Preface

These explanatory notes describe proposed amendments to the *Income Tax Act* and related legislation. These explanatory notes describe these proposed amendments, clause by clause, for the assistance of Members of Parliament, taxpayers and their professional advisors.

The Honourable William Francis Morneau, P.C., M.P.
Minister of Finance

These notes are intended for information purposes only and should not be construed as an official interpretation of the provisions they describe.

Table of Contents

Clause	Topic	Page
	Income Tax Act and Income Tax Regulations	
1	Canada Workers Benefit – Improving Access	4
6	Deductibility of Employee Contributions to the Enhanced Portion of the Quebec Pension Plan	10
7	Reporting Requirements for Trusts	10
11	Artificial Losses Using Equity-Based Financial Arrangements	14
13	Stop-Loss Rule on Share Repurchase Transactions	21
15	At-Risk Rules for Tiered Partnerships	26
16	Cross-Border Surplus Stripping using Partnerships and Trusts	27
20	Foreign Affiliates – Investment Businesses, Controlled Foreign Affiliate Status, Trading or Dealing in Indebtedness, Reassessments and Reporting Requirements	37
25	Foreign Divisive Reorganizations	45
27	Passive Investment Income – Allocation of Losses	50
28	Reassessment Period – Requirements for Information and Compliance Orders	51
31	Reassessment Period – Non-Resident Non-Arm's Length Persons	53
32	Sharing Information for Criminal Matters	54
	Mutual Legal Assistance in Criminal Matters Act	
33	Sharing Information for Criminal Matters	55
	Criminal Code	
38	Sharing Information for Criminal Matters	59

Income Tax Act and Income Tax Regulations

Canada Workers Benefit – Improving Access

Clause 1

Definitions concerning the Canada Workers Benefit (formerly the Working Income Tax Benefit)

Income Tax Act (ITA)

122.7(1)

Subsection 122.7(1) of the *Income Tax Act* (the "Act") defines a number of terms for purposes of the Canada Workers Benefit (CWB), which replaces the Working Income Tax Benefit.

"adjusted net income"

To ensure that the CWB is available only to low-income individuals, the CWB is gradually reduced for individuals whose "adjusted net income" (or, where applicable, the combined adjusted net income of the individual and his or her cohabitating spouse or common-law partner) exceeds certain thresholds. In this respect, the definition "adjusted net income" is a key component of the computation of the CWB.

An individual's adjusted net income for a taxation year is the individual's net income for the year adjusted to include amounts that would otherwise be excluded from income because of paragraph 81(1)(a) (amounts exempt from income under another enactment of Parliament other than a tax treaty) or subsection 81(4) (the first $1,000 of an allowance received as an emergency volunteer). There are also certain items that are excluded from an individual's net income for purposes of this definition.

The definition "adjusted net income" is amended in order to remove, from the inclusion in the computation of an individual's adjusted net income for a taxation year, income that is excluded pursuant to paragraph 81(1)(a) or subsection 81(4). However, pursuant to new subsection (1.1), an individual may choose to include these amounts in the definition of working income under this subsection, in which case the relevant amounts will also be included for the purposes of computing adjusted net income. For more information, see the commentary for subsection 122.7(1.1).

"working income"

The definition "working income" is relevant in determining if an eligible individual qualifies for the CWB in a taxation year.

An individual's working income for a taxation year is the total of the individual's income from employment (determined without reference to the deductions allowed in section 8 of the Act) and

from research grants, fellowships, scholarships, bursaries or prizes included under paragraph 56(1)(n) or (o) or amounts received under the *Wage Earner Protection Program Act* and from any business carried on by the individual (otherwise than as a specified member of a partnership). An individual's working income for a taxation year also includes any of these amounts that would, but for paragraph 81(1)(a) and subsection 81(4), be included in the individual's income for the year. Paragraph 81(1)(a) excludes income amounts that are exempt from income under another enactment of Parliament other than a tax treaty while subsection 81(4) excludes the first $1,000 of an allowance received by an emergency volunteer.

The definition "working income" is amended to exclude from the computation of an individual's working income for a taxation year income that is excluded pursuant to paragraph 81(1)(a) or subsection 81(4). However, pursuant to new subsection (1.1), an individual may still include these excluded amounts in determining that individual's working income. For more information, see the commentary for subsection 122.7(1.1).

The amendments to the definitions "adjusted net income" and "working income" apply as of January 1, 2019.

Optional amounts

ITA

122.7(1.1)

An individual's "working income", and if applicable, the "working income" of the individual's co-habiting spouse or common-law partner for a taxation year, is relevant in determining the amount of the individual's CWB entitlement, if any, for the taxation year. An individual's working income for a taxation year is the total of the individual's income from employment (determined without reference to the deductions allowed in section 8 of the Act) and from research grants, fellowships, scholarship, bursaries or prizes included under paragraphs 56(1)(n) or (o) or amounts received under the *Wage Earner Protection Program Act* and from any business carried on by the individual (otherwise than as a specified member of a partnership).

An individual's "adjusted net income" is relevant to ensure that the CWB is available only to low-income individuals. The CWB is gradually reduced for individuals whose "adjusted net income" (or, where applicable, the combined adjusted net income of the individual and their cohabitating spouse or common-law partner) exceeds certain thresholds.

New subsection 122.7(1.1) allows an individual to include amounts in the individual's working income (as defined in subsection (1)) that would normally be excluded from working income because of paragraph 81(1)(a) or subsection 81(4). Subsection 122.7(1.1) provides that an individual who includes these amounts in the calculation of the individual's working income must also include the amounts that would be excluded under paragraph 81(1)(a) or subsection 81(4) from the working income of that individual's eligible spouse, if applicable. Furthermore, where an individual includes these amounts in working income, the individual must also include

the amounts that would normally be excluded from adjusted net income (as defined in subsection 122.7(1)) because of paragraph 81(1)(a) or subsection 81(4) in calculating that individual's and, if applicable, the eligible spouse of that individual's, adjusted net income.

Choosing to include these amounts may increase the CWB entitlement of certain individuals, for instance individuals who would otherwise have insufficient working income to qualify for the credit.

These amendments apply as of January 1, 2019.

Deemed payment on account of tax

ITA

122.7(2)

Section 122.7 of the Act provides the CWB, a refundable credit for low-income individuals and families, who have earnings from employment or self-employment ("working income"). Subsection 122.7(2) provides for the calculation of the "basic" CWB and subsection (3) provides the CWB "disability supplement". To receive the basic CWB for a taxation year, subsection (2) provides that an eligible individual must file a return of income for the year and apply for the CWB.

Subsection (2) is amended to remove the requirement that an individual must apply for the CWB in order to receive an amount under this subsection.

This amendment applies as of January 1, 2019.

Only one eligible individual

ITA

122.7(5)

Subsection 122.7(5) of the Act provides that where an eligible individual and an eligible spouse of the eligible individual both make a claim under subsection 122.7(2) for the "basic" CWB, the amount of the basic CWB is deemed to be nil. This provision is intended to ensure that a couple does not file duplicate claims for the basic CWB. The terms "eligible individual" and "eligible spouse" are defined in subsection 122.7(1).

Consequential on the removal of the requirement that a person must apply for the basic CWB, subsection 122.7(5) is amended to introduce special rules that apply where both an individual and their spouse would otherwise qualify as an eligible individual for the purposes of the CWB.

New paragraph (a) of subsection 122.7(5) provides that where an individual and their spouse would both otherwise qualify as eligible individuals and the individual and their spouse agree which of them should qualify as the eligible individual for the taxation year, only the individual that is agreed upon as the eligible individual shall be an eligible individual for the year for the purposes of the basic CWB under subsection (2).

New paragraph (b) of subsection 122.7(5) provides that where the two individuals cannot agree, only the individual that the Minister of National Revenue designates shall be an eligible individual for the year for the purposes of the basic CWB under subsection 122.7(2).

This amendment applies as of January 1, 2019.

Special rules for eligible dependant

ITA

122.7(10)

Subsection 122.7(10) of the Act deems a child not to be an eligible dependant of an individual for a taxation year if the child is also an eligible dependant of another individual for the year and both individuals identify the child as an eligible dependant for purposes of the "basic" CWB or the CWB "disability supplement". This provision is intended to ensure that not more than one parent identifies the child as an eligible dependant in the taxation year.

Consequential on the removal of the requirement that a person must apply in order to receive the basic CWB, subsection 122.7(1) is amended to introduce special rules to provide that only one individual may claim a child as an eligible dependant for a taxation year.

New paragraph (a) of subsection 122.7(10) provides that where there is more than one individual who would otherwise be eligible to claim a child as an eligible dependant, the individuals can agree on which of them the child will be deemed to be an eligible dependant of a taxation year.

New paragraph (b) of subsection 122.7(10) provides that where the two individuals cannot agree, the child will be deemed to be an eligible dependant only of the individual designated by the Minister of National Revenue.

This amendment applies as of January 1, 2019.

Clause 2

Requirement to file

Income Tax Regulations (ITR)

203

New section 203 of the *Income Tax Regulations* (the "Regulations") imposes a requirement on designated educational institutions included in paragraph (a) of the definition of "designated educational institution" in subsection 118.6(1) of the Act to provide an annual information return, called a Tuition and Enrollment Certificate, to the Canada Revenue Agency.

This will facilitate the provision of the Canada Workers Benefit in situations where an individual has not applied for it.

This amendment applies to the 2019 and subsequent taxation years.

Clause 3

Date returns to be filed

ITR

205(3)

The Act and the Regulations impose various reporting obligations, including the requirement for certain taxpayers to file information returns with the Canada Revenue Agency by a specific date. The Act provides, with some exceptions, that when a person fails to file an information return on time, a penalty equal to $25 per day may apply, subject to a $100 minimum and a $2,500 maximum. The penalty is applicable to each information return that is filed late.

Recognizing that this penalty could be excessive in cases where a large number of returns of the same type are required to be filed, subsection 162(7.01) of the Act provides for a separate, lower, graduated penalty that would be applicable where information returns prescribed in subsection 205(3) of the Regulations, were filed late.

Subsection 205(3) is amended to add the Tuition and Enrollment Certificate to the list of prescribed returns for purposes of subsection 162(7.01).

This amendment applies as of January 1, 2019.

Clause 4

Electronic Filing

ITR

205.1

The Act and the Regulations impose various reporting obligations, including the requirement for certain taxpayers to file information returns with the Canada Revenue Agency in a specified manner. Section 205.1 of the Regulations provides that where an information return is prescribed and where over 50 of one type of a prescribed information return is filed in a taxation year, the return must be filed electronically through the internet.

Subsection 205(3) of the Regulations is amended to add the Tuition and Enrollment Certificate to the list of prescribed returns for purposes of this subsection.

This amendment applies as of January 1, 2019.

Clause 5

Distribution of taxpayers’ portions of returns

ITR

209(1)

Subsection 209(1) of the Regulations requires issuers of T4 slips and other specified information returns to provide two copies of the relevant portion of the return to the taxpayer to whom the return relates.

Subsection 209(1) is amended to add a reference to section 203 of the Regulations consequential on the introduction of that section, which imposes a requirement on designated educational institutions (as defined in subsection 118.6(1) of the Act) that are located in Canada to provide the Tuition and Enrollment Certificate to the Canada Revenue Agency.

Distribution of taxpayers’ portions of returns

ITR

209(5)

Subsection 209(5) of the Regulations permits the issuer of a T4 slip to provide the T4 slip to a taxpayer electronically, without having received the taxpayer’s express consent to receive the T4 slip in this format.

An issuer can provide a T4 slip electronically only if

- the issuer meets the criteria specified by the Minister of National Revenue pursuant to section 221.01 of the Act;
- the taxpayer has not requested that they be provided with a paper copy of the T4 slip; and
- the taxpayer is a current employee, is not on extended leave and can reasonably be expected to have access to their T4s.

Subsection 209(5) is amended to also permit designated educational institutions to provide Tuition and Enrolment Certificates to students electronically without having received the taxpayer’s express consent to receive the Certificate in that format.

Most of the conditions that allow an issuer to provide an information return under this subsection will also apply to a Tuition and Enrolment Certificate. However, subparagraph 209(5)(c)(ii) is amended in order to clarify that the condition that an information return can be provided electronically only if the taxpayer is a current employee and is not on extended leave, applies only in respect of the T4.

The amendments to section 209 apply as of January 1, 2019.

Deductibility of Employee Contributions to the Enhanced Portion of the Quebec Pension Plan

Clause 6

CPP/QPP contributions on self-employed earnings

ITA

60(e)(ii)

Subparagraph 60(e)(ii) of the Act provides a deduction for a taxpayer's first additional contribution and second additional contribution under the Canada Pension Plan made in respect of the taxpayer's self-employed earnings for the year.

Subparagraph (ii) is amended to permit a deduction for "a like contribution under a provincial pension plan" (*i.e.*, additional contributions to the Quebec Pension Plan).

Enhanced CPP contributions

ITA

60(e.1)

Paragraph 60(e.1) of the Act provides a deduction for a taxpayer's first additional contribution and second additional contribution under the Canada Pension Plan made in respect of the taxpayer's employment income other than self-employed earnings.

Subparagraph (i) is amended to permit a deduction for "a like contribution under a provincial pension plan" (i.e., additional contributions to the Quebec Pension Plan).

The amendments to section 60 apply to the 2019 and subsequent taxation years.

Reporting Requirements for Trusts

Clause 7

Exception

ITA

150(1.1)

Subsection 150(1) of the Act stipulates the tax return requirements and the filing dates for different categories of taxpayers. Subsection 150(1.1) sets out exceptions to subsection 150(1), when the filing of a tax return is not required.

Subsection 150(1.1) is amended to provide that the exceptions from filing a return outlined in that subsection do not apply to an express trust, or for civil law purposes a trust other than a trust that is established by law or by judgement, that is resident in Canada unless the trust meets one of the exceptions outlined in new paragraphs 150(1.2)(a) to (n).

The amendment applies to taxation years that end after December 30, 2021.

Exception trusts

ITA

150(1.2)

New subsection 150(1.2) of the Act provides for an exception to subsection 150(1.1) and requires that a trust that is resident in Canada (including trusts that are deemed resident in Canada under section 94 of the Act) and that is an express trust (or for civil law purposes a trust other than a trust that is established by law or by judgement) file a tax return notwithstanding that it may meet one of the exceptions to filing a return listed in subsection 150(1.1).

Subsection 150(1.2), however, also includes a number of exceptions to the requirement to file a return which are listed in paragraphs (a) to (n). In addition, a trust that meets one of the exceptions listed in paragraphs 150(1.2)(a) to (n) will not be required to provide the additional information set out in new section 204.2 of the Regulations. Trusts that are required to file a return, whether because of current filing requirements under subsection 150(1) or because of new subsection 150(1.2), will be required to provide the additional information outlined in section 204.2 of the Regulations. For more information, see the commentary on section 204.2 of the Regulations.

The exceptions to the reporting requirements in new subsection 150(1.2) are as follows:

- trusts that have been in existence for less than three months;
- trusts that hold assets with a total fair market value that does not exceed $50,000 throughout the year, where the only assets held by the trust throughout the year are one or more of
    - cash,
    - certain government debt obligations,
    - a share, debt obligation or right listed on a designated stock exchange,
    - a share of the capital stock of a mutual fund corporation,
    - a unit of a mutual fund trust, and
    - an interest in a related segregated fund (within the meaning assigned by paragraph 138.1(1)(a) of the Act);
- trusts that are required under the relevant rules of professional conduct or the laws of Canada or a province to hold funds for the purposes of the activity that is regulated under those rules or laws, provided the trust is not maintained as a separate trust for a particular client or clients (this provides an exception for a lawyer’s general trust account, but not for specific client accounts);

- trusts that qualify as non-profit organizations or registered charities;
- mutual fund trusts, segregated funds and master trusts;
- graduated rate estates;
- qualified disability trusts;
- employee life and health trusts;
- certain government funded trusts;
- trusts under or governed by a deferred profit sharing plan, pooled registered pension plan, registered disability savings plan, registered education savings plan, registered pension plan, registered retirement income fund or registered retirement savings plan; and
- cemetery care trusts and trusts governed by eligible funeral arrangements.

Subsection 150(1.2) applies to taxation years that end after December 30, 2021.

Clause 8

False statement or omission – trust return

ITA

163(5) and (6)

New subsection 150(1.2) and section 204.2 of the Regulations introduce reporting requirements for certain trusts to file a return of income and to provide additional information. New subsection 163(5) of the Act introduces a penalty for a failure to comply with these new reporting requirements, including the additional information requested in section 204.2 of the Regulations.

New subsection 163(5) of the Act imposes a penalty on any person or partnership that is subject to the reporting requirements in section 204.2 and who fails to file a return for a trust or who knowingly or under circumstances amounting to gross negligence either makes – or participates in, assents to or acquiesces in, the making of – a false statement or omission in the return.

In addition, the penalty will apply if the person or partnership fails to comply with a demand by the Canada Revenue Agency under subsection 150(2) or 231.2(1) to file the return.

New subsection (6) sets out the amount of the penalty in respect of a trust for the purposes of subsection (5) as the greater of

- $2,500; and
- five percent of the highest total fair market value of all the property held by the trust in the year.

Subsections 163(5) and (6) apply to taxation years that end after December 30, 2021.

Clause 9

Additional reporting trusts

ITR

204.2(1) and (2)

New section 204.2 of the Regulations is introduced in order to provide for additional information reporting requirements for certain trusts.

New subsection 204.2(1) introduces a requirement for all trusts that are required to file a return of income to provide additional information (in the T3 form), except for those trusts specifically listed in paragraphs 150(1.2)(a) to (n) of the Act. This additional information includes the name, address, date of birth (in the case of an individual other than a trust), jurisdiction of residence and taxpayer identification number (or TIN, as defined in subsection 270(1) of the Act) for each person who, in the year,

- is a trustee, beneficiary or settlor (as defined in subsection 17(15) of the Act) of the trust; or
- has the ability (through the terms of the trust or a related agreement) to exert influence over trustee decisions regarding the appointment of income or capital of the trust. This would include, for example, a protector of the trust.

New subsection 204.2(2) provides that for the purposes of subsection (1), the requirement to provide information in respect of the beneficiaries of a trust is met if

- the required information is provided in respect of each beneficiary of the trust whose identity is known or ascertainable with reasonable effort by the person making the return at the time of filing the return; and
- for beneficiaries whose identity is not known or ascertainable with reasonable effort by the person making the return, the person making the return provides sufficiently detailed information to determine with certainty whether any particular person is a beneficiary of the trust.

For example, the beneficiary of a trust may not be known where the trust provides for a class of beneficiaries that includes the settlor's current children and grandchildren and any children or grandchildren that the settlor may have in the future. In these circumstances the reporting requirement will be met if the relevant information in respect of all of the settlor's current children and grandchildren are included as well as the details of the terms of the trust that extend the class of beneficiaries to any of the settlor's future children or grandchildren.

Section 204.2 applies to taxation years that end after December 30, 2021.

Clause 10

Master trust

ITR

4802(1.1)

Subsection 4802(1.1) of the Regulations sets out the conditions to prescribe a trust as a "master trust" for the purposes of paragraph 1491(1)(o.4) of the Act. Among other things, a master trust holds investments exclusively for beneficiaries that are registered pension plans or deferred profit sharing plans.

Subsection 4802(1.1) is amended so that the conditions for prescribing a trust as a master trust apply for the purposes of new paragraph 150(1.2)(h) of the Act. For more information, see the commentary on subsection 150(1.2).

The amendment to subsection 4802(1.1) applies to taxation years that end after December 30, 2021.

Artificial Losses Using Equity-Based Financial Arrangements

Clause 11

Dividend rental arrangements - exception

ITA

112(2.31)(b)

Subsection 112 (2.31) of the Act provides an exception to the application of subsection 112(2.3) to a dividend received in a particular period if:

- the dividend rental arrangement is a dividend rental arrangement because of paragraph (c) of the definition "dividend rental arrangement" in subsection 248(1) (*i.e.*, it involves a synthetic equity arrangement)); and
- the taxpayer establishes that, throughout the particular period, no tax-indifferent investor or group of tax-indifferent investors, each member of which is affiliated with every other member, has all or substantially all of the risk of loss and opportunity for gain or profit in respect of the share because of the synthetic equity arrangement or a specified synthetic equity arrangement).

A taxpayer is considered to have satisfied the conditions described in paragraph 112(2.31)(b) if it meets the requirements of paragraph (a), (b), (c) or (d) of subsection 112(2.32). Each of these paragraphs allows the taxpayer to satisfy this condition by obtaining certain specified representations from its synthetic equity arrangement counterparty or counterparties.

Paragraph 112(2.31)(b) is amended to provide that, to fall within the exception, the taxpayer must establish that, throughout the particular period, no tax-indifferent investor or group of tax-

indifferent investors, each member of which is affiliated with every other member, has all or substantially all of the risk of loss and opportunity for gain or profit in respect of the share.

This amendment clarifies that the exception in subsection 112(2.31) cannot be met when a tax-indifferent investor or group of tax-indifferent investors obtains all or substantially all of the risk of loss and opportunity for gain or profit in respect of the share, in any way, including because of the synthetic equity arrangement or a specified synthetic equity arrangement in respect of the share.

This amendment applies to dividends that are paid, or become payable, on or after February 27, 2018.

Representations

ITA

112(2.32)

Subsection 112(2.32) of the Act sets out rules under which a taxpayer is able to satisfy the condition in paragraph 112(2.31)(b) by obtaining certain specified representations in writing from its synthetic equity arrangement counterparty or counterparties.

ITA

112(2.32)(a)(ii)

Paragraph 112(2.32)(a) of the Act applies to a single synthetic equity arrangement. Subparagraph 112(2.32)(a)(ii) is amended to provide that a taxpayer must obtain a representation from its synthetic equity arrangement counterparty or counterparties that all or substantially all of its risk of loss and opportunity for gain or profit in respect of the share during the particular period referred to in subsection 112(2.31) has not been eliminated and cannot be expected by it to be eliminated. This amendment is consequential on the amendment to paragraph 112(2.31)(b).

For more information, see the commentary on paragraph 112(2.31)(b).

This amendment applies to dividends that are paid, or become payable, on or after February 27, 2018.

ITA

112(2.32)(b)(iii)(B)

Paragraph 112(2.32)(b) of the Act applies to back-to-back chains of agreements or arrangements where the final counterparty is either a single counterparty or an affiliated group of counterparties.

Clause 112(2.32)(b)(iii)(B) is amended to provide that a taxpayer must obtain a representation from its synthetic equity arrangement counterparty or counterparties that it has obtained a representation from each of its specified counterparties that all or substantially all of its risk of loss and opportunity for gain or profit in respect of the share during the particular period referred to in subsection 112(2.31) has not been eliminated and cannot be expected by it to be eliminated. This amendment is consequential on the amendment to paragraph 112(2.31)(b).

For more information, see the commentary on paragraph 112(2.31)(b).

This amendment applies to dividends that are paid, or become payable, on or after February 27, 2018.

ITA

112(2.32)(c)(iii)(B)

Paragraph 112(2.32)(c) of the Act applies to back-to-back chains of agreements or arrangements where the final counterparties deal at arm’s length with each other, and generally allows a taxpayer to indirectly obtain representations in respect of certain arrangements that would not have constituted synthetic equity arrangements had they been entered into directly by the taxpayer with the final counterparties.

Clause 112(2.32)(c)(iii)(B) is amended to provide that a taxpayer must obtain a representation from its synthetic equity arrangement counterparty or counterparties that it has obtained a representation from each of its specified counterparties that all or substantially all of its risk of loss and opportunity for gain or profit in respect of the share during the particular period referred to in subsection 112(2.31) has not been eliminated and cannot be expected by it to be eliminated. This amendment is consequential on the amendment to paragraph 112(2.31)(b).

For more information, see the commentary on paragraph 112(2.31)(b).

This amendment applies to dividends that are paid, or become payable, on or after February 27, 2018.

End of particular period

ITA

112(2.33)

Subsection 112(2.33) of the Act is intended to ensure that the exception in subsection 112(2.31) is only available for the period during which the representations that have been provided remain accurate.

Subsection 112(2.33) is amended to provide that, if at a time during a particular period, a counterparty, specified counterparty, affiliated counterparty or affiliated specified counterparty

reasonably expects to become a tax-indifferent investor, or if it has provided a representation described by subparagraph 112(2.32)(a)(ii) or clause 112(2.32)(b)(iii)(B) or (c)(iii)(B) in respect of the share, that all or substantially all of its risk of loss and opportunity for gain or profit in respect of the share will be eliminated, the particular period for which it has provided a representation in respect of the share is deemed to end at that time. This amendment is consequential on the amendment to paragraph 112(2.31)(b).

For more information, see the commentary on paragraph 112(2.31)(b).

This amendment applies to dividends that are paid, or become payable, on or after February 27, 2018.

Clause 12

Definitions

ITA

260(1)

"SLA compensation payment"

An SLA compensation payment is an amount paid pursuant to a securities lending arrangement as compensation for an underlying payment.

This definition is amended so that an SLA compensation payment means an amount paid pursuant to a securities lending arrangement or a specified securities lending arrangement, as compensation for an underlying payment. An SLA compensation payment includes an amount paid pursuant to a specified securities lending arrangement as compensation for a taxable dividend paid on a share described in subparagraph (a)(i) of the definition "specified securities lending arrangement" if the property transferred or lent is described in subparagraph (a)(ii) of that definition.

The broadening of the definition to include an amount paid pursuant to a specified securities lending arrangement results in certain provisions in section 260 of the Act, including its subsections (5) and (5.1), applying to this amount.

For more information, see the commentary on the definition "specified securities lending arrangement".

This amendment applies in respect of amounts paid or payable, or received or receivable, as compensation for dividends on or after February 27, 2018 (or after September 2018 if they are pursuant to a written arrangement entered into before February 27, 2018).

“specified securities lending arrangement”

The definition “specified securities lending arrangement” is added to subsection 260(1). A specified securities lending arrangement means an arrangement, other than a securities lending arrangement, under which:

- a particular person (referred to in the definition as a “transferor”) transfers or lends at any particular time a property to another person (referred to in the definition as a “transferee”) and the property is:
    - a particular share described in paragraph (a) of the definition “qualified security”; or
    - an interest in a partnership or trust where all or any part of its fair market value, immediately before the transfer or loan, is derived, directly or indirectly, from a share described in paragraph (a) of the definition “qualified security”;
- it may reasonably be expected, at the particular time, that the transferee – or a person that does not deal at arm’s length with, or is affiliated with, the transferee – will transfer or return after the particular time to the transferor – or a person that does not deal at arm’s length with, or is affiliated with, the transferor (referred to in the definition as a “substitute transferor”) – a property that is identical to the particular property so transferred or lent; and
- the transferor’s (together with any substitute transferor’s) risk of loss or opportunity for gain or profit with respect to the particular property is not changed in any material respect.

This definition is intended to ensure that arrangements that are substantially similar to those that fall within the definition “securities lending arrangements” are subject to certain provisions normally applicable to those arrangements.

In particular, when a counterparty receives a compensation payment under such a substantially similar arrangement, subsection 260(5.1) will apply, which, in turn, will generally result in subsection 112(2.3) applying by virtue of paragraph (b) of the definition “dividend rental arrangement” to the person making the compensation payment. Therefore, in these circumstances, this person will be denied the inter-corporate dividend deduction on dividends received on the borrowed shares, resulting in a dividend income inclusion that will offset the available deduction in subsection 260(6.1) for the amount of the corresponding dividend compensation payments made to the counterparty under the arrangement.

Depending on the circumstances, subsection 112(2.3) could have already denied the inter-corporate dividend deduction in respect of an arrangement that is a specified securities lending arrangement because it is a synthetic equity arrangement, as defined in subsection 248(1).

For more information, see the commentary on the definition “SLA compensation payment”.

This amendment applies in respect of amounts paid or payable, or received or receivable, as compensation for dividends on or after February 27, 2018 (or after September 2018 if they are pursuant to a written arrangement entered into before February 27, 2018).

Where subsection (5.1) applies

ITA

260(5)

Subsection 260(5) of the Act describes the circumstances under which the compensation payment deeming rule, found in subsection 260(5.1), applies. This deeming rule generally applies where an amount is received under one of these circumstances:

- as an SLA compensation payment, from a person resident in Canada;
- as an SLA compensation payment, from a person not resident in Canada where the amount was paid in the course of carrying on business in Canada through a permanent establishment; or
- as a dealer compensation payment.

Subsection 260(5) provides that the compensation payment deeming rule under subsection 260(5.1) does not apply where the amount is received by a person under an arrangement and one of the main reasons for the person entering into the arrangement was to enable it to receive an SLA compensation payment or a dealer compensation payment that would be deductible in computing the taxable income, or not included in computing the income of the person.

Subsection 260(5) is amended to ensure that the compensation payment deeming rule under subsection 260(5.1) will apply where the amount is received by a person under an arrangement and one of the main reasons for the person entering into the arrangement was to enable it to receive an SLA compensation payment pursuant to a specified securities lending arrangement.

This amendment is intended to ensure that the above anti-avoidance rule is not used to avoid the application of subsection 260(5.1) and, in turn, the application of paragraph (b) of the definition “dividend rental arrangement” in subsection 248(1) to the person making the compensation payment.

For more information, see the commentary on the definition “specified securities lending arrangement” in subsection 260(1).

This amendment applies in respect of amounts paid or payable, or received or receivable, as compensation for dividends on or after February 27, 2018 (or after September 2018 if they are pursuant to a written arrangement entered into before February 27, 2018).

Deductibility

ITA

260(6)

Subsection 260(6) of the Act sets out rules regarding the deductibility of compensation payments made under securities lending arrangements.

Paragraph 260(6)(a) denies a deduction for any dividend compensation payment made by persons other than registered securities dealers, and provides that registered securities dealers may deduct up to 2/3 of the dividend compensation payments they make.

Paragraph 260(6)(a) is amended to clarify that the deduction of up to 2/3 of the dividend compensation payment is not available to a registered securities dealer to the extent that the payment may be deducted by it under subsection 260(6.1).

For more information, see the commentary on subsection 260(6.1).

This amendment applies in respect of amounts paid or payable, or received or receivable, as compensation for dividends on or after February 27, 2018 (or after September 2018 if they are pursuant to a written arrangement entered into before February 27, 2018).

Deductible amount

ITA

260(6.1)

Subsection 260(6.1) of the Act provides a deduction for dividend compensation payments made pursuant to certain dividend rental arrangements. The amount deductible is the lesser of the amount the corporation is obligated to pay as compensation under the arrangement and the amount of the dividends received by the corporation under the arrangement that were identified in its return of income as amounts which are not deductible because of subsection 112(2.3).

Subsection 260(6.1) is amended to remove the “notwithstanding” reference at the beginning of its preamble, in order to more clearly describe its interaction with subsection (6).

For more information, see the commentary on subsection 260(6).

This amendment applies in respect of amounts paid or payable, or received or receivable, as compensation for dividends on or after February 27, 2018 (or after September 2018 if they are pursuant to a written arrangement entered into before February 27, 2018).

Stop-Loss Rule on Share Repurchase Transactions

Clause 13

Adjustment re dividends

ITA

112(5.2)

Subsection 112(5.2) of the Act is a stop-loss rule that applies, in certain circumstances, to the disposition of a share by a taxpayer that is a financial institution, if the share is mark-to-market property to the taxpayer.

Where subsection 112(5.2) applies, the taxpayer's proceeds from the disposition of the share are determined by the formula A + B – (C – D).

Variable A is the taxpayer's proceeds before the application of subsection 112(5.2).

Variable B is the lesser of

- the loss (if any) from the disposition that would be determined before the application of subsection 112(5.2) if the cost of the share were determined without regard to certain provisions that specify the cost of property to a taxpayer; and
- the total of the deductible taxable dividends and the non-taxable dividends received by the taxpayer on the share
    - in the case of a partnership, taxable dividends are included in the total to the extent that they are deductible to members of the partnership;
    - and in the case of a trust, taxable dividends are included in the total to the extent that they have been allocated to beneficiaries of the trust.

Variable C is the sum of

- amounts by which subsection 112(5.2) increased the taxpayer's proceeds on deemed dispositions of the share before the current disposition;
- where the taxpayer is a corporation or trust, amounts by which losses of the taxpayer on deemed dispositions of the share before the current disposition were reduced by the stop-loss rule in subsection 112(3), (3.2), (4) or (4.2); and
- where the taxpayer is a partnership, amounts by which losses of members of the taxpayer on deemed dispositions of the share before the current disposition were reduced by the stop-loss rule in subsection 112(3.1) or (4.2).

Variable D is the amounts by which subsection 112(5.2) decreased the taxpayer's proceeds on deemed dispositions of the share before the current disposition.

Subsection 112(5.2) is amended so that, if the taxpayer received a dividend under subsection 84(3) in respect of the share, variable B always equals the second of the two amounts in the above "lesser of" formula. In cases where the taxpayer has not received a dividend under subsection 84(3) in respect of the share, variable B remains unchanged.

In general terms, this amendment is intended to prevent a taxpayer from realizing a loss on a share repurchase that exceeds any mark-to-market income previously realized with respect to the share and taxed in the hands of the taxpayer. To the extent that the repurchased share was fully hedged, which is typically the case, any mark-to-market income realized on the share due to its increase in value would be fully offset under the hedge and the taxpayer would generally have paid no net income tax in respect of that share. In this context, the amendment generally limits a loss on the repurchase of a share to the excess, if any, of the mark-to-market cost of the share (in contrast to the original cost) over its redemption price.

Subsection 112(5.2) is also amended to correct a reference not previously updated. The existing incorrect reference in subparagraph (c) of the description of C to subsection 112(4.2) is corrected by changing the reference to subsection 112(4).

Example 1

In 2009, Bank A acquired 100 shares of XYZ Corporation, which represent less than 5% of the issued shares, at a price of $800. In January 2019, XYZ Corporation repurchased its 100 shares owned by Bank A pursuant to a private agreement for $1,400 when their trading price was also $1,400. At the time of the repurchase, the paid-up capital of the shares was $200 and their mark-to-market cost was $1,400. Over the course of Bank A's holding period, the shares were hedged with a taxable Canadian counterparty and Bank A received $200 of actual dividends on these shares.

The tax consequences of the share repurchase for Bank A would be as follows:

S. 84(3) Deemed Dividend Inclusion		*S. 142.5(1) Loss*	
Redemption price:	*$1,400*	*Redemption price:*	*$1,400*
(minus)		*(minus)*	
PUC:	*$200*	*S. 142.5(4) deduction:*	*$1,200*
		plus	
Deemed dividend:	*$1,200*	*S. 112(5.2) adjustment:*	*$1,200*
(minus)			
S. 112(1) deduction:	*$1,200*	*Adjusted POD:*	*$1,400*
		(minus)	
Net dividend inclusion:	*nil*	*MTM cost:*	*$1,400*
		Deductible loss:	*nil*

In particular, given that the shares were not repurchased in the "open market", Bank A is deemed under subsection 84(3) to have received a dividend equal to the excess of the redemption price over the paid-up capital of the shares. Bank A claims an inter-corporate dividend deduction under subsection 112(1) on that deemed dividend. This inter-corporate dividend deduction would generally be available to the extent there is no "dividend rental arrangement" of Bank A in respect of the shares.

In calculating its proceeds, Bank A deducts the amount of the deemed dividend under subsection 84(3) from the redemption price under new subsection 142.5(4).

In these circumstances, amended subsection 112(5.2) will increase the proceeds otherwise determined by the amount of the deemed dividend under subsection 84(3).

The amount of actual dividends received on the shares is not included in the adjustment made under subsection 112(5.2) because the dividends qualify as excluded dividends under subsection 112(5.21). New subsection 112(9.1) would apply to ensure that the shares meet the 365-day holding period requirement in subsection 112(5.21) even though they were hedged during the entire period they were held by Bank A.

Example 2

Assume the same facts as Example 1 except that both the redemption price and the trading price of the shares at the time of repurchase are $1,500.

The tax consequences of the share repurchase for Bank A would be as follows:

S. 84(3) Deemed Dividend Inclusion		*S. 142.5(1) Loss*	
Redemption price:	*$1,500*	*Redemption price:*	*$1,500*
(minus)		*(minus)*	
PUC:	*$200*	*S. 142.5(4) deduction:*	*$1,300*
		plus	
Deemed dividend:	*$1,300*	*S. 112(5.2) adjustment:*	*$1,300*
(minus)			
S. 112(1) deduction:	*$1,300*	*Adjusted POD:*	*$1,500*
		(minus)	
Net dividend inclusion:	*nil*	*MTM cost:*	*$1,400*
		Profit inclusion:	*$100*

In this example, the shares have increased $100 in value from the last year-end of Bank A when their mark-to-market cost was determined to the repurchase date in January 2019. To the extent that the shares were hedged during that stub period, Bank A would have realized a $100 loss under the hedge. The profit inclusion of $100 under subsection 142.5(1) offsets that $100 loss.

For more information, see the commentary on subsection 112(5.21) and new subsections 112(9.1) and 142.5(4).

This amendment applies in respect of dispositions that occur on or after February 27, 2018.

Subsection (5.2) – excluded dividends

ITA

112(5.21)

Subsection 112(5.21) of the Act provides an exception to the stop-loss rule under subsection 112(5.2). This exception applies where a dividend was received on a share that the taxpayer held throughout the 365-day period that ended immediately before the disposition of the share and when the taxpayer and persons with whom the taxpayer did not deal at arm's length held in total

5% or less of the issued shares of any class of the capital stock of the dividend-paying corporation. This exception is limited to cases where the taxpayer received dividends on the share other than under subsection 84(3).

Subsection 112(5.1) is amended to replace a reference in its preamble to paragraph (b) of the description of B in subsection 112(5.2) with a reference to subparagraph (b)(ii) of the description of B in subsection 112(5.2). This amendment is consequential on an amendment to subsection 112(5.2).

For more information, see the commentary on subsection 112(5.2).

This amendment applies in respect of dispositions that occur on or after February 27, 2018.

Exception

ITA

112(9.1)

New subsection 112(9.1) provides an exception to the holding period test under subsection 112(8).

Subsection 112(8) provides that, if a synthetic disposition arrangement is entered into in respect of a property owned by a taxpayer and the synthetic disposition period in respect of the synthetic disposition arrangement is 30 days or more, then for the purposes of the listed exceptions to the stop-loss rules, the taxpayer is deemed not to own the property during the synthetic disposition period.

Subsection 112(9.1) provides that subsection 112(8) does not apply for the purpose of the 365-day ownership requirement under paragraph 112(5.21)(b) in respect of a dividend received on a share referred to in paragraph (a) of the description of B in subsection 112(5.2) during a synthetic disposition period of a synthetic disposition arrangement in respect of that share.

The exception under new subsection 112(9.1) is intended to ensure that an actual dividend received on a share prior to its repurchase, which absent the application of subsection 112(8) would qualify as an excluded dividend under subsection 112(5.21), will not increase the proceeds of disposition otherwise determined pursuant to subsection 112(5.2) unless a synthetic disposition arrangement with respect to the share was entered into after the payment of the actual dividend in order to meet the 365-day ownership requirement under paragraph 112(5.21)(b).

For more information, see the commentary on subsection 112(5.2).

This amendment applies in respect of dispositions that occur on or after February 27, 2018.

Clause 14

Proceeds – mark-to-market property

ITA

142.5(4)

New subsection 142.5(4) of the Act clarifies that the proceeds from the disposition of a share that is mark-to-market property of a financial institution do not include any amount that is deemed by subsection 84(2) or (3) to be a dividend received in respect of the share and that is not deemed by subparagraph 88(2)(b)(ii) not to be a dividend.

For more information, see the commentary on subsection 112(5.2).

This amendment applies in respect of dispositions that occur on or after February 27, 2018.

At-Risk Rules for Tiered Partnerships

Clause 15

Tiered partnerships

ITA

96(2.01)

New subsection 96(2.01) of the Act reverses the effect of a 2017 decision of the Federal Court of Appeal (*R v Green*), in which the court held that at least certain portions of section 96 do not apply to partnerships.

Subsection 96(2.01) provides that, for the purposes of section 96, a partnership is a taxpayer. This subsection is introduced to ensure that all portions of section 96 could apply to a partnership that is itself a partner of another partnership.

This amendment applies to taxation years that end after February 26, 2018.

Limited partnership losses

ITA

96(2.1)

Subsection 96(2.1) of the Act deals with the losses of limited partnerships. This subsection generally limits the deduction by a limited partner of losses to the extent of the limited partner's "at-risk amount" in respect of a partnership at the end of the fiscal period of the partnership ending in that year.

Paragraph 96(2.1)(e) is amended to ensure that a limited partner that is itself a partnership is not

deemed to have a limited partnership loss for the amount of losses rendered non-deductible by subsection 96(2.1) and cannot carry forward a limited partnership loss under paragraph 111(1)(e).

Paragraph 96(2.1)(f) provides that for a partnership that is a limited partner of another partnership, the losses from the other partnership that can be allocated to the partnership's members is restricted by that partnership's at-risk amount in respect of the other partnership. For the purposes of the calculation of the total of the amounts of the limited partner's share of the losses from the other partnership in paragraph 96(2.1)(a), this amount is to be determined without reference to the denial of a loss in paragraph (f).

This amendment applies to taxation years that end after February 26, 2018.

Tiered partnerships – adjustments

ITA

96(2.11)

New subsection 96(2.11) of the Act provides that an ultimate partner in a tiered partnership structure cannot deduct under section 111 in a taxation year that ends after February 26, 2018 partnership losses incurred in a taxation year that ended prior to February 27, 2018 that would have been reduced if subsection 96(2.01) and paragraph 96(2.1)(f) applied.

The adjusted cost base to the ultimate partner of a partnership interest in the tiered partnership structure will be increased by the amount that was denied as a deduction under section 111 by new paragraph 96(2.11)(a) to the extent that the amount can reasonably be considered to relate to an amount that was a loss previously deducted from the adjusted cost base under subparagraph 53(2)(c)(i). This subsection applies only to taxpayers that are not partnerships.

This new subsection is intended to preclude retrospective planning to carry forward losses arising in taxation years that ended before February 27, 2018.

Cross-Border Surplus Stripping using Partnerships and Trusts

Clause 16

Definition "equity amount"

ITA
18(5)

Subsection 18(5) of the Act defines certain expressions, including the term "equity amount", for the purposes of the "thin capitalization" rules in subsections 18(4) to (8).

Subparagraph (a)(ii) of the definition "equity amount" is amended to exclude any portion of a corporation's contributed surplus that arose at a time when the corporation was non-resident.

The definition is also amended to exclude any portion of a corporation's contributed surplus that arose in connection with a disposition to which subsection 212.1(1.1) applied because of subsection 212.1(1). Although the consequences under 212.1(1.1) would not apply to the extent contributed surplus arises, subsection 212.1(1.1) nevertheless applies where the conditions in paragraph 212.1(1) are met. As a result of this amendment, if a non-resident person disposes of shares of a subject corporation to a purchaser corporation for no consideration and the conditions in subsection 212.1(1) are met, any resulting contributed surplus will be excluded in determining the purchaser corporation's thin capitalization "room". In effect, this amendment puts contributed surplus on the same footing as paid-up capital (which is reduced under paragraph 212.1(1.1)(b)) for the purposes of the cross-border anti-surplus stripping rule in section 212.1.

These amendments apply in respect of transactions or events that occur after February 26, 2018.

Clause 17

Deemed dividend

ITA
84(1)(c.1) to (c.3)

Subsection 84(1) of the Act deems a dividend to have been paid by a corporation on the shares of a class of its capital stock where the paid-up capital of the class is increased by the corporation in circumstances other than those set out in that subsection. Paragraphs 84(1)(c.1) to (c.3) provide exceptions where the paid-up capital is increased by way of a conversion of contributed surplus in certain circumstances.

Paragraphs 84(1)(c.1) to (c.3) are amended to exclude any portion of a corporation's contributed surplus that arises at a time when the corporation is non-resident. Thus, a deemed dividend will now arise to the extent that contributed surplus created at a time when the corporation was non-resident is subsequently converted into paid-up capital at a time when the corporation is resident in Canada.

Paragraphs 84(1)(c.1) and (c.2) are also amended to exclude any portion of a corporation's contributed surplus that arises in connection with a disposition to which subsection 212.1(1.1) applies because of subsection 212.1(1). Thus, a deemed dividend will now arise to the extent that contributed surplus created in a non-arm's length sale of shares by a non-resident to which subsection 212.1(1.1) applies is converted into paid-up capital. For more information, see the commentary under the definition "equity amount" in subsection 18(5).

Paragraph 84(1)(c.3) is also amended by moving the reference to "subsection 212(1.1)" from subparagraph (i) to the portion of that paragraph before subparagraph (i). This amendment ensures that any portion of a corporation's contributed surplus that arises in connection with a disposition to which subsection 212.1(1.1) applies is excluded for purposes of paragraph 84(1)(c.3), regardless of whether the corporation issues shares in connection with the disposition.

These amendments apply in respect of transactions or events that occur after February 26, 2018.

Clause 18

Immigration

ITA
128.1

Section 128.1 of the Act sets out the income tax effects of becoming or ceasing to be resident in Canada.

Paragraph 128.1(1)(c.1) provides that if an immigrating corporation (Forco) at the time of immigration holds a share of a corporation resident in Canada (Canco), Canco is deemed to have paid a dividend to Forco immediately before the time at which Forco is deemed to dispose of its Canco shares as a result of its immigration. Generally, the deemed dividend is equal to the amount by which the fair market value of the share exceeds the paid-up capital in respect of the share, and is subject to non-resident withholding tax under Part XIII of the Act.

Section 128.1 is amended by adding new subsection 128.1(1.2), which contains a "look-through" rule for trusts and partnerships for the purpose of applying paragraph 128.1(1)(c.1). This rule is similar to, and is being added in connection with, the rule in new paragraph 212.1(6)(a), which is part of the new set of look-through rules being introduced to the anti-surplus stripping rules in section 212.1. For more information, see the commentary on new subsection 212.1(6).

New subsection 128.1(1.2) provides that, for the purposes of paragraph 128.1(1)(c.1), if shares of a corporation resident in Canada are owned by a trust or partnership (each referred to as a "conduit"), each person or partnership with an interest as a beneficiary under the conduit or that is a member of the conduit (each referred to as a "holder"), is deemed to own the shares in proportion to its interest in the conduit. More specifically, the holder is deemed to own the proportion of the number of shares of each class that are owned by the conduit that the fair market value of the holder's interest in the conduit is of the fair market value of all interests in the conduit.

If, for example, Forco holds a 50% interest in a conduit that owns 100 shares of Canco, subsection 128.1(1.2) will deem Forco to own 50 of the shares of Canco held by the conduit for the purpose of paragraph 128.1(1)(c.1). In certain circumstances, this could result in paragraph 128.1(1)(c.1) deeming Canco to have paid a dividend to Forco immediately before the time at which Forco is deemed to dispose of its Canco shares.

Because new subsection 128.1(1.2) applies also for purposes of itself, it will generally apply iteratively through tiers of conduits, thus ensuring that paragraph 128.1(1)(c.1) can apply in respect of tiered structures. For example, if Forco holds a 50% interest in a first conduit that holds a 50% interest in a second conduit that holds 100 shares of Canco, the first conduit would be deemed to hold 50% of the 100 shares of Canco held by the second conduit. Forco would then be deemed to hold 50% of the 50 shares of Canco that are deemed to be held by the first conduit. The end result would be that Forco would be deemed to hold 25 of the shares of Canco held by the second conduit.

This amendment applies in respect of transactions or events that occur after February 26, 2018.

Clause 19

Non-arm's length sales of shares by non-residents

ITA
212.1(1)

Subsection 212.1(1) of the Act, together with the operative rule in subsection 212.1(1.1), is an anti-avoidance rule designed to prevent the removal of corporate surplus – which would otherwise be subject to withholding tax under Part XIII of the Act upon distribution to a non-resident shareholder – as a tax-free return of capital or as proceeds from the disposition of the corporation's shares giving rise to a capital gain.

Subsection 212.1(1) sets out the conditions of application of subsection 212.1(1.1). In general terms, it provides that subsection 212.1(1.1) applies where shares of a Canadian corporation (the "subject corporation") held by a non-resident person or a designated partnership are transferred to another Canadian corporation (the "purchaser corporation") with which the transferor does not deal at arm's length and, immediately after the disposition, the subject corporation is connected (within the meaning that would be assigned by subsection 186(4), with certain modifications) with the purchaser corporation.

Subsection 212.1(1) is amended, in connection with the introduction of "look-through" rules for partnerships and trusts in new subsections 212.1(5) to (7)), to delete the reference to the term "designated partnership" (the definition of "designated partnership" in paragraph 212.1(3)(e) is also being deleted consequential on this amendment). This amendment, in combination with the new look-through rules, effectively extends the application of section 212.1 to dispositions of subject shares by partnerships that are not designated partnerships (as defined under existing paragraph 212.1(3)(e)) but that have one or more non-resident members, in circumstances where the other conditions in subsection 212.1(1) are met. For example, if a partnership with only one non-resident member (that has a minority interest in the partnership) disposes of subject shares to a purchaser corporation, for the purposes of subsections 212.1(1) and (1.1), new subsection 212.1(6) will deem the non-resident member (as well as any other members) to dispose of the subject shares to the purchaser in proportion to the relative fair market value of its partnership interest. Notably, however, in order for subsection 212.1(1.1) to apply to such a disposition, the non-resident member must not deal at arm's length with the purchaser corporation (including based on the expanded meaning of non-arm's length under paragraph 212.1(3)(a)).

Consequential on the deletion of the "designated partnership" reference, the defined term "non-resident person" is also deleted, as subsection 212.1(1) will apply only in respect of a non-resident person.

Subsection 212.1(1) is further amended, consequential on the introduction of the "look-through" rule in new subsection 212.1(6), to provide that, for the purpose of determining whether a subject corporation is connected with a purchaser corporation, subsection 186(4) is to be read without reference to subsection 186(6). This amendment ensures that the look-through rules in subsection 212.1(6) are used instead of the rules in subsection 186(6) for this purpose.

Non-arm's length sales of shares by non-residents

ITA
212.1(1.1)(a)

Subsection 212.1(1.1) of the Act sets out the operative rule that applies if the conditions in subsection 212.1(1) are satisfied.

Consequential on the amendment to subsection 212.1(1) eliminating the defined term "non-resident person", paragraph 212.1(1)(a) is amended to clarify that the reference in that paragraph to "the non-resident person" is to the non-resident person referred to in subsection 212.1(1), who disposes of (or is deemed to dispose of) the subject shares to the purchaser corporation.

Deemed consideration

ITA
212.1(1.2)

Subsection 212.1(1.2) of the Act provides a deemed consideration rule for the purposes of subsections 212.1(1) and (1.1), clarifying the application of those rules in situations where it may otherwise be uncertain whether consideration has been received by a non-resident person from a purchaser corporation in respect of the disposition by the non-resident person of subject shares.

Consequential on the amendment to subsection 212.1(1), which eliminates the defined term "non-resident person", subsection 212.1(1.2) is amended to ensure that its reference to the "non-resident person" is to the non-resident person referred to in subsection 212.1(1), who disposes of (or is deemed to dispose of) the subject shares to the purchaser corporation.

Relationship rules

ITA
212.1(3)

Subsection 212.1(3) of the Act sets out certain interpretive rules for the purpose of applying section 212.1.

Paragraph 212.1(3)(a) deems certain persons to not deal at arm's length for the purpose of applying section 212.1. Paragraph 212.1(3)(b) provides rules that, for the purposes of paragraph 212.1(3)(a), deem a non-resident person to own shares that are owned by certain other (generally, related) persons or partnerships.

Paragraphs 212.1(3)(a) and (b) are amended, consequential on the amendments to subsection 212.1(1), to remove the references to the term "designated partnership", as this is no longer a relevant concept or defined term for the purposes of section 212.1. The defined term "taxpayer" is also eliminated in paragraph 212.1(3)(b), consequential on the removal of the "designated partnership" references.

Paragraph 212.1(3)(e) defines "designated partnership" as a partnership in respect of which a majority interest partner or every member of a majority interest group of partners is a non-

resident person. Paragraph 212.1(3)(e) is repealed, consequential on the deletion of the reference to “designated partnership” in subsection 212.1(1).

For more information, see the commentary on subsection 212.1(1).

Where section does not apply

ITA
212.1(4)(b)

Subsection 212.1(4) of the Act provides a relieving exception to the rules in section 212.1 that applies in respect of a disposition by a non-resident corporation of shares of a subject corporation to a purchaser corporation that, immediately before the disposition, controlled the non-resident corporation.

Subparagraph 212.1(4)(b)(i) is amended by replacing the word “owns” with the word “held” for consistency within section 212.1.

Tiered trusts and partnerships

ITA
212.1(5)

New subsection 212.1(5) of the Act is a “look-through” rule for tiered trusts and partnerships (*i.e.*, trusts or partnerships that are themselves beneficiaries under trusts or members of partnerships). It is intended to apply to a tiered structure that includes any combination of trusts and partnerships in any number of tiers.

Paragraph 212.1(5)(a) looks through tiers of partnerships and trusts for the purpose of determining whether a person or partnership is a beneficiary of a lower-tier trust or a member of a lower-tier partnership. It ensures that

- a beneficiary of a trust that is itself a beneficiary of another trust will be deemed to be a beneficiary of the other trust;
- a beneficiary of a trust that is a member of a partnership will be deemed to be a member of the partnership;
- a member of a partnership that is a beneficiary of a trust will be deemed to be a beneficiary of the trust; and
- a member of a partnership that is a member of another partnership will be deemed to be a member of the other partnership.

Paragraph 212.1(5)(b) looks through tiers of partnerships and trusts for the purpose of determining the interest the beneficiary of the upper-tier trust or member of the upper-tier partnership is considered to have in the lower-tier trust or partnership. In effect, it deems the upper-tier beneficiary or member to hold a direct interest in the lower-tier trust or partnership that is equivalent to the interest it actually holds indirectly through tiers.

The one exception to the look-through rules for trusts and partnerships in subsection 212.1(5) is for a trust that is the non-resident person referred to in subsection 212.1(1) (*i.e.*, the non-resident that disposes of the subject shares to the purchaser corporation). Since a disposition by such a trust is within the scope of subsection 212.1(1) (*i.e.*, because it is a non-resident person), looking through such a trust would lead to inappropriate results under section 212.1 in certain circumstances.

While new subsection 212.1(5) applies for the purposes of section 212.1 as a whole, it is most relevant for the application of the ownership attribution rules in paragraphs 212.1(3)(b) and (c), and the look-through rules for trusts and partnerships in new subsections 212.1(6) and (7). Where a disposition or acquisition of subject shares is mediated by a tiered structure, it is intended that subsection 212.1(5) apply first, for the purposes of determining the identities and relative interests of trust beneficiaries or partnership members, and then subsection 212.1(6) be applied based on such determinations.

Trusts and partnerships look-through rule

ITA
212.1(6)

New subsection 212.1(6) of the Act contains “look-through” rules for trusts and partnerships for the purposes of subsections 212.1(1) and (1.1). These rules are intended to ensure that those subsections apply appropriately – and taxpayers cannot avoid, or obtain a more favourable result under, subsection 212.1(1.1) – where shares of a Canadian-resident corporation are held, disposed of or acquired through or by one or more trusts or partnerships.

Subsection 212.1(6) is, in general terms, organized as follows:

- Paragraph (a) looks through trusts and partnerships to attribute ownership of shares of a corporation resident in Canada to their beneficiaries or members;
- Where a trust or partnership holds shares of a corporation resident in Canada, paragraph (b) treats a disposition or acquisition of an interest in the trust or partnership as a disposition or acquisition of the shares by its beneficiaries or members;
- Paragraph (c) treats a disposition of shares of a corporation resident in Canada by a partnership as a disposition of the shares by its members; and
- Where a partnership or trust acquires shares of a corporation resident in Canada, paragraph (d) treats the acquisition an acquisition of the shares by its beneficiaries or members.

Paragraph 212.1(6)(a) provides that if shares of a corporation resident in Canada are owned by a trust (other than the non-resident person referred to in subsection 212.1(1)) or a partnership (referred to as a “conduit”), each beneficiary or member of the conduit (referred to as a “holder”), as the case may be, is deemed to own the shares in proportion to its interest in the conduit. More specifically, the holder is deemed to own the proportion of the number of shares of each class that are owned by the conduit that the fair market value of the holder’s interest in the conduit is of the fair market value of all interests in the conduit.

Paragraph 212.1(6)(a) is intended to apply primarily for the purpose of determining whether a subject corporation is connected with a purchaser corporation (within the meaning of 186(4), with certain modifications), as required under subsection 212.1(1), where the shares of the subject corporation are held by the purchaser corporation through one or more conduits. It is intended that, by deeming the holders to own, proportionately, the actual shares owned by the conduit, the holders will be considered to hold any rights attaching to those shares (*e.g.*, the voting rights attached to the shares).

Paragraph 212.1(6)(a) expressly does not apply in respect of a trust that is the non-resident person referred to in subsection 212.1(1) (*i.e.*, the non-resident that disposes of the subject shares to the purchaser corporation). Looking through such a trust may lead to inappropriate results under section 212.1 in certain circumstances.

The references to "interests" in subsection 212.1(6) are to interests as a beneficiary under a trust or as a member of a partnership. In addition, in the case of a structure involving tiers of trusts or partnerships (or both), the identities and interests of the beneficiaries of a trust or members of a partnership for the purposes of subsection 212.1(6) are to be determined under subsection 212.1(5). For more information, see the commentary on subsection 212.1(5).

Paragraph 212.1(6)(b) applies if a holder disposes of an interest in a conduit (referred to as the "pertinent interest") and any portion of the fair market value of the interest is attributable to shares of a corporation resident in Canada held, directly or indirectly, by the conduit (referred to as the "shares held by the conduit"). If paragraph 212.1(6)(b) applies, then the holder is deemed to have:

- disposed of, and the purchaser is deemed to have acquired, the shares held by the conduit in the proportion that the portion of the fair market value of the pertinent interest that is attributable to the shares held by the conduit is of the total fair market value of the shares held by the conduit; and
- received from the purchaser (and the purchaser is deemed to have paid to the holder) consideration for the shares that are deemed to have been disposed of by the holder. This deemed consideration is equal to the proportion of the fair market value of the consideration actually received by the holder from the purchaser for the pertinent interest that the portion of the fair market value of the pertinent interest that is attributable to the shares held by the conduit is of the total fair market value of the pertinent interest.

It is intended that, under paragraph 212.1(6)(b), each holder or purchaser is deemed to dispose of or acquire, as the case may be, a proportionate number of the shares held by the conduit, rather than a proportion of each such share. In this respect, the deeming rules in paragraphs 212.1(6)(c) and (d) are intended to apply with similar effect to paragraph 212.1(6)(b).

The dispositions are deemed to occur on a class-by-class basis. And so, if a conduit disposes of multiple classes of shares, the formula is applied so that the holder is deemed to dispose of a portion of each such class.

Paragraph 212.1(6)(c) provides that if a partnership disposes of shares of a corporation resident in Canada to a purchaser, then each member of the partnership is deemed to have:

- disposed of the shares to the purchaser in the proportion that the fair market value of the member’s interest in the partnership is of the total fair market value of all interests in the partnership, and
- received from the purchaser (and the purchaser is deemed to have paid to each member) consideration for the shares that are deemed to have been disposed of by the member. This deemed consideration is equal to the proportion of the fair market value of the consideration actually received by the partnership from the purchaser for the shares that the fair market value of the member’s interest in the partnership is of the total fair market value of all interests in the partnership.

Paragraph 212.1(6)(c) applies to dispositions by partnerships, but not by trusts, because subsections 212.1(1) and (1.1) already apply in respect of dispositions of shares of Canadian-resident corporations by trusts; looking through disposing trusts would provide inappropriate results in certain cases.

Paragraph 212.1(6)(c) amends the scheme under section 212.1 that applies to dispositions of shares of Canadian-resident corporations by partnerships. Under existing subsection 212.1(1), subsection 212.1(1.1) applies only in respect of dispositions by designated partnerships (as defined in paragraph 212.1(3)(e)). By contrast, the new look-through rule in paragraph 212.1(6)(c), in combination with the elimination of the “designated partnership” concept in section 212.1, extends the application of subsection 212.1(1.1) to dispositions by partnerships that are not (under the current rules) designated partnerships but that have one or more non-resident members, in circumstances where the other conditions in subsection 212.1(1) are met. For more information, see the commentary on subsection 212.1(1).

Paragraph 212.1(6)(d) provides that if a conduit acquires shares of a corporation resident in Canada from a vendor, then each holder of an interest in the conduit is deemed to have:

- acquired the shares from the vendor in the proportion that the fair market value of the holder’s interest in the conduit is of the total fair market value of all interests in the conduit, and
- paid to the vendor (and the vendor is deemed to have received from each such holder) consideration for the shares that are deemed to have been acquired by the holder. This deemed consideration is equal to the proportion of the fair market value of the consideration actually paid by the conduit to the vendor for the shares that the fair market value of the holder’s interest in the conduit is of the total fair market value of all interests in the conduit.

The deemed consideration rules in subparagraphs 212.1(6)(b)(ii), (c)(ii) and (d)(ii) do not apply in cases where shares of the purchaser corporation are issued as consideration for the subject shares. Rather, in such circumstances, paragraph 212.1(1.1)(b) applies to determine the amount of any paid-up capital reduction in respect of the shares of the purchaser corporation, without the need for a special deemed-consideration rule. Any use of one or more trusts or partnerships (*e.g.*, with one or more Canadian-resident beneficiaries or members) in order to increase the paid-up capital of shares through the interaction of the new look-through rules in subsection 212.1(6) with the rule in paragraph 212.1(1)(b) that provides for a reduction of paid-up capital, would be contrary to the policy underlying subsection 212.1(6) and, more generally, section 212.1.

Avoidance of subsections (5) and (6)

ITA
212.1(7)

New subsection 212.1(7) of the Act is an anti-avoidance rule predicated on the general policy against the use of discretionary or similar interests to avoid certain tax consequences. More particularly, subsection 212.1(7) is intended to prevent taxpayers from using discretionary interests in trusts with a view to circumventing the application of the look-through rules in new subsection 212.1(5) or (6) (*e.g.*, by taking the position that the fair market value of an interest as a beneficiary under a trust is nil or nominal because it is a discretionary interest in the trust).

Subsection 212.1(7) applies if

- the share, of a beneficiary under a trust, of the accumulating income or capital of the trust depends on the exercise by any person of, or the failure by any person to exercise, any discretionary power; and
- it can reasonably be considered that one of the reasons the discretionary power is conferred on the person is to avoid or limit the application of subsection 212.1(1.1).

The foregoing conditions of application reflect a concern that taxpayers may, in the absence of subsection 212.1(7), take discretionary interests in trusts in an attempt to mitigate or avoid certain results under the look-through rules that are based on the relative fair market value of an interest in a trust. To prevent this, new subsection 212.1(7) effectively deems a beneficiary under a trust to hold or acquire, as the case may be, all of the property held or acquired by the trust in certain circumstances. This result is achieved by deeming the beneficiary to have a 100% interest in the trust for the purposes of paragraphs 212.1(5)(b) and (6)(a) and subparagraph (6)(d)(i).

Coming-into-force

The above amendments to section 212.1 apply in respect of dispositions that occur after February 26, 2018.

Foreign Affiliates

Tracking Arrangements – Investment Businesses and Controlled Foreign Affiliate Status

Clause 20

Non-resident corporation shares held by a partnership

ITA

93.1(1.1)

Where a Canadian-resident corporation owns shares of a non-resident corporation through a partnership, subsection 93.1(1) applies in determining whether the non-resident corporation is a foreign affiliate of the Canadian-resident corporation for the purposes of certain provisions of the Act and Regulations. In those circumstances, subsection 93.1(1) provides a look-through rule that deems the Canadian corporation to own its proportionate number of the non-resident corporation's shares based on the relative fair market value of its interest in the partnership. The rule also applies where a foreign affiliate of the Canadian corporation owns shares of another non-resident corporation through a partnership.

Subsection 93.1(1.1) lists the purposes for which the look-through rule in subsection 93.1(1) applies. Paragraph 93.1(1.1)(d) is being amended by adding a reference to subsections 95(8) to (12) so as to ensure that foreign affiliate status can flow through a partnership for the purposes of the tracking interest rules in those subsections.

This amendment applies after February 26, 2018.

Clause 21

Tracking interests - overview

ITA

95(8) to (12)

New subsections 95(8) to (12) address certain tax consequences under the foreign affiliate rules in the Act in relation to structures that use so-called "tracking arrangements" in respect of foreign affiliates of taxpayers. Tracking arrangements often involve the grouping of assets and activities of multiple shareholders in a common corporation in order to achieve certain tax benefits. In such arrangements, the assets contributed by the shareholders are not truly pooled or integrated within the corporation as the economic outcome for each shareholder in respect of their contributed assets is comparable to the outcome that would arise if the assets had continued to be held by the shareholder directly or had been contributed by each shareholder into separate, wholly-owned corporations. This "tracking" is often effected either through rights attaching to the shares of the common corporation (*i.e.*, separate share classes) or contractual arrangements with a similar effect.

Two specific measures are being introduced to ensure appropriate income tax consequences in cases where there is a tracking arrangement in respect of a foreign affiliate of a taxpayer. The

first deals with the avoidance of the "investment business" rules contained in subsection 95(1) – a significant component of the "foreign accrual property income" (FAPI) regime applicable to foreign affiliates of Canadian taxpayers. The second deals with the avoidance of immediate FAPI inclusions through the avoidance of "controlled foreign affiliate" status. These new rules are aimed at providing greater assurance that taxpayers cannot achieve unintended tax benefits under the foreign affiliate rules through the use of tracking arrangements.

Tracking interests – interpretation

ITA
95(8)

New subsection 95(8) is an interpretation rule applicable for the new rules dealing with tracking arrangements. It generally provides that, for the purposes of new subsections 95(9) to (11), a property constitutes a tracking interest in a person or partnership (referred to as the "tracked entity") if

- all or part of the fair market value of the property, or of any payment or right to receive an amount in respect of the property, can reasonably be considered to be determined, directly or indirectly, by reference to certain criteria (enumerated in subparagraphs 95(8)(a)(i) to (iv)) in respect of property and activities (referred to as the "tracked property and activities") of the person or partnership; and
- the tracked property and activities do not represent all of the property and activities of the person or partnership.

For example, a tracking interest will generally exist if a corporation's assets and activities are not fully pooled together for the benefit of all of its shareholders, such that one or more shareholders holds shares of a class that derive their value from only some, and not all, of the corporation's property and activities. The reference in paragraph 95(8)(a) to "any payment or right to receive an amount" is intended to capture cases where the value of the payment or right to receive the amount is not clearly reflected in the fair market value of the taxpayer's rights (referred to in the legislation as "property") in respect of the corporation. For example, this could include a discretionary interest in respect of the corporation.

The reference in paragraph 95(8)(a) to the fair market value of the property being determined "directly or indirectly" by reference to the enumerated criteria is intended to capture not only circumstances where the tracking is embedded in the terms of shares issued by the tracked entity, but also where the tracking is more indirect, such as through a chain of entities that includes the tracked entity or through contractual rights.

In determining whether a particular property or activity of a tracked entity is part of the tracked property and activities, what is relevant is not whether the value of the particular property or activity (or another criterion described in subparagraphs 95(8)(a)(i) to (iv) in respect of the property or activity) actually contributes to the fair market value of the tracking interest, but rather whether in principle it would so contribute if the particular property or activity had value. Thus, where, for example, the value of a particular property or activity does not contribute to the fair market value of shares of the tracked entity owned by a taxpayer because the particular

property or activity is of nil or indeterminate value, this would not in and of itself exclude the property or activity from being part of the tracked property and activities (*i.e.*, it would not lead to the conclusion that the tracked property and activities do not represent all of the tracked entity's property and activities such that the condition in paragraph 95(8)(b) is met).

Tracking interests –*investment business* definition

ITA
95(9)

Subsection 95(9) is one of the two main operative rules being introduced to address tracking arrangements in the context of foreign affiliates of Canadian taxpayers. It applies for the purpose of the "investment business" definition in subsection 95(1), to deem certain properties and activities that may otherwise be considered to be part of one business to instead constitute two or more separate businesses. As the investment business rules apply on a business-by-business basis, the intention is that the deeming of a separate business under subsection 95(9) will require, among other things, each separate business to satisfy the "more than five employees" condition in paragraph (c) of the "investment business" definition on its own in order to be excepted from the investment business rules.

In determining whether a deemed separate business meets the conditions for an exception from the "investment business" definition, the characteristics and components of the actual business are to be to attributed to the separate business on a reasonable basis (*e.g.*, the necessary employees for the property and activities forming the separate business are to be allocated to the separate business). If the separate business is determined to be an investment business, then income attributable to the tracked property and activities (*i.e.*, the property and activities of the separate business) is to be treated as income from an investment business, which is included in the "income from property" (as defined in subsection 95(1)) of a foreign affiliate of a taxpayer.

It is notable that in many circumstances, business activities that track separately to different tracking interests in a corporation would be expected to constitute separate businesses under general principles, even absent subsection 95(9); this new rule simply ensures this result in all cases involving tracking interests.

Tracking interests –controlled foreign affiliate

ITA
95(10)

New subsection 95(10) is one of the two main operative rules being introduced to address tracking arrangements in the context of foreign affiliates of Canadian taxpayers. It is intended to ensure that "controlled foreign affiliate" (CFA) status is not avoided where a taxpayer has a tracking interest in a foreign affiliate.

Tracking arrangements often involve the grouping of assets and activities of multiple shareholders in a common corporation in order to achieve certain tax benefits, but with the economic outcome – and often the degree of control – for each shareholder in respect of their

contributed assets and activities being comparable to a situation where the assets and activities had been contributed by each shareholder in separate, wholly-owned corporations. Where the corporation is a foreign affiliate of the taxpayer, it is generally appropriate that the affiliate be treated as a controlled foreign affiliate in these circumstances.

Subsection 95(10) deems a foreign affiliate of a taxpayer to be a CFA of the taxpayer throughout a taxation year of the affiliate if the following conditions are met:

- At any time in the year, the taxpayer holds a "tracking" interest in the affiliate or a partnership of which the affiliate is a member;
- The affiliate, or a lower-tier affiliate, has FAPI for the year; and
- No election under subsection 95(11) applies in respect of the affiliate for the year.

The intention is to subject such a foreign affiliate to immediate accrual taxation under the FAPI regime.

Subsection 95(10) is a general, default rule. It can be overridden by the elective "separate corporation" regime provided for in subsections 95(11) and (12). For more information, see the commentary on subsections 95(11) and (12).

Tracking class – separate corporation

ITA
95(11) and (12)

New subsections 95(11) and (12) provide an alternative to the deemed CFA rule in subsection 95(10). On an elective basis, these rules deem the property and activities of a foreign affiliate of a taxpayer that are tracked under the taxpayer's tracking interest in the affiliate to be a separate corporation, for certain purposes. Although these rules are elective, they are not meant to be used as a tax-planning tool.

Subsections 95(11) and (12) are intended to address two situations. First, the rules address the situation where a taxpayer would be unable to reasonably comply with the FAPI computational requirements of subsection 91(1) due to a lack of information as to the overall operations and income of a foreign affiliate. Electing under these rules allows the taxpayer to treat only the tracked property and activities (*i.e.*, the affiliate's property and activities that are tracked under the taxpayer's tracking interest) as a separate corporation in respect of which any FAPI required to be included in income under subsection 91(1) is determined. Second, the rules address the situation where the tracked portion of a foreign affiliate would not, if it had been a separate corporation, be a CFA of the taxpayer. Electing under these rules ensures that the affiliate does not become a CFA in these circumstances.

Subsection 95(11) provides the conditions for the application of the operative rule in subsection 95(12). In general terms, subsection 95(12) applies in respect of a foreign affiliate of a taxpayer for a taxation year of the affiliate if the affiliate would otherwise be a CFA of the taxpayer because of subsection 95(10), and

- The taxpayer holds at any time in the year a tracking interest in the affiliate;

- The tracking interest is shares of a class (referred to as the "tracking class") of the affiliate the fair market value of which can reasonably be considered to be determined by reference to the tracked property and activities of the affiliate; and
- The taxpayer duly elects for subsection 95(12) to apply in respect of the affiliate for the year.

Notably, while the concept of a "tracking interest" – and thus the default rule in subsection 95(10) that is based on that concept – is broad, the deemed separate corporation election in subsections 95(11) and (12) is only available in more limited circumstances, namely where the tracking arrangement is effected through a tracking class.

Where applicable, subsection 95(12) effectively

- deems the existence of a corporation that is separate from the actual corporation that has issued the shares of the tracking class (paragraph 95(12)(a));
- attributes to that separate corporation the tracked property and activities, any associated rights and obligations, and any income, losses or gains in respect of the tracked property and activities (paragraphs 95(12)(a) to (c)); and
- deems the separate corporation to be a "non-resident corporation without share capital" and the tracking class to be equity interests in the separate corporation, which is intended to trigger the application of section 93.2 to create the share structure of the separate corporation for the purpose of attributing the appropriate amount of FAPI under subsection 91(1) (paragraphs 95(12)(a), (d) and (e)).

The overall effect of these separate corporation rules is twofold. First, as noted above, they ensure that a tracked portion of a foreign affiliate that would not, if it had been a separate corporation, be a CFA of the taxpayer does not become one under the default rule of subsection 95(10). This follows from paragraph 95(12)(d) deeming the shares of the tracking class to be equity interests in the separate non-share capital corporation, which, in combination with the rules in section 93.2, allows for the possibility that a particular taxpayer may have a minority interest in the separate corporation.

Second, where the deemed separate corporation is a CFA and is therefore subject to immediate accrual taxation in respect of its FAPI, the deeming rules in subsection 95(12)

- facilitate the computation of that FAPI and the determination of the portion to be attributed to the taxpayer under subsection 91(1);
- allow for the determination of any deductions available to the taxpayer under subsection 91(4) in respect of foreign tax paid; and
- allow for the determination of the taxpayer's reporting obligations under section 233.4, generally requiring the taxpayer to report on the separate corporation using the more detailed reporting requirements applicable to CFAs.

Otherwise, the normal rules in the Act in respect of foreign affiliates, in particular those dealing with the taxation of dividends received from a foreign affiliate, will continue to apply in respect of the actual affiliate. In order to ensure that amounts included in a taxpayer's income under

subsection 91(1) in respect of the separate corporation, and any related amounts deducted under 91(4), are properly integrated with the taxpayer's tax results in respect of the actual affiliate – and especially to avoid double taxation when amounts included in the FAPI of the separate corporation are ultimately distributed by the actual affiliate – paragraph 95(12)(f) deems such amounts to be included and deducted, respectively, by the taxpayer in respect of the tracking class of the actual affiliate. In particular, this is intended to ensure appropriate increases and deductions under subsection 92(1) to the adjusted cost base of shares of a foreign affiliate.

New subsections 95(8) to (12) apply to taxation years of a foreign affiliate of a taxpayer that begin after February 26, 2018.

Trading or Dealing in Indebtedness

Clause 22

Trading or dealing in indebtedness

ITA
95(2)(l)

Paragraph 95(2)(l) of the Act includes, in the income from property of a foreign affiliate of a taxpayer, the affiliate's income from a business if the principal purpose of the business is to derive income from trading or dealing in certain indebtedness (which includes the earning of interest on indebtedness). Generally, paragraph 95(2)(l) does not apply to the affiliate if two conditions are satisfied. The first condition requires that the business of the affiliate be described in subparagraph 95(2)(l)(iii) (*i.e.*, as a foreign bank, a trust company, a credit union, an insurance corporation or a trader or dealer in securities, the activities of which are, in general terms, locally regulated). The second condition requires that the taxpayer be a person or partnership described in any of clauses 95(2)(l)(iv)(A) to (D) (*i.e.*, a regulated Canadian financial institution, a subsidiary wholly-owned corporation of a regulated Canadian financial institution, a corporation of which a regulated Canadian financial institution is a subsidiary wholly-owned corporation or a partnership each member of which is such a corporation).

Paragraph 95(2)(l) is amended in three respects:

- The condition that the taxpayer be a person or partnership described in any of clauses 95(2)(l)(iv)(A) to (D) is repealed and is effectively replaced with the set of conditions in paragraphs 95(2.11)(a) and (b) (which are in the analogous exception from the "investment business" definition in subsection 95(1)). The latter is effected by amending subsection 95(2.11) such that its conditions apply also for purposes of subparagraph 95(2)(l)(iii). As a result of this amendment, to qualify for the exception from paragraph 95(2)(l), the taxpayer must be a regulated Canadian financial institution that meets a minimum threshold with respect to its equity or its taxable capital employed in Canada. For more information, see the commentary on subsection 95(2.11).

- Paragraph 95(2)(l) is amended to specify that, in order for the conditions in subparagraph 95(2)(l)(iii) to be met, it must be established by the taxpayer or the affiliate that the conditions are met throughout the period in the taxation year during which the business of trading or dealing in indebtedness is carried on by the affiliate. As with the first amendment above, this amendment better aligns the exception from paragraph 95(2)(l) with the exception from the "investment business" definition.
- Subparagraph 95(2)(l)(iii) is amended by adding a further condition that is also present in the exception from the "investment business" definition, namely the requirement that the affiliate's business of trading or dealing in indebtedness must be conducted principally with arm's length persons.

These amendments apply to taxation years of a foreign affiliate of a taxpayer that begin after February 26, 2018.

Rule for "investment business" definition and paragraph 95(2)(l)

ITA
95(2.11)

Subsection 95(2.11) of the Act provides that, for the purposes of the definition "investment business" in subsection 95(1), a taxpayer or a foreign affiliate of the taxpayer, as the case may be, is deemed not to have established that the requirements in subparagraph (a)(i) of that definition have been satisfied throughout a period in a taxation year of the affiliate, unless certain additional conditions set out in paragraphs 95(2.11)(a) and (b) have been met.

Subsection 95(2.11) is amended so that the additional conditions set out in paragraphs 95(2.11)(a) and (b) apply also in respect of subparagraph 95(2)(l)(iii). As a result, a taxpayer or a foreign affiliate of the taxpayer, as the case may be, is deemed not to have established that the conditions in subparagraph 95(2)(l)(iii) have been satisfied throughout a period in a taxation year of the affiliate, unless the additional conditions set out in paragraphs 95(2.11)(a) and (b) have been met.

In general, the rules respecting investment businesses (as defined in subsection 95(1)) and those respecting businesses of trading or dealing in certain indebtedness (under subsection 95(2)(l)) ensure that income from those businesses is treated as income from property, unless certain exceptions are met. This amendment is intended to ensure consistency among the exceptions to both sets of rules.

This amendment applies to taxation years of a foreign affiliate of a taxpayer that begin after February 26, 2018.

Reassessments

Clause 23

Assessment and reassessment – limitation period

ITA
152(4)(b)(iii)

Subsection 152(4) of the Act generally provides that the Minister of National Revenue may at any time assess tax and other amounts payable by a taxpayer for a taxation year, but may not assess after the normal reassessment period for the year. The normal reassessment period for a year is for corporations (other than Canadian-controlled private corporations) and mutual fund trusts, in general, four years from the date of the initial notice of assessment. For other taxpayers, it is, in general, three years from the date of the initial notice of assessment. Subsection 152(4) includes exceptions that apply in certain circumstances. These exceptions are described in paragraphs 152(4)(a) to (d).

Subparagraph 152(4)(b)(iii) allows the Minister to assess tax within an additional three year period, if the assessment of a taxpayer for a taxation year is made as a consequence of a transaction involving the taxpayer and a non-resident person with whom the taxpayer was not dealing at arm’s length. While this three-year extended reassessment period applies to many transactions involving foreign affiliates of a taxpayer, it does not apply in all such circumstances.

Subparagraph 152(4)(b)(iii) is amended by dividing it into clauses and by adding a new exception in clause (B), which permits the assessment of a taxpayer for a taxation year outside of the normal reassessment period, if the assessment is made in respect of any income, loss or other amount in relation to a foreign affiliate of the taxpayer. This amendment expands the circumstances under which subparagraph 152(4)(b)(iii) can apply in order to ensure that the Government has a reasonable opportunity to properly examine all activities in respect of foreign affiliates of a taxpayer that are relevant to the Canadian tax base.

This amendment applies to taxation years of a taxpayer that begin after February 26, 2018.

Extended period assessment

ITA
152(4.01)(b)(iii)

Subsection 152(4.01) limits the matters in respect of which the Minister of National Revenue can assess when an assessment to which paragraph 152(4)(a), (b), (b.1), (b.3), (b.4) or (c) applies is made beyond the normal reassessment period for a taxpayer in respect of a taxation year. In general terms, such a reassessment can be made only to the extent that it can reasonably be regarded as relating to a matter specified in any of paragraphs 152(4)(a), (b), (b.1), (b.3), (b.4) or (c), because of which the Minister is able to reassess beyond the normal reassessment period.

Subparagraph 152(4.01)(b)(iii) is amended consequential on the addition of its new clause (B), which allows the Minister to assess tax outside of the normal reassessment period for a taxation year of a taxpayer, if the assessment is made in respect of any income, loss or other amount in

relation to a foreign affiliate of the taxpayer. As such, the assessment for a taxation year, authorized to be made after the normal reassessment period by new clause 152(4)(b)(iii)(B), is limited by subparagraph 152(4.01)(b)(iii) to that which can reasonably be regarded as relating to the income, loss or other amount in relation to a foreign affiliate of a taxpayer.

This amendment applies to taxation years of a taxpayer that begin after February 26, 2018.

Reporting Requirements

Clause 24

Returns respecting foreign affiliates

ITA
233.4(4)

Section 233.4 establishes reporting requirements in respect of foreign affiliates. In general terms, it provides that taxpayers resident in Canada (or certain partnerships), of which a non-resident corporation is a foreign affiliate, must file an information return in respect of the affiliate. The entity required to file this information return is defined by the expression "reporting entity" for the purposes of section 233.4.

Subsection 233.4(4) requires a reporting entity for a taxation year or fiscal period to file an information return in prescribed form (T1134) in respect of each foreign affiliate of the entity in the year or period. The filing deadline for the information return is 15 months after the end of the reporting entity's taxation year or fiscal period.

Subsection 233.4(4) is amended to provide that the new filing deadline for this prescribed information return is six months after the end of a reporting entity's taxation year or fiscal period.

This amendment applies to taxation years or fiscal periods of a reporting entity that begin after 2019.

Foreign Divisive Reorganizations

Clause 25

Division of corporation under foreign laws

ITA

15(1.4)(e)

Paragraph 15(1.4)(e) of the Act deems a non-resident corporation (the "original corporation") to have conferred a benefit on its shareholder if, among other conditions, the original corporation is divided under the laws of the foreign jurisdiction that govern the original corporation and the

shareholder acquires a share of another corporation as a consequence of the division of the original corporation.

Paragraph 15(1.4)(e) is repealed consequential on the introduction of new subsection 15(1.5). For more information, see the commentary on new subsection 15(1.5).

This amendment applies in respect of divisions that occur after October 23, 2012.

Division of corporation under foreign laws

ITA

15(1.5)

New subsection 15(1.5) of the Act provides deeming rules for certain foreign divisive reorganizations. Although paragraph 15(1.5)(a) is situated among the shareholder benefit provisions in section 15, it applies for the purposes of the Act more generally. These rules are intended to provide greater certainty with respect to various tax consequences arising from these transactions. New subsection 15(1.5) replaces paragraph 15(1.4)(e), which is repealed.

Subsection 15(1.5) generally applies to transactions in which a non-resident corporation (the “original corporation”) undergoes a division under foreign law that meets certain conditions. First, the division must result in all or part of its assets and liabilities becoming assets and liabilities of one or more other non-resident corporations (each, a “new corporation”). Second, as a consequence of the division, a shareholder of the original corporation must acquire one or more shares of a new corporation. An example of a transaction contemplated by subsection 15(1.5) is a division (or “escisión”) of a corporation under Mexican law.

The deeming rules in paragraph 15(1.5)(a) address the consequences to a shareholder of the original corporation acquiring shares of the new corporation on a division, but only to the extent that none of the exceptions (from the shareholder-benefit inclusion under subsection 15(1)) in subparagraphs 15(1)(a.1)(i) to (iii) or paragraph 15(1)(b) applies. To the extent that the rules in paragraph 15(1.5)(a) apply, they provide that, depending on the circumstances, a shareholder is considered to have received either a dividend-in-kind or shareholder benefit. The amount of the dividend-in-kind or benefit is equal to the fair market value, immediately after acquisition, of the shares of the new corporation acquired by the shareholder on the division. More specifically, clause 15(1.5)(a)(i)(A) deems the original corporation to have distributed, and a particular shareholder of the original corporation to have received, a dividend-in-kind if the shares of the new corporation are received by shareholders of each class of shares of the original corporation on a *pro rata* basis.

If the conditions in subparagraph 15(1.5)(a)(i) are not met, subparagraph 15(1.5)(a)(ii) deems the original corporation to have conferred a benefit on the shareholder equal to the total fair market value of the shares of the new corporation acquired by the shareholder on the division. The amount of this shareholder benefit is to be included in the shareholder’s income in accordance with subsection 15(1). However, as noted above, subparagraph 15(1.5)(a)(ii) does not deem a shareholder benefit to the extent that any of subparagraphs 15(1)(a.1)(i) to (iii) and paragraph 15(1)(b) apply to the acquisition of the shares of the new corporation.

Paragraph 15(1.5)(b) deems any gain or loss of the original corporation from the distribution of shares of the new corporation, as a consequence of the division, to be nil. In particular, this ensures that, if the original corporation is considered to distribute the shares of the new corporation as a dividend-in-kind – whether because of the application of clause 15(1.5)(a)(i)(A) or otherwise – any gain or loss resulting from the consequent application of subsection 52(2) will be deemed to be nil.

Paragraph 15(1.5)(c) provides that each property of the original corporation that becomes property of the new corporation as a consequence of the division is deemed to be

- disposed of by the original corporation for proceeds of disposition equal to its fair market value; and
- acquired by the new corporation at a cost equal to the amount of those proceeds of disposition.

Deemed dispositions under paragraph 15(1.5)(c) can give rise to tax consequences under the Act (*e.g.*, where the property disposed of is taxable Canadian property, or the original corporation is a foreign affiliate of a taxpayer). In order to ensure that appropriate consequences under the foreign affiliate surplus regulations result from such dispositions, amendments are being made to the definition “designated person or partnership” in subsection 5907(1) of the *Regulations*, and a new rule is being introduced in subsection 5907(2.011) (with consequential changes to subparagraphs 5907(2)(f)(ii) and (j)(iii)). For more information, see the commentary on those provisions.

Subsection 15(1.5) applies in respect of divisions that occur after October 23, 2012.

Clause 26

Interpretation

ITR
5907

Section 5907 of the Regulations provides definitions and rules of interpretation for the purposes of Part LIX of the Regulations and also prescribes certain rules for particular foreign affiliate provisions of the Act.

Definitions

ITR
5907(1)

“designated person or partnership”

The definition “designated person or partnership” generally identifies certain non-arm’s length persons or partnerships in relation to a taxpayer. This definition is amended consequential on the introduction of new subsection 15(1.5) of the Act.

Subsection 15(1.5) provides rules that apply if, among other conditions, a non-resident corporation (the "original corporation") governed by the laws of a foreign jurisdiction undergoes a division under those laws that results in all or part of its assets and liabilities becoming assets and liabilities of one or more other non-resident corporations (each, a "new corporation"). For more information, see the commentary on new subsection 15(1.5).

The definition "designated person or partnership" is amended to explicitly include a new corporation in respect of a division under subsection 15(1.5), to ensure that the definition is met in the case of every foreign divisive reorganization to which subsection 15(1.5) applies.

The definition "designated person or partnership" supports various provisions in section 5907 of the Regulations. For example, in general terms, under the anti-avoidance rule in existing subsection 5907(2.02) of the Regulations, if a disposition of property (other than money) by a foreign affiliate of a taxpayer to a "designated person or partnership", in respect of the taxpayer, is an "avoidance transaction" (as defined in subsection 245(3) of the Act), any resulting increase in "exempt earnings" is reclassified to "taxable earnings". In this context, the purpose of the disposition may be relevant. In applying subsection 5907(2.02) in relation to a division described in new subsection 15(1.5), because the deemed disposition of property under subparagraph 15(1.5)(c)(i) by the original corporation to a new corporation (which, under this amendment, is a designated person in respect of the taxpayer) occurs in the context of the division, the purpose of the deemed disposition would be expected to be determined by reference to the purpose of the division – and, in particular, to the purpose of assets and liabilities of the original corporation becoming assets and liabilities of the new corporation in the course of the division.

This amendment comes into force on Announcement Date.

ITR
5907(2)(f)(ii)

In general terms, paragraph 5907(2)(f) of the Regulations provides for additions to "earnings" (as defined in subsection 5907(1) of the Regulations) of certain items of revenue, income or profit that are not otherwise included in earnings under the relevant foreign tax law. Existing subparagraph 5907(2)(f)(ii) provides an exception to this addition in certain circumstances in which, generally, a foreign tax rollover rule applies on a disposition to a "designated person or partnership" (as defined in subsection 5907(1) of the Regulations) in respect of a taxpayer.

Subparagraph 5907(2)(f)(ii) is amended, consequential on the introduction of new subsection 5907(2.011), to make it subject to subsection 5907(2.011) so that the exception in subparagraph 5907(2)(f)(ii) does not apply in the case of a deemed disposition of property under subparagraph 15(1.5)(c)(i) by an original corporation to a new corporation (both within the meaning of subsection 15(1.5)) to which subsection 5907(2.011) applies. For more information, see the commentary on subsection 5907(2.011).

This amendment applies in respect of dispositions that occur after October 23, 2012.

ITR
5907(2)(j)(iii)

In general terms, paragraph 5907(2)(j) of the Regulations provides for reductions to "earnings" (as defined in subsection 5907(1) of the Regulations) of certain amounts that are otherwise included (or not deducted) in computing earnings under the relevant foreign tax law. Existing subparagraph 5907(2)(j)(iii) provides an exception to this reduction in certain circumstances in which, generally, a foreign tax rollover rule applies on a disposition to a "designated person or partnership" (as defined in subsection 5907(1) of the Regulations) in respect of a taxpayer.

Subparagraph 5907(2)(j)(iii) is amended, consequential on the introduction of new subsection 5907(2.011), to make it subject to subsection 5907(2.011) so that the exception in subparagraph 5907(2)(j)(iii) does not apply in the case of a deemed disposition of property under subparagraph 15(1.5)(c)(i) by an original corporation to a new corporation (both within the meaning of subsection 15(1.5)) to which subsection 5907(2.011) applies. For more information, see the commentary on subsection 5907(2.011).

This amendment applies in respect of dispositions that occur after October 23, 2012.

ITR
5907(2.011)

New subsection 5907(2.011) of the Regulations is added, in connection with the introduction of new subsection 15(1.5), to override the tax rollover exceptions in subparagraphs 5907(2)(f)(ii) and (j)(iii) and subsection 5907(5.1), in certain specified circumstances. These circumstances (which are outlined below) are similar to the circumstances in which existing subsection 5907(2.01) overrides those rollover exceptions.

Generally, subsection 15(1.5) provides rules that apply if, among other conditions, a non-resident corporation (the "original corporation") governed by the laws of a foreign jurisdiction undergoes a division under those laws that results in all or part of its assets and liabilities becoming assets and liabilities of one or more other non-resident corporations (each, a "new corporation"). Among other consequences of such a division, subparagraph 15(1.5)(c)(i) deems each property of the original corporation that becomes property of a new corporation as a consequence of the division to be disposed of by the original corporation to the new corporation for proceeds of disposition equal to its fair market value.

New subsection 5907(2.011) ensures that any unrealized value in the properties that are deemed to be disposed of by the original corporation to a new corporation under subparagraph 15(1.5)(c)(i) will be eligible for surplus recognition provided, among other conditions, the shares of the new corporation are sold within 90 days to a person or partnership that is not a designated person or partnership (as defined in subsection 5907(1)) in respect of the taxpayer.

This new rule is intended to apply to transactions that would otherwise be structured as direct asset sales but that are instead, for foreign commercial reasons, structured as share sales. Where such transactions are so structured primarily for Canadian tax reasons, they could be subject to the anti-avoidance rule in subsection 5907(2.02). For more information, see the commentary on the amendment to the definition "designated person or partnership" in subsection 5907(1).

This amendment applies in respect of dispositions that occur after October 23, 2012.

Passive Investment Income – Allocation of Losses

Clause 27

Part IV tax – allocation of losses

ITA

129(4.1) and (4.2)

New subsections 129(4.1) and (4.2) of the Act are introduced consequential to the introduction of the eligible refundable dividend tax on hand (ERDTOH) and non-eligible refundable dividend tax on hand (NERDTOH) accounts. These new subsections provide an allocation rule for situations in which losses are claimed by a corporation to partly reduce its Part IV taxes otherwise payable and those Part IV taxes would otherwise be added to both ERDTOH and NERDTOH.

Based on the conditions set out in subsection 129(4.1), subsection 129(4.2) will apply in respect of a taxation year of a corporation if the corporation

- has an amount of tax payable for the year under Part IV;
- has claimed amounts under paragraph 186(1)(c) or (d) in respect of the year; and
- would, in the absence of paragraphs 186(1)(c) and (d), have an amount determined, at the end of the year, under both paragraph (a) of the ERDTOH definition and paragraph (b) of the NERDTOH definition in subsection 129(4).

When it applies, subsection 129(4.2) allocates a corporation's non-capital loss and farm loss claims in respect of Part IV taxes otherwise payable first to the amount otherwise added to its NERDTOH account. The excess is allocated the corporation's ERDTOH account.

Example 1:

A corporation receives a $100 eligible dividend and a $100 non-eligible dividend, both from non-connected corporations. In the absence of the utilization of any offsetting losses, the corporation would pay 38.33 per cent Part IV tax on each of these amounts, with $38.33 added to its ERDTOH account and $38.33 added to its NERDTOH account. However, if that same corporation also had a $150 non-capital loss that it chose to utilize, its Part IV taxes would be reduced by 38.33 per cent of the loss, or $57.50.

Subsection 129(4.2) will first allocate the losses claimed to reduce the amount allocated to the corporation's NERDTOH. In this example, as the tax-effected amount of the losses claimed ($57.50) exceeds the amount that would otherwise be allocated to the corporation's NERDTOH ($38.33), the NERDTOH addition is reduced to zero. The amount by which the losses claimed exceeds the amount that would otherwise be added to the corporation's NERDTOH ($57.50 - $38.33 = $19.17) is allocated to ERDTOH, i.e. it reduces the amount that would otherwise be added to the corporation's ERDTOH.

In summary, the $150 loss claim, or its tax-effected amount of $57.50, reduces the corporation's Part IV tax otherwise payable from $76.66 to $19.16. Based on the formula in subsection 129(4.2), no portion of this residual Part IV tax payable of $19.16 is added to NERDTOH – the entire amount is added to ERDTOH.

Example 2:

A corporation receives a $100 eligible dividend and a $100 non-eligible dividend, both from non-connected corporations. In the absence of the utilization of any offsetting losses, the corporation would pay 38.33 per cent Part IV tax on each of these amounts, with $38.33 added to its ERDTOH account and $38.33 added to its NERDTOH account. However, if that same corporation also had a $50 non-capital loss that it chose to utilize, its Part IV taxes would be reduced by 38.33 per cent of the loss, or $19.17.

As in Example 1, subsection 129(4.2) will first allocate the losses claimed to reduce the amount allocated to the corporation's NERDTOH. In this example, as the tax-effected amount of the losses claimed ($19.17) is less than the amount that would otherwise be allocated to the corporation's NERDTOH ($38.33) the NERDTOH addition is reduced to $19.16 and there is no excess to allocate to ERDTOH.

In summary, the $50 loss claim, or its tax-effected amount of $19.17, reduces the corporation's Part IV tax otherwise payable from $76.66 to $57.49. Based on the formula in subsection 129(4.2), the residual amount of Part IV tax payable of $57.49 is allocated to ERDTOH in the amount of $38.33 and to NERDTOH in the amount of $19.16.

Subsections 129(4.1) and (4.2) apply to taxation years that begin after 2018.

Reassessment Period – Requirements for Information and Compliance Orders

Clause 28

Definitions

ITA

231

Section 231 of the Act provides definitions for the purposes of sections 231.1 to 231.7, the provisions that set out the rules relating to the powers of the Canada Revenue Agency to audit and examine taxpayers' books and records.

Section 231 is amended to provide that the section also provides definitions for the purposes of new section 231.8, which applies to extend the reassessment period when taxpayers challenge requirements for information or compliance orders. For more information, see the commentary on section 231.8.

This amendment comes into force on Royal Assent.

Clause 29

Time period not to count

ITA

231.6(7)

Section 231.6 provides rules which enable the Minister to obtain such foreign-based information or documentation as is necessary to permit a proper assessment for Canadian tax purposes. Under subsection 231.6(2) a person resident in Canada or a non-resident person carrying on business in Canada must provide, when required by notice of the Minister, any foreign-based information or document. Under subsection 231.6(4) a person served with a notice under subsection (2) is permitted within 90 days of service thereof to apply to a judge for a review of the requirement to provide the foreign-based information or document.

Subsection 231.6(7) of the Act provides that the period of time that elapses between the application for review and its final disposition does not count toward the six-year statutory limit for making tax assessments relating to foreign transactions between non-arm's length taxpayers under subparagraph 152(4)(b)(iii), nor in the time permitted for the production of the information or document.

To ensure consistency with the wording of new section 231.8, which extends the statutory limitation period on taxpayer challenges to compliance orders and requirements for information that do not involve foreign-based information, subsection 231.6(7) is amended to clarify that the period of time that does not count towards the statutory limit or in the time permitted to produce the information or document, lasts until the application is finally disposed of. For further information, see the commentary on section 231.8.

This amendment comes into force on Royal Assent.

Clause 30

Time period not to count

ITA

231.8

New section 231.8 of the Act extends the reassessment period when a taxpayer makes an application for judicial review of a requirement for information (other than a requirement for foreign-based information under section 231.6) or when a taxpayer files a notice of appearance or otherwise challenges a compliance order. Section 231.8 provides that the period of time that elapses between the filing of the application for review of a requirement for information or the filing of a notice of appearance (or otherwise challenging the application for a compliance order) and the time either the application for judicial review or the application to obtain the compliance order is finally disposed of, does not count toward the statutory limit for making tax assessments.

This new section comes into force on Royal Assent.

Reassessment Period – Non-Resident Non-Arm's Length Persons

Clause 31

Reassessment Period – Non-Resident Non-Arm's Length Persons

The French version of 152(4)(b)(iii) is amended to eliminate any potential ambiguity in its wording and to better align the French and English versions of the Act. The relationship described in French as "between" ("entre") taxpayers is replaced by the relationship described in French as "involving" ("impliquant") taxpayers.

This amendment is deemed to have come into force on February 27, 2018.

Assessment and reassessment

ITA

152(4)

Subsection 152(4) of the Act generally provides that the Minister of National Revenue may at any time assess tax and other amounts payable by a taxpayer for a taxation year, but may not assess after the normal reassessment period for the year. The normal reassessment period for a year is generally four years from the date of the initial notice of assessment for corporations (other than Canadian-controlled private corporations) and mutual fund trusts. For other taxpayers, it is generally three years from the date of the initial notice of assessment. Subsection 152(4) includes exceptions that apply in certain circumstances.

Subsection 152(4) is amended by adding new paragraph (b.4). New paragraph (b.4) provides that an assessment, reassessment or new assessment may be made within six years after the end of the normal reassessment period where:

- as a consequence of a transaction involving a taxpayer and a non-resident person with whom the taxpayer does not deal at arm's length, a reassessment of tax is made or a notice that no tax is payable for a taxation year is issued;
- the reassessment or notice that no tax is payable reduces the taxpayer's loss for the taxation year that is available for carryback; and
- all or any portion of that loss had in fact been carried back to the prior taxation year.

New paragraph 152(4)(b.4) applies in respect of a taxation year if a reassessment of tax for the year was required under subsection 152(6), or would have been so required if the taxpayer had claimed an amount by filing the prescribed form referred to in that subsection on or before the day referred to in that subsection, in order to take into account a deduction claimed under section 111 of the Act in respect of a loss for a subsequent taxation year that ends on or after February 27, 2018.

Extended period assessment

ITA

152(4.01)

Subsection 152(4.01) of the Act limits the matters in respect of which the Minister of National Revenue can assess when an assessment to which paragraph 152(4)(a), (b), (b.1), (b.3) or (c) applies is made beyond the normal reassessment period for a taxpayer in respect of a taxation year.

Subsection 152(4.01) is amended to add a reference to new paragraph 152(4)(b.4).

As such, a reassessment for a taxation year made by the Minister after the normal reassessment period as a result of the conditions described in new subparagraph 152(4)(b.4) is limited by new paragraph 152(4.01)(b.4) to that which can reasonably be regarded as relating to the reduction in the amount of the loss.

Sharing Information for Criminal Matters

Clause 32

Where taxpayer information may be disclosed

ITA

241(4)(e)

Subsection 241(4) of the Act authorizes the communication of taxpayer information to government officials for limited purposes.

New subparagraph 241(4)(e)(xiii) is added to permit an official to provide taxpayer information, or allow the inspection of or access to taxpayer information, for the purposes of an order made under the *Mutual Legal Assistance in Criminal Matters Act*, with respect to an investigation or prosecution relating to an act or omission that, if it had occurred in Canada, would constitute an offence for which an order could be obtained under subsection 462.48(3) of the *Criminal Code,* in response to a request made pursuant to

- an administrative arrangement entered into under section 6 of the *Mutual Legal Assistance in Criminal Matters Act*, or
- a bilateral agreement for mutual legal assistance in criminal matters to which Canada is a party.

This amendment comes into force on Royal Assent.

Mutual Legal Assistance in Criminal Matters Act (MLACMA)

Clause 33

Interpretation

MLACMA

2

Subsection 2(1) of the MLACMA defines an “agreement” for the purposes of the Act to mean “a treaty, convention or other international agreement that is in force, to which Canada is a party and that contains a provision respecting mutual legal assistance in criminal matters”. This provision currently delineates the type of agreement that triggers the application of the Act.

This amendment maintains the current definition of “agreement” in new paragraph (a) of the definition of “agreement” in subsection 2(1). However, it is proposed to amend the definition of “agreement” by adding paragraph (b) in subsection 2(1) in order to enable international cooperation, relating to a criminal investigation or prosecution, under the *Convention on Mutual Administrative Assistance in Tax Matters* (the Convention), concluded at Strasbourg, on January 25, 1988, as amended from time to time by a protocol, or other international instrument, as ratified by Canada and comprehensive tax information exchange agreements and tax treaties that have effect and that Canada has entered into. This amendment does not apply for the purposes of Part II and III of MLACMA.

Clause 34

Publication of Agreements in Canada Gazette

MLACMA

5

Section 5 of the MLACMA addresses requirements to publish “an agreement - or the provisions respecting mutual legal assistance in criminal matters contained in a convention or other international agreement”, within the meaning of the Act, in the *Canada Gazette*. Once published, subsection 5(3) provides that these agreements and provisions are to be judicially noticed.

This amendment is consequential to the addition of new paragraph (b) to the existing definition of “agreement” in subsection 2(1) and ensures that the provision continues to apply to the current definition of agreement (now in paragraph (a)) expressly dealing with mutual legal assistance in criminal matters.

Clause 35

Functions of Minister

MLACMA

7

Under subsection 7(1) of the MLACMA, the Minister of Justice is responsible for the implementation of every agreement and the administration of the MLACMA. This amendment is consequential to the addition of new paragraph (b) to the existing definition of “agreement” in subsection 2(1). Subsection 7(1) would be amended to ensure that the Minister of Justice continues to be responsible for the implementation of agreements, set out in the existing definition of “agreement” that deal with mutual legal assistance in criminal matters, while continuing her responsibilities for the administration of the MLACMA as a whole.

Subsection 7(2) ensures that when a request is presented to the Minister, the Minister shall deal with the request in accordance with the agreement and the Act. This amendment is consequential to the addition of new paragraph (b) to the existing definition of “agreement” in subsection 2(1). It would ensure that when requests are made to Canada by a state or entity or a competent authority as defined in the MLACMA, the Minister of Justice continues to deal with the request under the current mutual legal assistance process, in accordance with the relevant agreement as defined in the existing definition of “agreement” (in new paragraph (a)) dealing with mutual legal assistance in criminal matters.

Under proposed new subsection 7(3), the Minister of National Revenue, who receives a request for assistance under a tax treaty, comprehensive tax information exchange agreement or the Convention from a foreign state or entity for the purposes of a criminal investigation or prosecution, would present the foreign request to the Minister of Justice, who shall deal with the request in accordance with the relevant tax treaty, comprehensive tax information exchange agreement or the Convention, and the MLACMA.

Clause 36

Limitation — requests under agreements

MLACMA

8

Subsection 8(1) of the MLACMA currently limits mutual legal assistance requests so that the Minister may not give effect to a request for mutual legal assistance unless the agreement that Canada has entered into provides for “mutual legal assistance with respect to the subject matter of the request”. This amendment is consequential to the addition of new paragraph (b) to the existing definition of “agreement” in subsection 2(1) and expands the application of the MLACMA.

Clause 37

Orders to gather tax information

MLACMA

22.06

New section 22.06 of the MLACMA is added to provide an order for the production of tax information relating to certain serious criminal offences ("an act or omission that, if it had occurred in Canada, would have constituted an offence under subsection 462.48(1.1) of the *Criminal Code*") being investigated or prosecuted by an entity or state as defined in MLACMA.

Subsection 22.06(1) would permit a judge (as defined in section 2) to whom an application is made to issue a production order to gather tax information in certain circumstances. The order could be made only with respect to "an investigation or prosecution relating to an act or omission that, if it had occurred in Canada, would have constituted an offence under subsection 462.48(1.1) of the *Criminal Code*". The order would be limited to gathering the information or documents referred to in paragraph 462.48(2)(c).

Subsection 22.06(2) would clarify that, subject to subsection 22.06(3), the production order to gather tax information may be obtained and made in accordance with subsections 462.48(1) to (5) of the *Criminal Code* and the order could be executed in the manner set out in the *Criminal Code*, with any necessary modifications.

Subsections 462.48(1) to (5) of the *Criminal Code* address such issues as the type of offence that may be investigated or prosecuted, the application before the judge and the threshold for issuing the production order.

Subsection 22.06(3) would provide that where there is an inconsistency between the *Criminal Code* provisions and the provisions in MLACMA, the MLACMA provisions specified for dealing with a foreign request, with necessary modifications, would prevail. In particular:

- The reference to paragraphs 18(2) (b) and (c) is intended to clarify that a production order can only be obtained to gather information and to produce copies but not to examine any person;
- The reference to subsections 18(3) to (7) are intended to make clear that:
    - A judge may designate a person to whom copies may be produced;
    - An order may be executed anywhere in Canada;
    - The order may include terms and conditions the judge considers desirable to protect the interests of persons named in it or third parties;
    - The terms and conditions of the order may be varied;
    - A person named in the order may refuse to produce a record or thing if:
        - producing the record or thing would disclose information that is protected by the Canadian law of non-disclosure of information or privilege;

    - producing the record or thing would constitute a breach of a privilege recognized by a law in force in the state or entity that presented the request; or
    - producing the record or thing would constitute the commission by the person of an offence against a law in force in the state or entity that presented the request.
  - The reference to subsections 18(8) and (9) would apply the MLACMA process for dealing with refusals to produce records or things on the above grounds.

- Subsection 22.06(3) also provides that sections 19 to 22 of MLACMA (except for paragraph 19(1)(a)) would apply to a production order under section 22.06, with any necessary modifications, and prevail over any provision of the *Criminal Code* that is inconsistent with them. In particular,
  - Subsections 19(1) and (2) provide for a report to the judge who made the order or a judge of the same court, and to the Minister of Justice, generally describing the records or things produced, or if required, the record or thing itself. Paragraph 19(1)(a), which refers to transcripts of examinations, would not apply as the order relates only to the production of records or things.
  - Under paragraph 19(1)(c) and subsection 19(3), a copy of the reasons for refusals to produce any record or thing under subsection 18(9) shall also be provided to the judge and the Minister. A determination of whether the refusals are well-founded are made under subsections 19(3) and (4). If not, the judge may order the information to be produced. Subsections 20(1) to (4) provide for a sending hearing in which a judge determines whether or not to send the information to the foreign state making the request and can impose any terms and conditions that the judge considers desirable, to give effect to the request, the preservation and return to Canada of any record or thing so produced; and for the protection of third parties.
  - Under section 21, information that is ordered sent to the requesting state or entity cannot be sent until the Minister is satisfied that the state or entity has agreed to comply with any terms or conditions imposed.
  - Section 22 applies contempt of court provisions in the event a person who has been ordered to produce information fails to comply with that order.

Related amendments to the *Income Tax Act*, the *Excise Tax Act* and the *Excise Act, 2001*, would permit taxpayer and other confidential tax information to be provided pursuant to a production order under section 22.06 made pursuant to an administrative arrangement under section 6 of the MLACMA or a bilateral agreement for mutual legal assistance in criminal matters to which Canada is a party.

Criminal Code of Canada

Part XII.2 Proceeds of Crime

Clause 38

Disclosure Provisions

Paragraph 462.48(2)(c) of the *Criminal Code* provides that the Attorney General may make an application under subsection 462.48(1.1) in respect of "the type of information or book, record, writing return or other document obtained by or on behalf of the Minister of National Revenue for the purposes of the *Income Tax Act*," for the purpose of investigating and prosecuting the criminal offences set out in paragraphs 462.48(1.1)(a) to (d).

Under the proposed amendment, an order for similar information ("information or book, record, writing return or other document") obtained by or on behalf of the Minister of National Revenue for the purposes of the *Income Tax Act*, Part IX of the *Excise Tax Act* and the *Excise Act, 2001* could be sought for an investigation of the offences in paragraphs 462.48(1.1)(a) to (d). This amendment adds confidential tax information (GST/HST and excise tax information) to the information that can be gathered under section 462.48 of the *Criminal Code*.