International Fiscal Association

YIN SESSION

LOST IN THE SHUFFLE: UNENACTED TAX PROPOSALS YOU MAY HAVE MISSED

PRESENTERS:

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PRESENTED ON MARCH 20, 2025

AGENDA

Proposed Amendments to:

1. ITA s. 15(2)
2. ITA s. 212(13.1)(a) – Partnerships and Part XIII
3. ITA ss. 85.1(4), 85.1(4.1) 87(8.3), 87(8.31)
4. RTF for CCPCs / ITA s. 88(3.3)

ITA S. 15(2)

David Bunn

OUTLINE

1. Overview of subsection 15(2)
2. Legislative history
3. Technical amendments
4. Remaining gaps

OVERVIEW OF SUBSECTION 15(2)

- Subsection 15(2) is often referred to as a "shareholder loan rule"
- However, it extends beyond amounts owing by a shareholder and also contemplates amounts owing by certain persons and partnerships who do not deal at arm's length with a shareholder
- The purpose of subsection 15(2) is to prevent corporate funds from being transferred to a shareholder of a particular corporation, or to certain connected persons or partnerships, without the recipient being subject to tax in an amount equal to the liability that would have arisen had the funds been extracted through the payment of taxable dividends

LEGISLATIVE HISTORY

- Originally, subsection 15(2) was fairly narrow and only applied to a loan from a corporation to a shareholder
- Effective 1977, the provision was expanded to include situations where the loan was made by the particular corporation, a corporation to which the particular corporation was related, or a partnership of which either or both of the corporations was a member
- The provision was also expanded to include situations where the recipient of the loan was a person "connected" with a shareholder of the particular corporation
- The meaning of "connected" was defined to exclude a foreign affiliate of the particular corporation, or of another Canadian resident person not dealing at arm's length with the particular corporation, but made no reference to partnerships

LEGISLATIVE HISTORY (continued)

- Effective 1981, the provision was expanded to include not only loans but also other types of indebtedness, as well as situations where the loan or indebtedness was owing by certain partnerships
- In *Gillette Canada Inc. v The Queen*, 2001 DTC 895 (TCC), the Tax Court of Canada held that a loan from a Canadian corporation to a partnership the majority partner of which was the non-resident shareholder of the Canadian corporation was not within the scope of subsection 15(2) as a partnership is not a "person" and the "connected" concept, as written at the time, did not extend to partnerships
- In response to *Gillette*, the legislation was amended (effective October 31, 2011) to contemplate connected "persons" or "partnerships" – although the exclusion for foreign affiliate debtors continued to refer only to foreign affiliates "of a person"

TECHNICAL AMENDMENTS

- Draft technical amendments were released on August 12, 2024
- Under the technical amendments:
  - Subsection 15(2) will be "subject to subsection 15(2.01)"
  - Subsection 15(2.01) will clarify that subsection 15(2) does not apply (in respect of loans and indebtedness incurred after October 31, 2011) to:

    a) a person that is a corporation resident in Canada; or

    b) a partnership, each member of which is a person described in paragraph (a) or another partnership described in this paragraph

TECHNICAL AMENDMENTS (continued)

- For loans & indebtedness incurred after the Announcement Date (i.e., after August 12, 2024), paragraph (a) (as described on previous slide) will be further expanded to:

a) a person that is

i. a corporation resident in Canada,

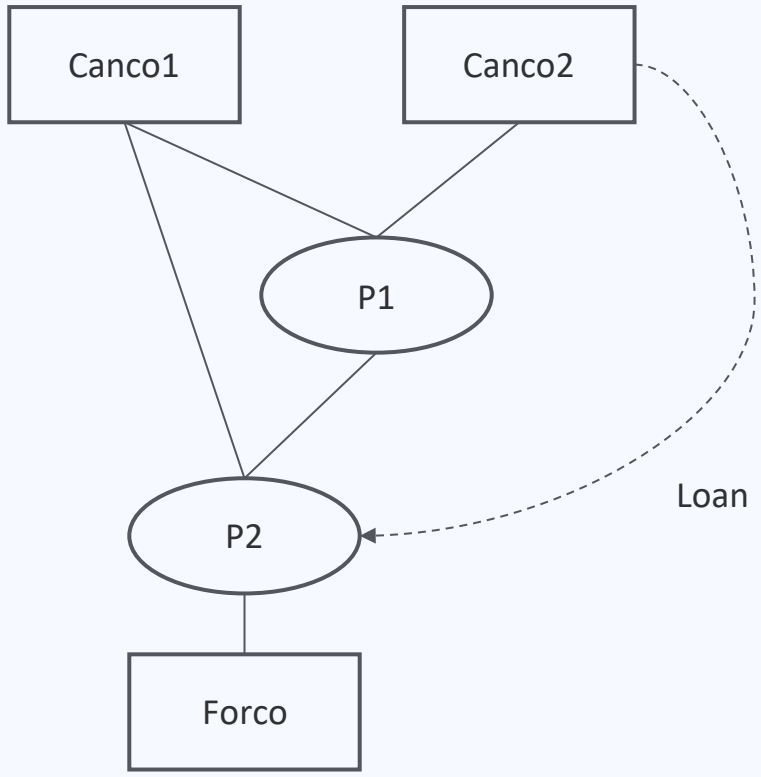
ii. a foreign affiliate of the particular corporation referred to in subsection 15(2), or

iii. a foreign affiliate of a person resident in Canada with which the particular corporation referred to in subsection 15(2) does not deal at arm's length

TECHNICAL AMENDMENTS (continued)

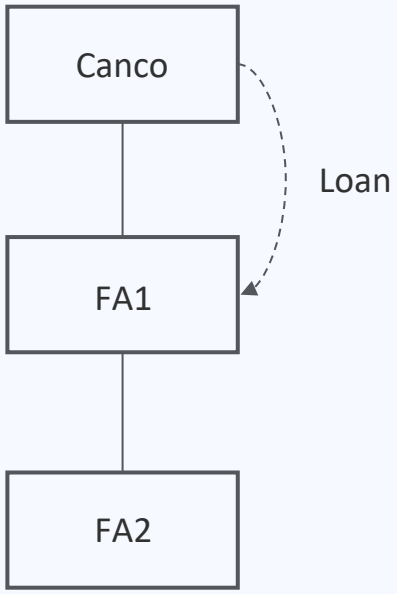
- The amendments clarify that the shareholder loan rule is not intended to apply to loans received by a partnership each member of which is, directly or indirectly through one or more other partnerships, a corporation resident in Canada (CRIC)
  - This accommodates loans to a partnership in a tiered partnership structure with all of the ultimate members being CRICs
- The amendments also address the potential concern that subsection 15(2) may unintentionally impact certain debtors belonging to the same foreign affiliate group as the particular corporation
  - This addresses the commonly encountered situation involving a loan to a foreign affiliate holding company
  - It also addresses a loan to a partnership all of the members of which are foreign affiliates of the particular corporation or a person resident in Canada with which the particular corporation does not deal at arm's length

EXAMPLE 1 – Tiered Partnership Structure



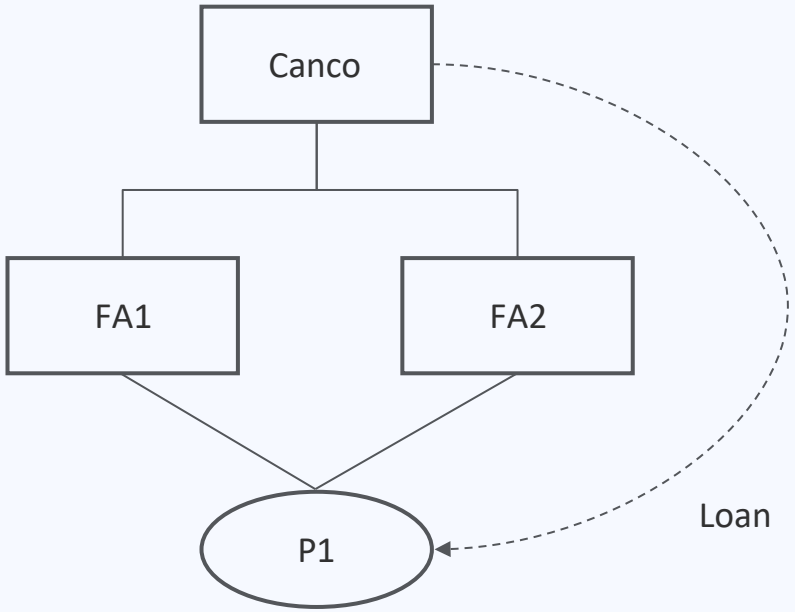
- Two CRICs (Canco1 and Canco2) are the sole members of a partnership (P1)
- Canco1 and P1 are the sole members of a second partnership (P2)
- P2 owns all the shares of a foreign corporation (Forco)
- Canco2 makes a loan to P2
- Since P2 is a shareholder of a particular corporation (Forco), and P2 has received a loan from a corporation related to Forco (Canco2), in the absence of proposed subsection 15(2.01), subsection 15(2) could potentially apply to include the amount of the loan in computing the income of P2 for the year
- However, P2 is a partnership described in proposed paragraph 15(2.01)(b) because each member of the partnership is a CRIC (Canco1) or another partnership described in paragraph (b) (P1). P1 is a partnership described in paragraph (b) because each member is a CRIC
- Consequently, subsection 15(2) does not apply to the loan from Canco2 to P2

EXAMPLE 2 – Loan to Foreign Holding Company



- A CRIC (Canco) owns all the shares of a foreign corporation (FA1)
- FA1 owns all the shares of another foreign corporation (FA2)
- Canco makes a loan to FA1
- Since FA1 is a shareholder of a particular corporation (FA2), and FA1 has received a loan from a corporation related to FA2 (Canco), in the absence of proposed subparagraph 15(2.01)(a)(iii), subsection 15(2) could potentially apply to include the amount of the loan in computing the income of FA1 for the year
- However, FA1 is a foreign affiliate of a person resident in Canada with which FA2 does not deal at arm's length (Canco) as described in proposed subparagraph 15(2.01)(a)(iii)
- Consequently, subsection 15(2) does not apply to the loan from Canco to FA1

EXAMPLE 3 – Loan to Partnership held by FAs

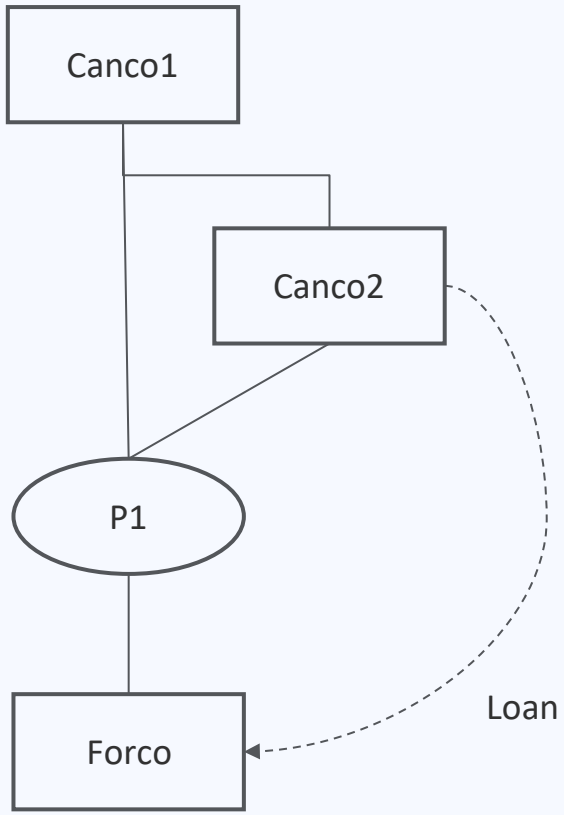


- A CRIC (Canco) owns all the shares of a two foreign corporations (FA1 and FA2)
- FA1 and FA2 are the sole members of a partnership (P1)
- Canco makes a loan to P1
- Pursuant to subsection 15(2.1), P1 is connected, in respect of a particular corporation (FA1), with a shareholder of FA1 (Canco) because P1 is affiliated with Canco
- P1 is connected with a shareholder of FA1 (Canco), and P1 has received a loan from a corporation related to FA1 (Canco), which means subsection 15(2) could potentially apply to include the amount of the loan in computing the income of P1 for the year
- However, with proposed subparagraph 15(2.01)(a)(iii), P1 is a partnership described in paragraph 15(2.01)(b) because each member of the partnership (FA1 and FA2) is a foreign affiliate of a person resident in Canada with which FA1 does not deal at arm's length (Canco)
- Consequently, subsection 15(2) does not apply to the loan from Canco to P1

REMAINING GAPS

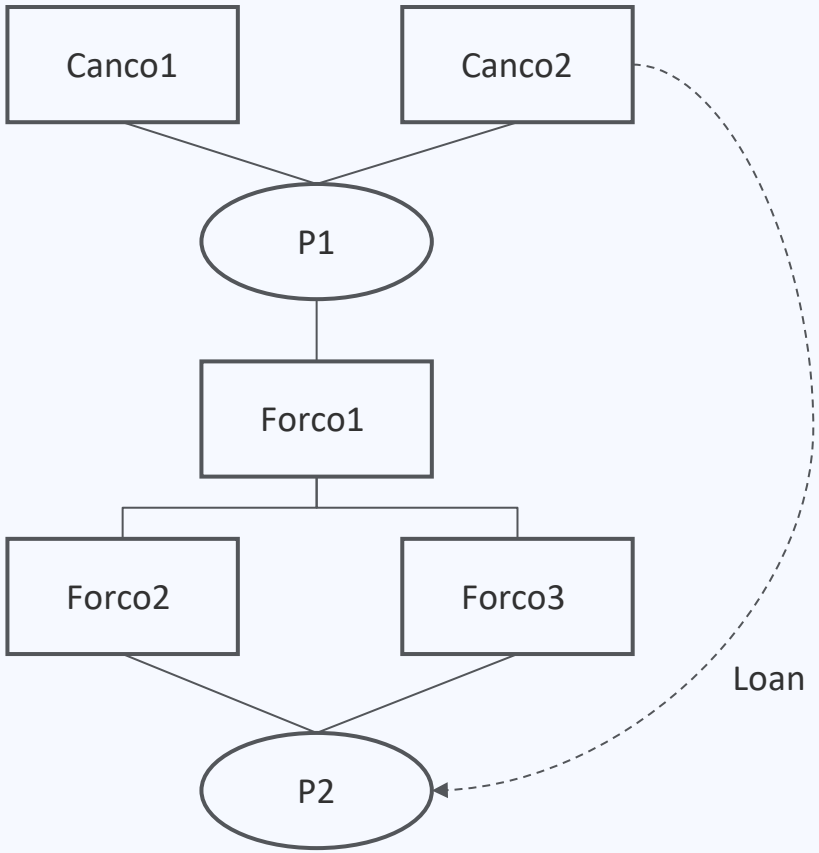
- The amendments are a welcome change; however:
  - There continues to be a lack of clarity for loans and indebtedness incurred prior to the Announcement Date involving certain debtors belonging to the same foreign affiliate group as the particular corporation, as well as loans to partnerships with foreign affiliate members
  - Also, while the amendments address certain areas of concern, they do not address commonly encountered situations involving debts owing by a foreign corporation below a partnership

EXAMPLE 4 – Loan to Foreign Corp below Partnership



- Two non-arm's length CRICs (Canco1 and Canco2) are the sole members of a partnership (P1)
- P1 owns all the shares of a foreign corporation (Forco)
- Canco1 makes a loan to Forco
- While it is clear from a policy standpoint that such loans are intended to be outside the scope of subsection 15(2), Forco is not a foreign affiliate of Canco 1 or Canco 2 (because of the intervening partnership) and a partnership is not considered to be a person for these purposes
- As such, this situation is not covered by any of the exceptions in proposed paragraph 15(2.01)(a)

EXAMPLE 5 – Loan to Partnership in FA Group



- Two non-arm's length CRICs are the sole members of a partnership (P1)
- P1 owns all the shares of a foreign corporation (Forco1)
- Forco1 owns all the shares of two foreign corporations (Forco2 and Forco3)
- Forco2 and Forco3 are the sole members of a second partnership (P2)
- Canco2 makes a loan to P2
- There is a concern that subsection 15(2) could apply to the loan since P2 is connected with a shareholder (Forco1) of a particular corporation (Forco2) by virtue of P2 being affiliated with that shareholder (Forco1)
- The exception in proposed paragraph 15(2.01)(b) is insufficient in this case, as Forco2 is not, for purposes of section 15, a foreign affiliate of Canco2 because of the intervening partnership (P1), and therefore P2 is technically not a partnership each member of which is a person described in proposed paragraph 15(2.01)(a)

ITA S. 212(13.1)(A) PARTNERSHIPS AND PART XIII

Alexandra Carbone

ITA S. 212(13.1)(A) PARTNERSHIPS AND PART XIII

CURRENT ITA s. 212(13.1)(a)

- If a partnership pays/credits an amount to a non-resident person, it is deemed to be a person resident in Canada for Part XIII purposes (other than s. 216) in respect of the portion of the amount that is deductible in computing the partnership's Canadian-source income/loss under s. 96(1)(f) or (g)
- August 9, 2022 proposed amendments to s. 212(13.1)(a) apply to amounts paid/credited no earlier than date of future release of draft legislation, to occur after consultation period

ITA S. 212(13.1)(A) PARTNERSHIPS AND PART XIII

PROPOSED ITA s. 212(13.1)(a)

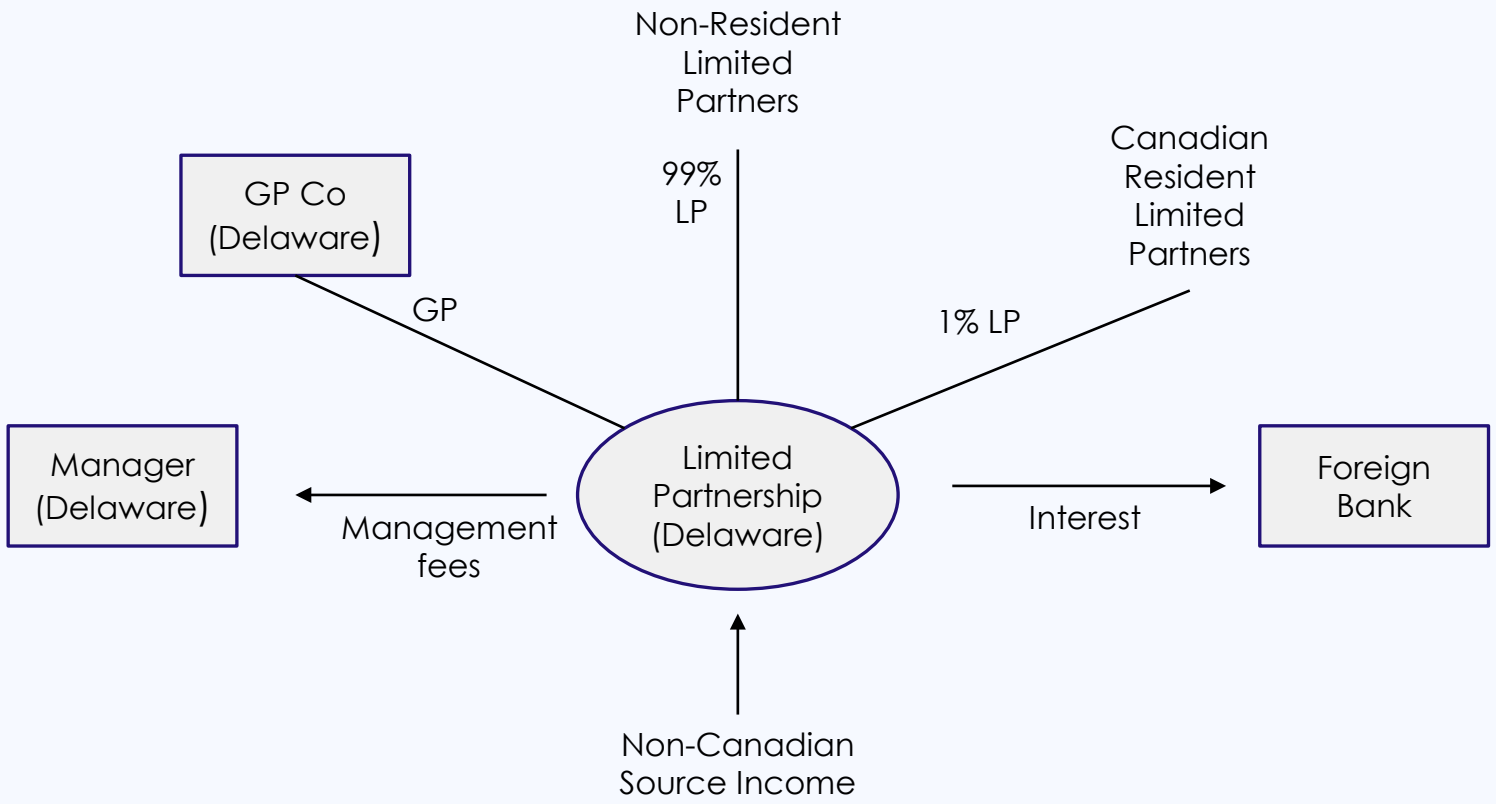
- If a partnership pays/credits a particular amount to a non-resident person, the partnership is deemed to be a person resident in Canada in respect of the total of all amounts each of which is a portion of the particular amount that is deductible, or that would but for section 21 be deductible, in computing, with respect to each member of the partnership:
  - **Canadian-resident member**: the member's share of the partnership's income/loss
  - **Non-resident member**: the portion of the member's share of the partnership's income/loss that is included in (i) the member's taxable income earned in Canada, or (ii) the amount on which the member is liable to pay tax under Part I because of section 216

ITA S. 212(13.1)(A) PARTNERSHIPS AND PART XIII

PROPOSED ITA s. 212(13.1)(a) (cont'd)

- Deeming rule under s. 212(13.1)(a) no longer tied to payments deductible in computing the partnership's Canadian-source income → rule applies to any payment by the partnership to a non-resident person if payment can be deducted in computing income subject to Part I tax of a member
- See also: proposed s. 212(13.11) for deeming rules, including where a partnership pays/credits an amount to another partnership (other than a "Canadian partnership"), and look-through rules for tiered partnerships

EXAMPLE PROPOSED 212(13.1)(A)



ITA S. 212(13.1)(A.1) PARTNERSHIPS AND PART XIII

CURRENT ITA s. 212(13.1)(a.1)

- If a partnership pays/credits/provides an amount described in s. 212(5.1)to a non-resident person, the partnership is deemed to be a person
- no proposed amendments

ITA S. 212(13.1)(B) PARTNERSHIPS AND PART XIII

CURRENT ITA s. 212(13.1)(b)

- If a person resident in Canada pays/credits an amount to a partnership that is not a Canadian partnership (per s. 102), the partnership is deemed to be a non-resident person
- August 9, 2022 proposed amendments to s. 212(13.1)(b) apply no earlier than date of future release of draft legislation, to occur after consultation period for August proposals

ITA S. 212(13.1)(B) PARTNERSHIPS AND PART XIII

Paragraph 212(13.1)(b) of the Act is replaced by the following:

(b) where a person resident in Canada pays or credits an amount (other than a partnership, or a non-resident person, that is deemed, in respect of that amount, to be a person resident in Canada under paragraph (a) or (13.2)(b), as the case may be)to a partnership (other than a Canadian partnership), the partnership is deemed, in respect of that amount, to be a non-resident person.

ITA S. 212(13.1)(B) PARTNERSHIPS AND PART XIII

PROPOSED ITA s. 212(13.1)(b)

- Deeming rule in s. 212(13.1)(b) does not apply if the payor of the amount is a partnership or a non-resident person that is deemed to be a resident of Canada by s. 212(13.1)(a) or s. 212(13.2)(b)
  - i.e., if the amount is paid or credited by a partnership or non-resident person that is deemed to be a resident, the payee who is not a Canadian partnership will not be deemed to be a non-resident person

CBA/CICA JOINT COMMITTEE LETTER

March 22, 2023

"possibly insurmountable tax compliance issues"

- Significant concerns with application of proposed amendments to foreign partnerships whose only connection to Canada is the residence of a very small minority of partners and who are often passive investors
- Concerns with the possibility of effective tax compliance with proposed amendments by foreign partnerships

ITA SS. 85.1(4), 85.1(4.1) 87(8.3) & 87(8.31)

Carolyn MacDonald

PROPOSED SUBSECTIONS 85.1(4), 85.1(4.1) 87(8.3) AND 87(8.31)

- In general terms, current subsections 85.1(4) and 87(8.3) address concerns regarding the use of rollover rules in subsections 85.1(3) and 87(8), respectively, by preventing the deferral of tax in respect of gains on FA shares that constitute excluded property.
- Proposed amendments introduced as part of August 8, 2022 draft technical amendment package seek to broaden the application of these existing anti-avoidance rules.
- Proposed amendments are applicable in respect of dispositions that occur after August 8, 2022.
- See February 16, 2023 Joint Committee Submission.

SUBSECTION 85.1(4)

Existing Conditions (para (a))	Proposed Conditions (para (a))
Disposition of particular FA share to another FA	Particular disposition of particular FA share to another FA
All or substantially all of particular FA property was EP	All or substantially all of particular FA property was EP or (other) property disposed of was EP of a FA
Part of a transaction or event or series	Part of a transaction or event or series
For the purpose of disposing of the FA share	Includes another disposition of (i) the share, (ii) substituted property or (iii) property any FMV of which is derived, directly or indirectly, from (i) or (ii)

SUBSECTION 85.1(4) (CONT)

Existing Conditions (para (a)) cont	Proposed Conditions (para (a)) cont
To an AL person or partnership (other than FA in which the taxpayer has a qualifying interest)	To an acquirer that is AL or a NAL non-resident (other than a section 17 CFA). *Note subsection 85.1(4.1) interpretational rule for partnerships

Proposed Subsection 85.1(4.1) – Interpretational Rule

Taxpayer and acquirer deemed AL if:

- Either is partnership and other is not: any partner is AL with other party
- Both are partnerships: taxpayer or any partner of taxpayer is AL with acquirer or any partner of acquirer

Acquirer deemed NR NAL person if:

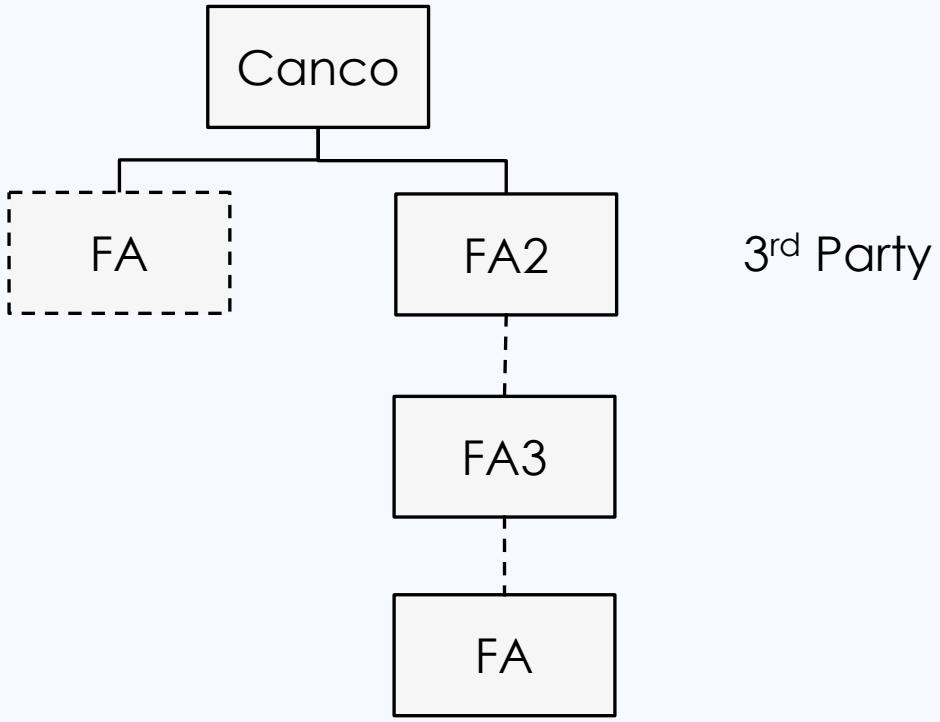
- Either is partnership and other is not: any partner is NAL with other party and acquirer (or any partner of acquirer, if a partnership) is NR
- Both are partnerships: taxpayer or any member is NAL with acquirer or any member, and any acquirer member is NR

SUBSECTION 85.1(4) (CONT)

Existing Conditions (para (b))	Proposed Conditions (para (b))
ACB of FA share > POD	ACB of FA share > POD in respect of particular disposition

SUBSECTION 85.1(4) (CONT)

Example



1. Canco forms FA2 and FA3.
2. Canco transfers FA to FA2, in exchange for FA2 shares.
3. FA2 transfers FA to FA3, in exchange for FA3 shares.

How does proposed subsection 85.1(4) apply on a sale of FA3 shares to the 3rd party? A sale of FA2 shares? What if the 3rd party instead invests in FA3 as a joint venture?

SUBSECTION 87(8.3)

Existing Conditions	Proposed Conditions
Foreign Merger	Foreign Merger
New foreign corporation is FA	New foreign corporation is FA
Part of a transaction or event or series	Part of a transaction or event or series
Includes a disposition of shares of (i) new foreign corporation or (ii) substituted property	Includes a disposition of (i) shares of new foreign corporation, (i) substituted property or (iii) property any FMV of which is derived, directly or indirectly, from (i) or (ii)
Disposition to an AL person (other than FA in which taxpayer has a qualifying interest) or partnership in which such person is a member	Disposition to an acquirer that is (i) not a NAL Canadian resident and (ii) not a section 17 CFA. *Note subsection 87(8.31) interpretational rule for partnerships

SUBSECTION 87(8.3) (CONT)

Existing Conditions (cont)	Proposed Conditions (cont)
Shares of new foreign corporation are EP	All or substantially all of predecessor foreign corporation property was EP or property disposed of was EP of a FA

Proposed Subsection 87(8.31) – Interpretational Rule

Taxpayer and acquirer deemed AL if:

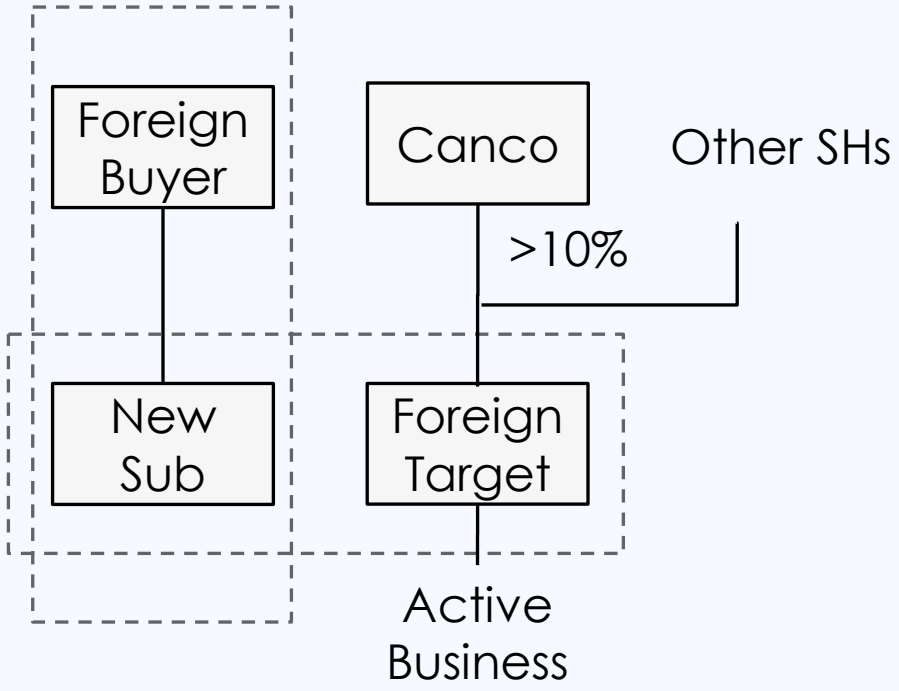
- Either is partnership: any partner is AL with other party
- Both are partnerships: taxpayer or any partner of taxpayer is AL with acquirer or any partner of acquirer

Acquirer deemed NR NAL person if:

- Either is partnership: any partner is NAL with other party and acquirer (or any partner of acquirer, if a partnership) is NR
- Both are partnerships: taxpayer or any member is NAL with acquirer or any member, and any acquirer member is NR

SUBSECTION 87(8.3) (CONT)

EXAMPLE



1. Foreign Buyer forms New Sub.
2. New Sub merges with and into Foreign Target with foreign target surviving ("Merged Target"). Canco exchanges its Foreign Target shares for shares in Foreign Buyer, and will hold >10% of Foreign Buyer.
3. Merged Target merges with and into Foreign Buyer, with Foreign Buyer surviving.

How does proposed subsection 87(8.3) apply to Merger #1? Merger #2? Future transactions?

RFT AMENDMENTS / ITA S. 88(3.1)

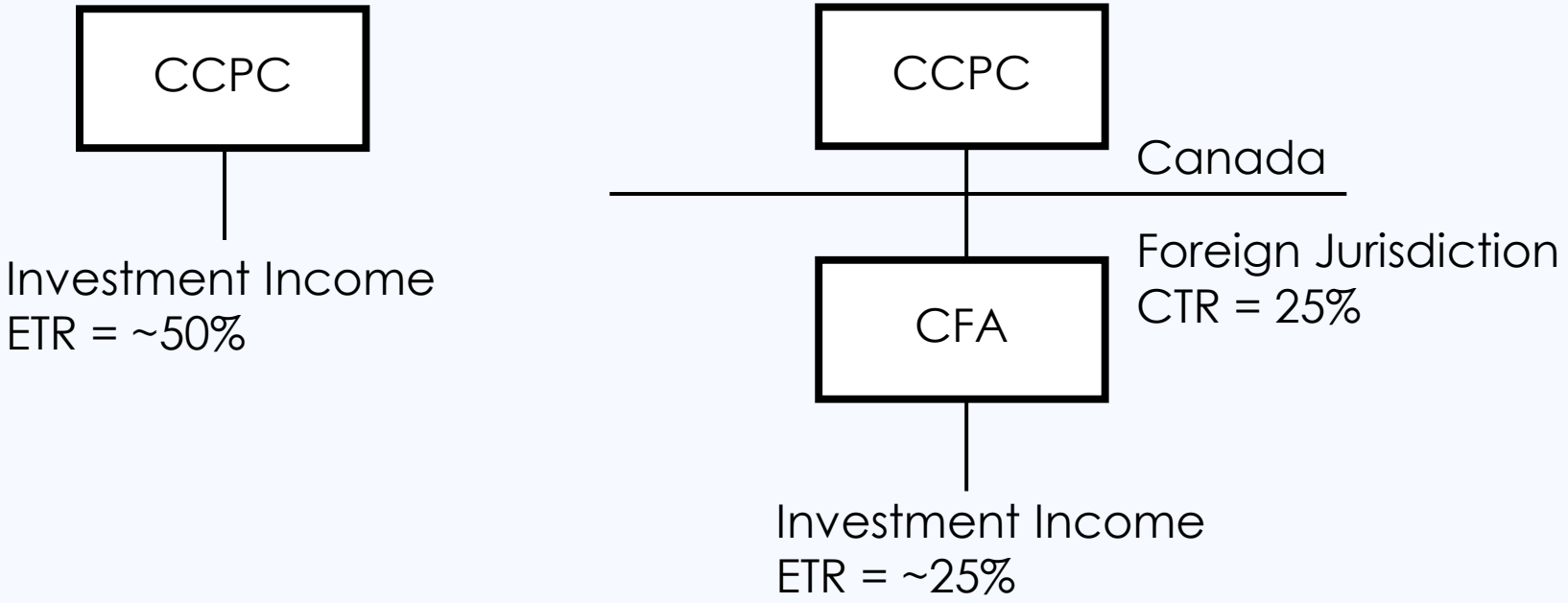
Christopher Montes

OUTLINE

1. Proposed RTF Amendments
2. Proposed s. 88(3.3) Amendment

PROPOSED RTF AMENDMENTS

- THE PERCEIVED PROBLEM – MISALIGNMENT BETWEEN AII AND FAPI REGIMES

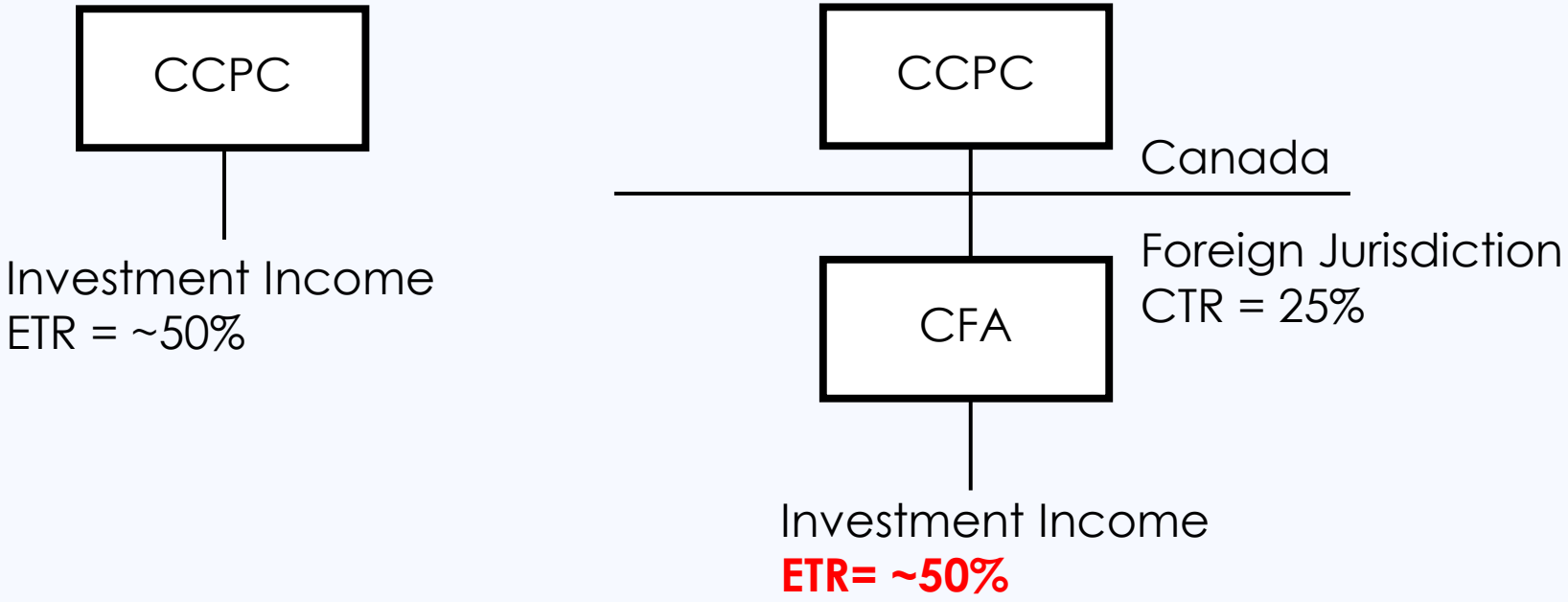


PROPOSED RTF AMENDMENTS

- BUDGET 2022 / AUGUST 2022 DRAFT LEGISLATION
  - RTF = 1.9 instead of 4 for CCPCs / SCCPCs
    - s. 91(4) FAT deduction
    - s. 113(1) deductions for hybrid and taxable surplus dividends
  - Integration through CDA account rather than GRIP
    - s. 113(1)(a) and (d) deductions (less withholding tax on dividend) continue to go into GRIP
    - s. 113(1)(a.1), (b) and (c) deductions (less withholding tax on dividend) go into CDA
  - Applied to tax years that begin on or after Budget Day

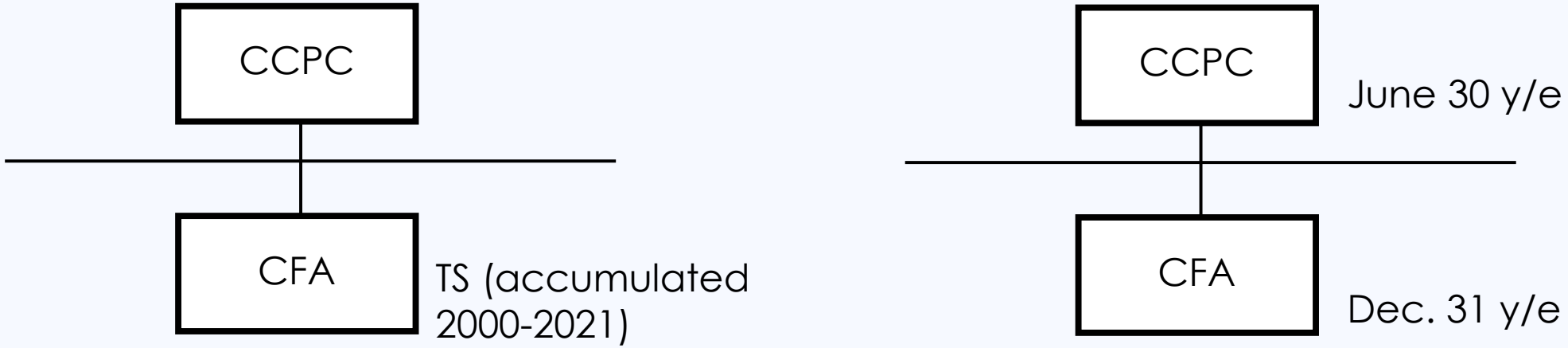
PROPOSED RTF AMENDMENTS

- THE INTENDED RESULT



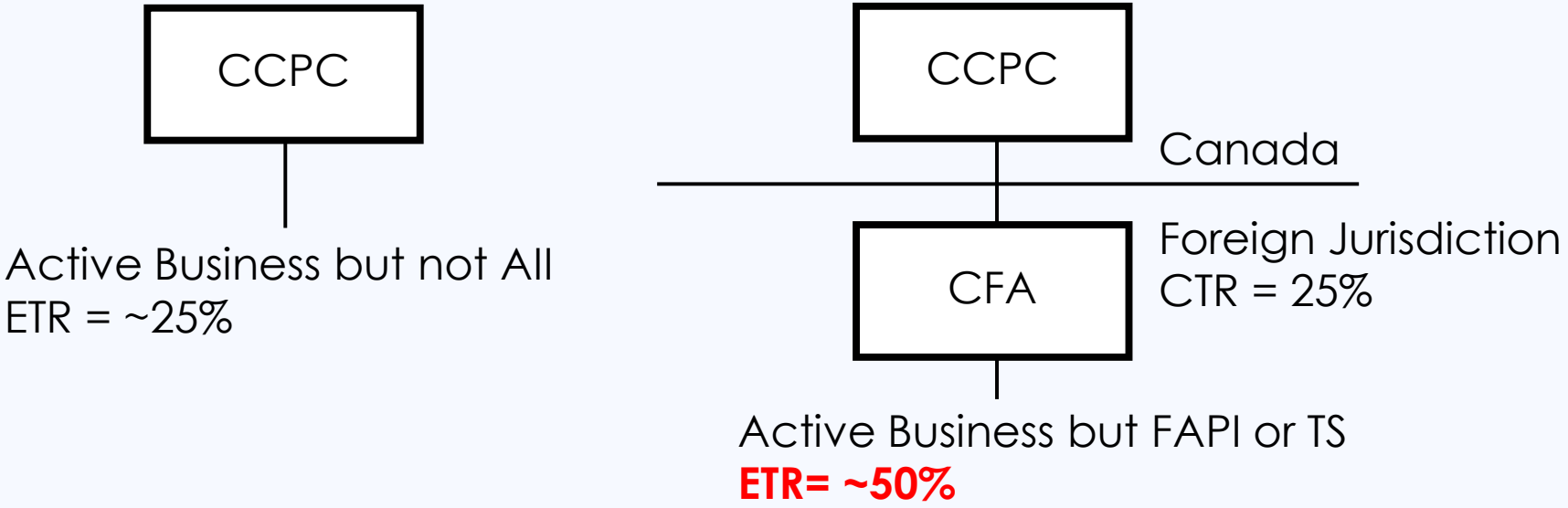
PROPOSED RTF AMENDMENTS

- ISSUES WITH THE BUDGET 2022 PROPOSALS / AUGUST 2022 DRAFT LEGISLATION
  - Retroactivity
    - Examples:
      - CFA with a historical taxable surplus balance
      - CFA with a December 31, 2022 year-end; CCPC with a June 30, 2023 year-end



PROPOSED RTF AMENDMENTS

- ISSUES WITH THE BUDGET 2022 PROPOSALS / AUGUST 2022 DRAFT LEGISLATION
  - FAPI and taxable surplus include amounts that would not be AII if earned directly by a CCPC
    - e.g., active business that is an investment business (but would not be AII if earned by a CCPC)
    - e.g., active business where M&M is not in jurisdiction of residence



PROPOSED RTF AMENDMENTS

- AUGUST 2024 DRAFT LEGISLATION
  - Maintains key features of August 2022 draft legislation
    - RTF = 1.9 instead of 4 for CCPCs / SCCPCs
    - Integration through CDA account rather than GRIP
  - Does not deal with retroactivity
    - Applies to tax years that begin on or after Budget Day
  - Attempts to more closely align All and FAPI/TS rules through limited exceptions
    - Foreign accrual business income
    - FABI surplus
    - Underlying FABI surplus tax

PROPOSED RTF AMENDMENTS

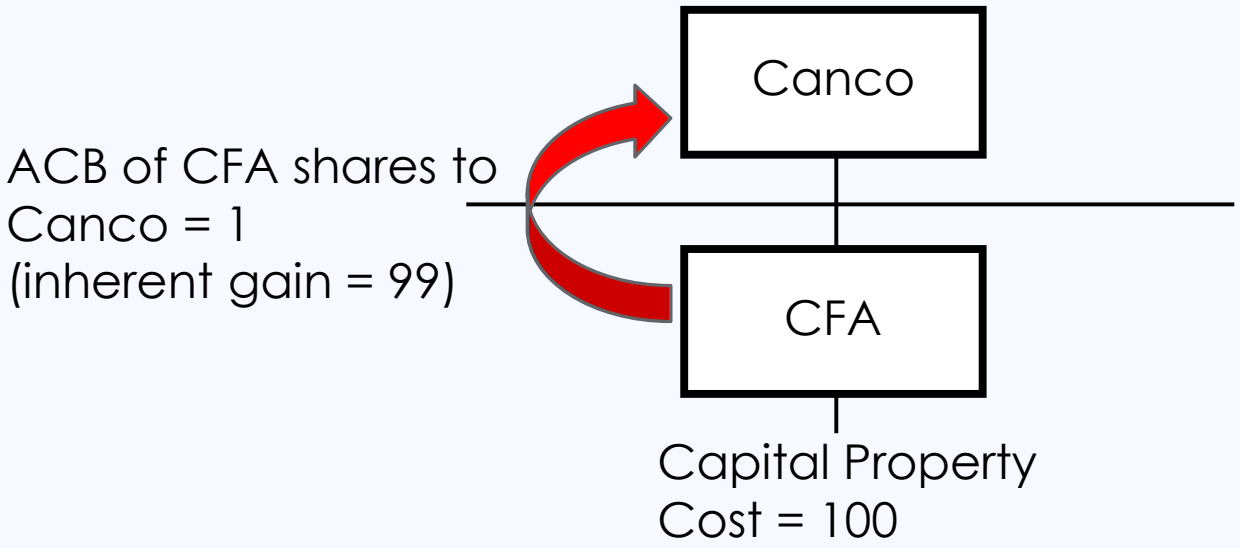
- AUGUST 2024 DRAFT LEGISLATION
  - Foreign accrual business income
    - Services income under s. 95(2)(b)(i) if certain conditions are met
    - Investment business income from the development or leasing of real property if 5+ employee test would be met by counting Canadians
    - s. 93.4(2) election needs to be filed to get s. 91(4) deduction at an RTF of 4
  - FABI surplus
    - Add: FABI (less foreign tax), FABI surplus dividends received, net earnings from active business
    - Deduct: FABI dividends paid, net loss from active business
    - s. 93.4(3) election needs to be filed to get s. 113 deduction at an RTF of 4
  - Underlying FABI surplus tax
    - Foreign tax reasonably applicable to FABI surplus
    - Disproportionate allocation can be made
  - FABI elections have historical effect

PROPOSED RTF AMENDMENTS

- ISSUES WITH THE AUGUST 2024 DRAFT LEGISLATION
  - The FABI exception is far too narrow – many other types of income are FAPI but not AII
  - A better solution is to define FABI as anything that is FAPI but would not be AII if earned directly by a CCPC

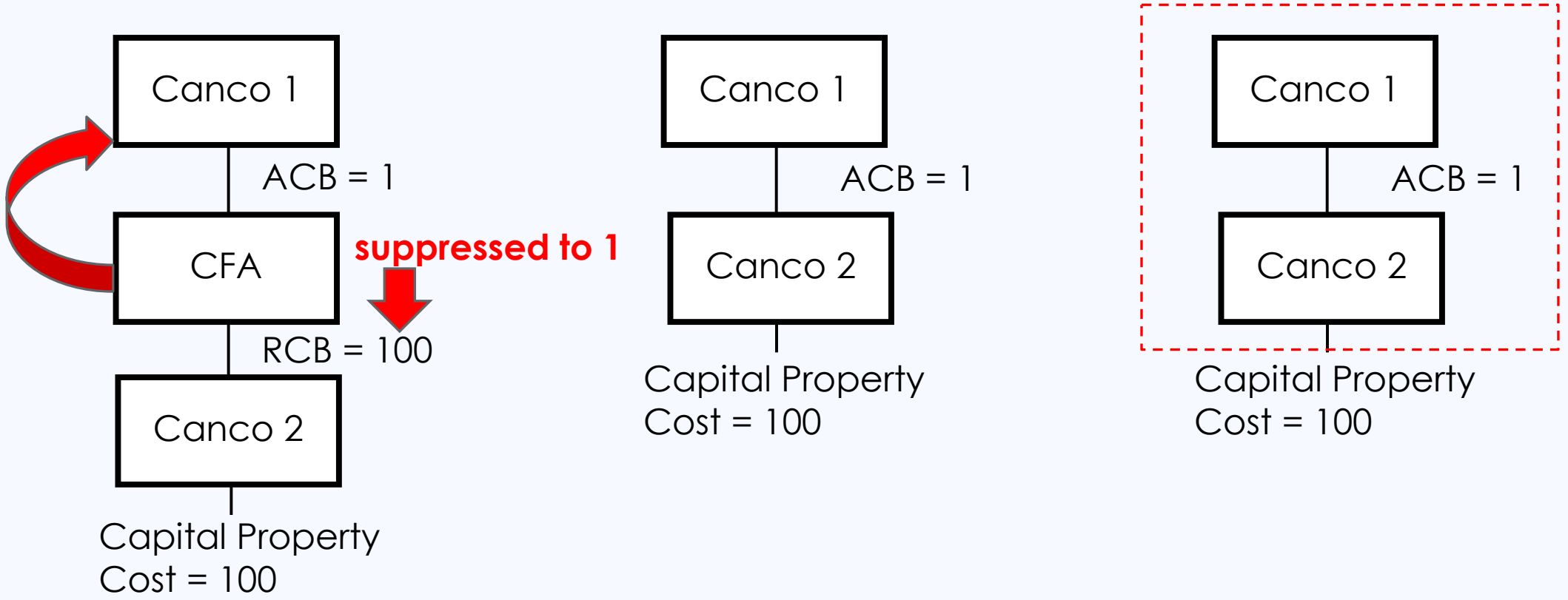
PROPOSED S. 88(3.3) AMENDMENT

- On liquidation and dissolution of a first-tier FA that is a QLAD
  - Proceeds to Canco for CFA shares = cost to CFA of its property
  - Can file s. 88(3.3) election to suppress the cost of capital property distributed by CFA to reduce proceeds to Canco for CFA shares



PROPOSED S. 88(3.3) AMENDMENT

- PERCEIVED PROBLEM – GAIN ELIMINATION OR DEFERRAL



PROPOSED S. 88(3.3) AMENDMENT

- Proposed s. 88(3.3) amendment limits the availability of the suppression election to shares of other foreign affiliates
- However, this may be too narrow

QUESTIONS?

SPEAKER PROFILE

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