

## **SUMMARY TABLE OF CONTENTS**

Dedication .....	iii
Acknowledgments .....	v
Some Introductory Remarks on the Taxation of Corporations, Partnerships and Trusts .....	vii
Foreword to the First Edition .....	xvii
Summary Table of Contents .....	xix
Detailed Table of Contents .....	xxi
Table of Cases .....	xxxi
Table of Statutes .....	xlv
Chapter 1      First Principles and Best Practices .....	1
Chapter 2      Partnership Income .....	31
Chapter 3      Contributions to/Distributions from a Partnership .....	75
Chapter 4      Trust Income .....	127
Chapter 5      Contributions to/Distributions from a Trust .....	161
Chapter 6      Control, Residence and Classification of Corporations and of Income .....	191
Chapter 7      Arm's Length Dealings, Affiliated Persons, Associated Corporations and the Small Business Deduction .....	225
Chapter 8      Taxation of Corporate Distributions and Appropriations .....	265
Chapter 9      Integration of Corporation and Shareholder Taxes .....	305
Chapter 10     Dividend (Surplus) Stripping .....	327
Chapter 11     Capital Gains Stripping .....	355
Chapter 12     Tax Deferred Transfers/Exchanges/Conversions .....	387
Chapter 13     Amalgamations and Windings-Up .....	419
Index .....	453



## **DETAILED TABLE OF CONTENTS**

### **CHAPTER 1 — FIRST PRINCIPLES AND BEST PRACTICES**

1.1 The Art of Reading the <i>Income Tax Act</i> .....	4
(a) General Structure of the <i>Income Tax Act</i> .....	4
(b) Specific Provisions of the Act .....	6
(c) “Backing Into” the <i>Income Tax Act</i> .....	8
(d) Secondary Sources for Understanding the <i>Income Tax Act</i> .....	13
(e) Additional Considerations in Reading the <i>Income Tax Act</i> .....	14
(i) Preambles .....	14
(ii) Turns of Phrase .....	15
(iii) Defined Terms .....	17
(iv) Pro-rations .....	18
(v) Formulae .....	18
1.2 Interpreting the <i>Income Tax Act</i> .....	19
(a) Tax Law as an Accessory System.....	19
(b) Other Sources of Law .....	20
(c) Statutory Construction and the <i>Income Tax Act</i> .....	21
(i) The Rule of Strict Construction .....	22
(ii) <i>Stubart</i> and the Rejection of Strict Construction .....	23
(iii) The “Modern” Rule and the Legacy of <i>Stubart</i> .....	24
(iv) Current State of the Law .....	26
1.3 Concluding Remarks .....	28
Review Questions .....	29

### **CHAPTER 2 — PARTNERSHIP INCOME**

2.1 Nature of a Partnership .....	33
(a) “Between Persons” .....	37
(i) Tiered Partnership Structures .....	37
(ii) Can a Trust be a Partner? .....	39
(b) “A Business”.....	40
(c) “With a View to Profit” .....	41
(d) Foreign Law .....	44
2.2 Partnership a “Person” for Income Computation Purposes .....	45

## Detailed Table of Contents

(a) Introduction .....	45
(b) Taxpayer .....	47
(c) Person .....	47
(d) Individual .....	47
(e) Corporation .....	48
2.3 Fictions Created by Subsection 96(1) .....	48
(a) Partnership a Separate Person — 96(1)(a) .....	49
(b) Taxation Year a Fiscal Period — 96(1)(b) .....	53
(c) Each Activity Carried on by Partnership as a Separate Person — 96(1)(c) .....	54
(d) Miscellaneous — 96(1)(d), (e) and (e.1) .....	55
(e) Flow-through of Source to Partner — 96(1)(f) and (g) .....	56
Example 2.3-1 — Subsection 96(1) .....	58
2.4 Preferential Allocations of Partnership Income/Loss .....	58
Example 2.4-1 — Subsection 96(1) .....	59
Example 2.4-2 — Subsection 96(1) .....	60
2.5 Payments to a Retired Partner .....	61
(a) Effect of Withdrawal at Law .....	61
(b) Allocation of Partnership Income to a Retired Partner under Subsection 96(1.1) .....	61
(c) Treatment of Payments to a Retired Partner if Subsection 96(1.1) Not Applicable .....	65
2.6 Attribution — 96(1.8) .....	66
2.7 At-Risk Rules .....	67
(a) Partnership Losses versus Partnership Liabilities .....	67
(b) At-Risk Rules .....	68
2.8 Anti-Avoidance — Section 103 .....	69
2.9 Concluding Remarks .....	71
Review Questions .....	73
<b>CHAPTER 3 — CONTRIBUTIONS TO/DISTRIBUTIONS FROM A PARTNERSHIP</b>	
3.1 Nature of a Partnership Interest .....	77
3.2 Transfers of Property to or from a Partnership — Subsections 97(1) and 98(2) .....	82
Example 3.2-1 — Subsection 98(2) .....	85
3.3 Transfers of Property to a Partnership under Subsection 97(2) .....	86

## Detailed Table of Contents

(a) Overview .....	86
(b) Elected Amount — 85(1)(a) as Modified for Partnerships .....	89
(c) Elected Amount — 85(1)(b) as Modified for Partnerships .....	90
Example 3.3-1 — Subsection 97(2) .....	90
(d) Elected Amount — 85(1)(c) as Modified for Partnerships .....	91
Example 3.3-2 — 85(1)(c) as Modified by 97(2)(a) .....	92
(e) Loss Limitation Rules as Modified for Partnerships .....	92
(f) Benefit Conferred on Related Person — 85(1)(e.2) as Modified for Partnerships .....	93
Example 3.3-3 — Paragraph 85(1)(e.2) as Modified for Partnerships .....	94
(g) Paragraph 85(1)(e.3) as Modified for Partnerships .....	95
(h) Cost of Boot — 85(1)(f) as Modified for Partnerships .....	95
(i) Adjustments to Cost of Partnership Interest — 97(2)(b) .....	96
Example 3.3-4 — Paragraph 85(1)(f) and 97(2)(b) .....	96
3.4 Adjusted Cost Base of a Partnership Interest .....	98
(a) Deemed Gain — Subsections 40(3.1) and 40(3.11) .....	99
(b) Adjustments in Computation of Adjusted Cost Base of Partnership Interest — Section 53 .....	101
Example 3.4-1 — Cost Adjustments under Paragraph 53(1)(e) .....	102
Example 3.4-2 — Adjustments under Section 53 .....	103
3.5 Partner Withdrawal/Partnership Dissolution .....	104
(a) Time of Partnership Dissolution .....	104
(b) Income Tax Implications of Partnership Dissolution or Partner Withdrawal .....	104
(c) Subsection 98(1) — Partnership Dissolution .....	107
3.6 Tax-Deferred Partnership Dissolutions .....	109
(a) Conversion of a Partnership to a Co-ownership or Proprietorship .....	110
Example 3.6-1 — Subsection 98(3) .....	116
(b) Incorporation of a Partnership .....	117
(c) Replacement of Partnership .....	120
3.7 Elections .....	121
3.8 Concluding Remarks .....	121
Review Questions .....	123
<b>CHAPTER 4 — TRUST INCOME</b>	
4.1 Introduction .....	129

## Detailed Table of Contents

4.2 Meaning of “Trust” .....	131
4.3 Graduated Rate Estate Regime .....	136
4.4 Trust a “Taxpayer” .....	138
4.5 Trust Income Payable to a Beneficiary — Taxation of Beneficiary .....	141
4.6 Trust Income Payable to a Beneficiary — Taxation of Trust .....	146
4.7 Income Deemed not Paid — Subsection 104(13.1) and (13.2)	
Designations .....	148
4.8 Source and Character of Trust Income .....	150
(a) General Rule .....	150
(b) Dividends from Taxable Canadian Corporations .....	151
(c) Net Taxable Capital Gains .....	151
(d) Non-taxable Dividends .....	153
(e) Trust Benefits .....	154
4.9 21-Year Deemed Disposition Rule .....	155
(a) Introduction .....	155
(b) Pre-1972 Spousal Trusts, Post-1971 Partner Trusts, Joint Partner Trusts, Alter-Ego Trusts & “Self-Benefit” Trusts .....	156
4.10 Anti-Avoidance .....	159
4.11 Concluding Remarks .....	160
<b>CHAPTER 5 — CONTRIBUTIONS TO/DISTRIBUTIONS FROM A TRUST</b>	
5.1 Introduction .....	163
5.2 Classification of Trusts .....	163
(a) Personal Trusts .....	163
(b) Unit Trusts .....	165
(c) Employment-Related Benefits Trusts .....	166
5.3 Contributions of Property to a Trust .....	167
(a) Default Scheme .....	167
(b) Exceptions to Default Scheme .....	170
(i) Qualifying Transfer .....	170
(ii) Qualifying Disposition .....	172
5.4 Disposition of Trust’s Interests .....	173
5.5 Income Interests .....	173
(a) Cost of Income Interest .....	174
(b) Disposition of Income Interest .....	175
5.6 Capital Interests .....	177

## Detailed Table of Contents

(a) Capital Interest Defined .....	177
(b) Disposition of Capital Interest .....	177
(c) Cost of Capital Interest .....	178
(d) Personal Trust or Prescribed Trust — Subsection 107(1.1) .....	179
(e) Trusts Generally — Subsection 107(1) .....	180
(f) Distributions In Satisfaction of Capital Interest .....	183
Example 5.6-1 .....	186
Example 5.6-2 .....	187
5.7 Concluding Remarks .....	188
Review Questions .....	190
<b>CHAPTER 6 — CONTROL, RESIDENCE AND CLASSIFICATION OF CORPORATIONS AND OF INCOME</b>	
6.1 Introduction .....	193
6.2 Classification of Income .....	194
6.3 Corporate Residence .....	196
(a) Common Law Residence.....	196
(b) Deemed Residence under the Act .....	198
6.4 Concepts of Control.....	199
(a) <i>De Jure</i> Control .....	200
(i) Shares Held by a Corporation.....	201
(ii) Shares Held by a Trust .....	202
(iii) Shares Held by a Partnership .....	203
(iv) Other Issues .....	204
(b) <i>De Facto</i> Control .....	206
(c) Deemed Control .....	213
6.5 Classification of Corporations .....	214
(a) Private Corporation .....	214
(b) Public Corporation .....	214
(c) Canadian Corporation .....	215
(d) Canadian-Controlled Private Corporation .....	215
6.6 Corporate Rates of Tax .....	217
(a) Basic Federal Rate .....	217
(b) Provincial Abatement .....	217
(c) General Rate Reduction .....	218
(d) Additional Refundable Tax .....	218

## Detailed Table of Contents

(e) Small Business Deduction .....	218
6.7 Concluding Remarks .....	219
Review Questions .....	221
<b>CHAPTER 7 — ARM'S LENGTH DEALINGS, AFFILIATED PERSONS, ASSOCIATED CORPORATIONS AND THE SMALL BUSINESS DEDUCTION</b>	
7.1 Introduction .....	225
7.2 Arm's Length Dealings .....	226
7.3 Related Persons .....	229
Example 7.3-1 — Subsection 251(2).....	231
7.4 Affiliated Persons .....	232
(a) Definition of "Affiliated Persons" .....	232
(b) Superficial Loss .....	235
(c) Subsections 40(3.3) to (3.6) .....	237
(d) Stop-Loss System in Section 112 .....	240
7.5 Associated Corporations .....	242
(a) Specified Class .....	243
(b) Deeming Rules for Association Purposes .....	243
Example 7.5-1 — Paragraph 256(1.2)(c) .....	245
7.6 The Small Business Deduction .....	249
(a) Introduction .....	249
(b) Income of the Corporation for the Year from an Active Business .....	250
(c) Active Business Carried on by a Corporation .....	253
(d) Specified Investment Business .....	253
(e) Personal Services Business .....	256
(f) Specified Partnership Income/Specified Corporate Income .....	257
(g) Taxable Income Exempt from Federal Tax .....	259
Example 7.6-1 — Paragraph 125(1)(b) .....	260
(h) Business Limit .....	260
7.7 Concluding Remarks .....	261
Review Questions .....	262
<b>CHAPTER 8 — TAXATION OF CORPORATE DISTRIBUTIONS AND APPROPRIATIONS</b>	
8.1 Corporate Distributions .....	267
(a) Overview .....	267
Example 8.1-1 — Integration .....	274

## Detailed Table of Contents

(b) Dividends in Kind .....	275
(c) Stock Dividends .....	275
(d) Paid-up Capital .....	278
Example 8.1-2 — “Paid-up Capital” Subsection 89(1) .....	281
(e) Capital Dividends .....	282
8.2 Deemed Dividends .....	288
(a) Overview .....	288
(b) Paid-up Capital Reductions .....	288
(c) Purchase, Redemption or Other Acquisition of Shares .....	289
(d) Winding-up Distributions .....	291
(e) Dispositions on a Purchase, Redemption or Cancellation of Shares .....	292
.....	292
Example 8.2-1 — Gain Realized on Redemption of Shares .....	293
(f) Paid-up Capital Increases .....	293
(g) Miscellaneous Provisions in Section 84 .....	295
8.3 Shareholder Benefits .....	296
8.4 Shareholder Debt .....	300
8.5 Concluding Remarks .....	302
Review Questions .....	304
<b>CHAPTER 9 — INTEGRATION OF CORPORATION AND SHAREHOLDER TAXES</b>	
9.1 Introduction .....	307
9.2 Dividend Gross-up and Tax Credit .....	310
Example 9.2-1 — Example of integration assuming a 20% corporate tax rate and a 30% individual tax rate .....	310
9.3 Refundable Tax .....	315
(a) Refundable Tax on Aggregate Investment Income of a CCPC .....	315
(b) Refundable Dividend Tax on Hand .....	316
(c) Part IV Tax .....	319
Example 9.3-1 — Part IV Tax .....	322
(d) Dividend Refund .....	322
Review Questions .....	325
<b>CHAPTER 10 — DIVIDEND (SURPLUS) STRIPPING</b>	
10.1 Introduction .....	329
10.2 Pre-1972 Tax Reform .....	331
10.3 Post-1972 Tax Reform .....	334

## Detailed Table of Contents

Example 10.3-1 — Section 84.1 .....	340
10.4 General Anti-Avoidance Rule .....	345
10.5 Provisions that Limit Paid-up Capital Increases .....	348
Example 10.5-1 — Subsection 85(2.1) .....	350
Example 10.5-2 — Paragraph 85(2.1)(b).....	352
10.6 Concluding Remarks .....	353
Review Questions .....	354
<b>CHAPTER 11 — CAPITAL GAINS STRIPPING</b>	
11.1 Introduction .....	357
11.2 The Incentive to Capital Gains Strip .....	357
11.3 History of Section 55 .....	360
11.4 Subsection 55(2) Dissected .....	361
First Condition .....	365
Second Condition .....	366
Third Condition [First Alternative] .....	371
Third Condition [Second Alternative].....	373
Third Condition [Third Alternative] .....	373
Fourth Condition .....	374
Fifth Condition .....	374
11.5 Safe Income Related Issues .....	375
(a) Income Earned or Realized .....	375
(b) Safe Income On Hand .....	377
(c) Safe Income Determination Time .....	380
(d) Consolidated Approach .....	382
(e) Allocation of Safe Income .....	383
11.6 Supporting Provisions .....	384
11.7 Concluding Remarks .....	385
Review Questions .....	386
<b>CHAPTER 12 — TAX DEFERRED TRANSFERS/EXCHANGES/CONVERSIONS</b>	
12.1 Introduction .....	389
12.2 Price Adjustment Clauses .....	389
12.3 Types of Property and their Respective Cost Amounts .....	392
(a) Tax Value versus Book Value .....	392
(b) Non-depreciable Capital Property or Inventory.....	394

## Detailed Table of Contents

(c) Depreciable Property .....	394
12.4 Transfers of Property to a Corporation under Section 85 .....	395
(a) Conditions of Rollover .....	395
(b) Property Eligible for Rollover.....	396
(c) Elected Amount.....	398
(d) Significance of Elected Amount .....	398
Example 12.4-1 — Paragraphs 85(1)(f), (g) and (h) .....	399
(e) Adjustments to Elected Amount .....	400
Example 12.4-2 — Paragraph 85(1)(e.2) .....	404
(f) Late-Filed and Amended Elections .....	406
(g) Intersection of Federal and Provincial Elective Provisions and Inter-Provincial Tax Avoidance .....	406
12.5 Share for Share Exchange under Section 85.1.....	407
(a) Conditions for Rollover.....	407
(b) Exclusions from Rollover .....	408
12.6 Conversions/Exchanges under Section 51/51.1 .....	409
12.7 Conversions/Exchanges under Section 86 .....	413
12.8 Concluding Remarks .....	416
Review Questions .....	417
<b>CHAPTER 13 — AMALGAMATIONS AND WINDINGS-UP</b>	
13.1 Introduction .....	421
(a) Amalgamations .....	421
(b) Windings-up .....	423
13.2 Qualifying Amalgamations — Section 87 .....	425
(a) Carry Over of Tax Attributes of Property of a Predecessor Corporation .....	433
(b) Carry Over of Tax Profiles of Each Predecessor Corporation .....	434
(c) Shareholder Level Tax Consequences .....	435
13.3 Windings-up .....	437
(a) Tax Deferred Windings-up — Subsection 88(1) .....	438
(b) Taxable Windings-up — Subsections 84(2) and 88(2) .....	448
13.4 Concluding Remarks .....	450
Review Questions .....	451
<b>INDEX .....</b>	<b>453</b>