treaty country, or

**(3) Subsections (1) and (2) apply in respect of taxation years of a foreign affiliate of a taxpayer that begin after October 2012.**

