

TABLE OF CONTENTS

<i>Dedication</i>	iii
<i>Preface</i>	v
<i>Table of Cases</i>	xxi
<i>Table of Statutory References</i>	xlvi
1 INTRODUCTION	1
1.1 General.....	1
1.2 Arrangements	3
1.3 Draft Legislation	4
2 NON-ARM'S LENGTH TRANSFERS OF PROPERTY	5
2.1 The Non-Arm's Length Concept.....	5
2.1.1 Related Persons	6
(a) <i>De Jure</i> Control of a Corporation	8
(b) Control by an Unrelated Group	12
(c) Rights in Respect of Shares	13
(d) Amalgamations.....	17
2.1.2 Non-Arm's Length in Fact	18
(a) Common Mind.....	18
(b) Accommodation Party	20
(c) Acting in Concert without Separate Interests.....	21
(d) <i>De Facto</i> Control.....	27
(e) Shareholders and Corporations.....	30
(f) Partnerships.....	31
2.1.3 Trusts	32
2.2 Section 69(1).....	34
2.3 Section 69(11).....	37
2.4 Price Adjustment Clauses.....	40
2.5 Affiliated Persons	43
2.5.1 Individuals.....	43
2.5.2 Corporations	44
2.5.3 Partnerships.....	45
2.5.4 Trusts	46
2.6 Stop-Loss Rules.....	48
2.6.1 Non-Depreciable Capital Property	49
(a) Suspended Losses: Section 40(3.4).....	49
(b) Superficial Losses: Section 40(2)(g)(i)	53
(c) Identical Property	55

	(d) Repurchase or Redemption of Shares: Section 40(3.6)	58
	(e) Shares of a Controlled Corporation: Section 40(2)(h)	60
	(f) Prescribed Shares: Section 40(2)(i)	60
	(g) Certain Bonds and Debentures: Section 40(2)(d)	61
	(h) Related-Party Debt: Section 40(2)(e.1)	61
	(i) Commercial Obligations: Section 40(2)(e.2)	63
	(j) Non-Income Earning Debt: Section 40(2)(g)(ii)	64
2.6.2	Depreciable Property	69
	(a) Buildings: Section 13(21.1)	69
	(b) Terminal Losses: Section 13(21.2)	73
2.6.3	Class 14.1 Depreciable Property: Sections 14(12) and 13(42)(b)	76
2.6.4	Dividend Stop-Loss Rules	78
	(a) Natural Persons and Corporations	79
	(b) Partnerships	83
	(c) Trusts	87
	(d) Grandfathered Shares	91
	(e) Exchanged Shares	91
	(f) Non-Resident Individuals	92
2.6.5	Certain Inventory: Section 18(15)	92
2.7	Non-Arm's Length Transfer of Depreciable Property: Section 13(7)(e)	94
2.8	Class 14.1 Depreciable Property	97
	(a) Non-Arm's Length Transfers	97
	(b) Rollover to Controlled Corporation: Section 24(2)	100
2.9	Non-Arm's Length Transfer to Defeat Tax Liability	100
3	TAX DEFERRED ROLLOVERS: SECTION 85(1)	109
3.1	Eligible Transferors and Transferees	110
3.2	Eligible Property	111
	3.2.1 Capital Property	112
	3.2.2 Shares of the Transferee	113
	3.2.3 Right to Income and Accounts Receivable	113
	3.2.4 Real Property	115
	3.2.5 Partnership Interests	117
3.3	Agreed Amount	118
	3.3.1 General Deeming Rules on Agreed Amounts	118

3.3.2	Specific Deeming Rules for Certain Kinds of Property	120
	(a) Inventory and Non-Depreciable Capital Property	120
	(b) Farm Inventory	120
	(c) Depreciable Property	121
	(d) Passenger Vehicles	123
3.3.3	Priority of Deeming Rules	123
3.3.4	Order of Disposition of Properties	124
3.3.5	Consequences Where Benefit Conferred on a Related Person	125
3.4	Shareholder Benefit	128
3.5	V-Day Amounts	129
3.6	Consideration Received by Taxpayer	130
3.6.1	Timing of Share Issuance.....	130
3.6.2	Determination of the Taxpayer's Cost of Consideration	131
	(a) Cost of Boot.....	131
	(b) Cost of Preferred Shares	131
	(c) Cost of Common Shares.....	133
3.6.3	Paid-up Capital of Shares Received	133
3.6.4	Taxable Canadian Property	135
3.6.5	Capital Property or Inventory.....	135
3.7	Property Received by Transferee Corporation.....	136
3.8	Deemed Dividends under Section 84.....	136
3.9	Partnership Transfers and Wind-ups: Sections 85(2) and (3)..	137
3.10	Election	140
3.10.1	Mechanics of the Election.....	140
3.10.2	Listing of Transferred Properties	142
4	CAPITAL REORGANIZATIONS	145
4.1	Section 86: Exchange of Shares in a Reorganization of Capital	145
4.1.1	Eligible Transferors and Corporations	147
4.1.2	Disposition of All of the Shares of the Class Held by the Taxpayer	147
4.1.3	Reorganization of the Capital of the Corporation	149
4.1.4	Indirect Gift	150
4.1.5	Shareholder Benefit	153
4.1.6	Paid-up Capital of New Shares	154
4.1.7	Deemed Dividend	156
4.1.8	Preservation of Reduced Cost for Debt Forgiveness Purposes.....	156

4.1.9	Shares Held Since 1971	157
4.1.10	Comparison with Section 85	157
4.2	Share Issuances and Option Grants	158
4.2.1	Option to Acquire Securities of Another Corporation.....	161
4.2.2	Option to Acquire Securities of the Granting Corporation.....	162
4.2.3	Shareholder and Employee Benefits	163
4.2.4	Put Options	165
4.2.5	Non-Arm's Length Option Grants	165
4.3	Section 51: Convertible Property.....	166
4.3.1	Eligible Transferors and Corporations	169
4.3.2	Indirect Gift	169
4.3.3	Shareholder Benefit	171
4.3.4	Paid-up Capital of the Acquired Shares	171
4.3.5	Convertible Property Held Since 1971.....	172
4.4	Section 51.1: Debt Obligation Conversions	172
4.5	Non-Resident Withholding Tax on Convertible Debt.....	174
4.6	Stock Splits and Consolidations.....	178
4.7	Stock Dividends.....	179
4.7.1	Shareholder Benefit on the Payment of a Stock Dividend.....	183
4.8	Capitalization of Surplus: Section 84(1)	184
4.8.1	Exceptions under Section 84(1)	186
4.9	Redemption of Shares: Section 84(3).....	189
4.10	Returns of Capital	193
4.10.1	Private Corporations: Section 84(4).....	193
4.10.2	Public Corporations: Section 84(4.1).....	194
4.10.3	Preferred Shares: Sections 84(4.2) and (4.3).....	197
4.11	Section 86.1: Foreign Spin-offs	198
5	SURPLUS STRIPPING.....	203
5.1	Section 84.1	203
5.1.1	Relevant Transferors and Transferees	204
5.1.2	Non-Arm's Length	205
	(a) Factual Non-Arm's Length.....	205
	(b) Expanded Meaning of Non-Arm's Length for Section 84.1.....	208
	(c) Expanded Meaning of Non-Arm's Length for Section 84.1(2)(a.1).....	210
5.1.3	"Connected" Corporations	210
5.1.4	Paid-up Capital Reduction.....	212
5.1.5	Deemed Dividend	214

5.1.6	Capital Dividends, Eligible Dividends and RDTOH	217
5.1.7	Arm's Length Adjusted Cost Base	218
5.2	Section 212.1: Non-Arm's Length Sales of Shares by Non-Residents	221
6	SHARE FOR SHARE EXCHANGES—SECTION 85.1	225
6.1	Domestic Exchanges	225
6.1.1	Vendor Must Be a "Taxpayer"	228
6.1.2	Effect on Vendor	229
6.1.3	Effect on Purchaser	228
6.1.4	Paid-up Capital of Issued Shares	231
6.2	Exchanges Involving Foreign Affiliates	232
6.3	Foreign Exchanges	234
6.4	Cross-Border Share-for-Share Exchanges	237
7	AMALGAMATIONS	241
7.1	Definition	241
7.2	Amalgamated Corporation	258
7.2.1	Taxation Year	258
7.2.2	Inventory	260
7.2.3	Income Computation	261
7.2.4	Depreciable Property	262
7.2.5	Capital Property	274
7.2.6	Partnership Interests	274
7.2.7	Property Used in an Insurance or Money Lending Business	276
7.2.8	Certain Property of Financial Institutions	276
7.2.9	Eligible Capital Property	276
7.2.10	Reserves	277
	(a) General	278
	(b) Bad Debts	278
	(c) Doubtful Debts	279
	(d) Contingent Reserves for Banks and Insurers	279
	(e) Properties Sold in the Course of Business	280
	(f) Undelivered Goods and Services	280
	(g) Capital Properties	281
	(h) Quadrennial Surveys	282
	(i) Uncollectible Proceeds	282
	(j) Credit Unions	283
7.2.11	Holdbacks	283
7.2.12	Interest Income	284
7.2.13	Prepaid Expenses	284
7.2.14	Injected Substances	285

xii TABLE OF CONTENTS

7.2.15	Employee Benefit Plans	286
7.2.16	Lease Cancellation Payments	287
7.2.17	Inducement Payments and Government Assistance.....	287
7.2.18	Ineligible Partnership Transfers.....	288
7.2.19	Cooperative Corporations.....	289
7.2.20	Financial Institutions.....	289
7.2.21	Income Attribution.....	288
7.2.22	Employee Payments.....	290
7.2.23	Scientific Research and Experimental Development	291
7.2.24	Replacement Property.....	291
7.2.25	Warranty Outlays	292
7.2.26	Options.....	292
7.2.27	Foreign Affiliate Shares	293
7.2.28	Resource Properties	294
7.2.29	Interest Expense	298
7.2.30	Penalties, Bonuses, and Rate Reduction Payments	299
7.2.31	Charitable Donations.....	299
7.2.32	Debts of a Predecessor.....	300
7.2.33	Public Corporation Status.....	303
7.2.34	Livestock	304
7.2.35	Fuel Tax Rebates.....	305
7.2.36	Losses.....	305
	(a) Restricted Farm Loss and Farm Loss	305
	(b) Non-Capital Loss and Net Capital Loss	306
	(c) Dividends on Shares	310
	(d) Losses on Certain Shares	310
	(e) Superficial Losses	311
7.2.37	Corporate Loss Trading.....	311
7.2.38	Tax Credits.....	311
	(a) Small Business Deduction	311
	(b) Manufacturing and Processing Profits Deduction.....	313
	(c) Investment Tax Credit	313
	(d) Foreign Tax Credit	314
	(e) Large Corporations Tax and Financial Institutions Tax	315
7.2.39	Special Tax Accounts.....	316
	(a) Capital Dividend Account	316
	(b) Refundable Dividend Tax on Hand	317

	(c) Pre-1972 Capital Surplus on Hand.....	318
	(d) Contributed Surplus	319
	(e) GRIP and LRIP	319
7.2.40	Special Corporations.....	320
	(a) Mutual Fund Corporation.....	320
	(b) Investment Corporations	320
	(c) Non-Resident-Owned Investment Corporation.....	320
	(d) Life Insurance Corporation.....	321
7.2.41	Parts III and III.1 Tax.....	321
7.2.42	Parts IV.1 and VI.1 Tax on Taxable Preferred Shares.....	322
7.2.43	Transfer of Part VI.1 Tax Liability	322
7.2.44	Paid-Up Capital	322
7.2.45	Functional Currency Rules	326
7.2.46	Superficial Losses	327
7.2.47	Instalment Deferral.....	327
7.2.48	Qualifying Environmental Trusts	328
7.2.49	Film and Video Productions	328
7.2.50	Section 80.....	329
7.2.51	Gift of a Non-Qualifying Security.....	329
7.2.52	SIFT Wind-Up Corporation	330
7.2.53	Eligible Derivatives	330
7.2.54	Balance-Due Date.....	330
7.2.55	Canada Pension Plan and Employment Insurance Payments	331
7.2.56	Use of Amalgamation to Access Tax Benefits	331
7.2.57	Goods and Services Tax	332
7.2.58	Non-Resident Trusts and Other Non-Resident Entities	332
7.2.59	Employees Profit Sharing Plan.....	333
7.3	Securityholders of Predecessor Corporations.....	333
	7.3.1 Proceeds of Disposition and Cost	333
	7.3.2 Term Preferred Shares	339
	7.3.3 Other Preferred Shares.....	340
	7.3.4 Rights to Acquire “Grandfathered” Shares	341
	7.3.5 Flow-Through Shares	342
	7.3.6 Options.....	343
	7.3.7 Tax-Deferred Shares of an Agricultural Co-operative Corporation.....	344
	7.3.8 Transitional Rules	345
	7.3.9 Creditors of Predecessor Corporations.....	346

7.3.10	Continuation of Listed Status	348
7.3.11	Flow-Through Entities.....	348
7.4	Triangular Amalgamations	349
7.5	Vertical Amalgamations.....	353
7.6	Foreign Mergers	353
8	CAPITAL GAINS STRIPS AND DIVISIVE REORGANIZATIONS	357
8.1	Capital Gains Strips: Section 55(2).....	357
8.1.1	Relevant Dividends: Section 55(2.1)(a)	361
8.1.2	Purpose of a Transaction or Series of Transactions: Section 55(2.1)(b)	362
	(a) The Purpose Test.....	362
	(b) Reduction of the Fair Market Value of a Share: Section 55(2.1)(b)(ii)(A).....	364
	(c) Increase in the Cost of Property: Section 55(2.1)(b)(ii)(B).....	365
8.1.3	Stock Dividends.....	367
8.1.4	Part IV Tax Exception.....	367
8.1.5	Safe Income Exception: Section 55(2.1)(c).....	367
	(a) Income Earned or Realized after 1971 and before the Safe-Income Determination Time.....	373
	(b) Uncertainties About Safe Income: Series of Dividends and Sections 55(5)(f) and 55(2.3)	383
	(c) Safe-Income Determination Time.....	386
8.2	“Divisive” Reorganizations: Overview and Historical Perspective.....	388
8.2.1	Types of Divisive Reorganizations	394
	(a) Section 55(3)(a) “Internal Butterfly” Reorganization	394
	(b) Section 55(3)(b) Butterfly Reorganization	394
8.2.2	Undefined Terms	397
	(a) “Reorganization”.....	397
	(b) “Series of Transactions”	400
	(c) “In Contemplation Of”.....	407
	(d) “Immediately Before” and “Immediately After”	409
8.3	The Section 55(3)(a) Exemption	413
8.3.1	Interpretive Rules	413
	(a) Unrelated Persons.....	415
	(b) Dividend Recipient	420

	(c) Amalgamations and Windings-up	421
	(d) Section 55(3.01): Proceeds of Disposition	422
	(e) “Series of Transactions” and “Immediately”	425
	(f) Significant Increase in the Total Direct Interest	425
8.3.2	Prohibited Transactions	428
	(a) Section 55(3)(a)(i)—Dispositions of Property	428
	(b) Section 55(3)(a)(ii)—Significant Increase in Interest in a Corporation	431
	(c) Section 55(3)(a)(iii)—Dispositions of Shares of the Dividend Payer or Derivative Property	433
	(d) Section 55(3)(a)(iv)—Dispositions of Shares of the Dividend Recipient or Derivative Property	435
	(e) Section 55(3)(a)(v)—Significant Increase in Direct Interest in Dividend Payer	437
	(f) GAAR Issues	437
8.4	The Section 55(3)(b) Exemption	438
8.4.1	Defined Terms	442
	(a) Distribution	442
	(b) Specified Class	447
	(c) Permitted Redemption	450
	(d) Permitted Exchange	454
	(e) Permitted Acquisition	467
	(f) Qualified Person	468
8.4.2	Types of Property	473
	(a) Consolidated Look-Through Approach	475
	(b) Valuation of Types of Property: Net Equity or Gross Equity	478
8.4.3	Divisive Reorganizations—The Butterfly Exemption: Section 55(3)(b)	481
	(a) Specified Corporations: Spin-Off Butterfly Reorganizations Involving Public Corporations and Their Subsidiaries	481
	(b) Section 55(3)(b): The Basic Exemption	484
	(c) Prohibition on Property Becoming Property: Section 55(3.1)(a)	485
	(d) Requirement for Continuity of Share Ownership: Section 55(3.1)(b)	492

	(e) Post-Butterfly Restrictions: Sections 55(3.1)(c) and (d)	516
9	WINDING-UP	531
9.1	Definition	531
9.2	Winding-up of Resident Corporation Where Section 88(1) Applies	534
9.2.1	Rules Applicable to the Subsidiary	535
9.2.2	Rules Applicable to the Parent	540
	(a) Shares of the Subsidiary	540
	(b) Cost to Parent of Property of the Subsidiary and Other Flow-Through Provisions.....	541
	(c) Carryover of Losses to Parent	547
	(d) The Bump	550
	(e) The Bump Denial Rule.....	563
9.2.3	Rules Applicable to Creditors	582
9.2.4	Rules Applicable to Minority Shareholders.....	582
9.3	Winding-up of Resident Corporations Where Section 88(1) Does Not Apply	583
9.3.1	Deemed Sale of Property	583
9.3.2	Deemed Dividend	584
9.3.3	Pre-1972 Capital Surplus on Hand.....	588
9.3.4	Deemed Disposition of Shares	589
9.3.5	Part XIII and Section 116.....	590
9.4	Liability of Legal Representatives and Clearance Certificates	592
9.4.1	Section 159	592
	(a) Requirement to Obtain Clearance Certificate.....	592
	(b) Legal Representatives	596
10	CONTINUANCE AND CORPORATE MIGRATION.....	601
10.1	Continuance within Canada.....	601
10.2	Corporate Emigration.....	602
10.2.1	Continuance Outside Canada.....	602
10.2.2	Deemed Disposition of Property	604
10.2.3	Deemed Year End	604
10.2.4	Foreign Exploration and Development Expenses/ Foreign Resources Expenses	605
10.2.5	Additional Tax on Corporate Emigration	605
10.3	Corporate Immigration.....	607
10.3.1	Continuance into Canada	607
10.3.2	Deemed Disposition of Property	607
10.3.3	Deemed Year End	607

10.3.4	Deemed Dividend by Canadian Subsidiary	608
10.3.5	Branch Tax.....	609
10.3.6	Adjustments to Paid-Up Capital	609
10.3.7	Deemed Dividend by the Corporation	610
10.3.8	Cost of Shares of the Corporation	611
10.3.9	Adjustments to Paid-up Capital: Foreign Affiliate Debt Dumping	611
10.3.9	Former Foreign Affiliate.....	612
<i>APPENDIX A</i>		614
11	ACQUISITIONS OF CONTROL	615
11.1	Control.....	615
11.2	Acquisition of Control Determination.....	617
11.2.1	Share Acquisitions, Redemptions and Cancellations, and Changes in Share Attributes ...	617
11.2.2	Amalgamations.....	623
11.2.3	Reverse Takeover Share Exchanges.....	625
11.2.4	SIFT Reverse Takeover Transactions.....	627
11.2.5	Other Share Exchanges	629
11.2.6	SIFT Trust Conversions	631
11.2.7	Corporation Without Share Capital	633
11.2.8	Change of Trustee	633
11.2.9	Loss Restriction Event in a Controlling Trust.....	635
11.2.10	Distribution of Securities from a Trust or Partnership	639
11.2.11	Bankruptcy.....	639
11.3	Consequences of an Acquisition of Control	639
11.3.1	Taxation Year-End	639
11.3.2	Expiration of Net Capital Losses	641
11.3.3	Expiry of ABILs.....	642
11.3.4	Streaming of Non-Capital Losses and Farm Losses.....	642
	(a) Non-Capital Losses from a Business	645
	(b) “That Business”	647
	(c) One Business or Multiple Businesses	647
	(d) Continuity of That Business.....	650
	(e) Reasonable Expectation of Profit.....	659
	(f) Deductible from Income from the Same or Similar Business	660
	(g) Meaning of Income	666
	(h) Substantially all the Income	668
	(i) Income Derived	669
11.3.5	Recognition of Accrued Losses	670

xviii TABLE OF CONTENTS

	(a) Non-Depreciable Capital Property	671
	(b) Depreciable Capital Property	672
	(c) Inventory	672
	(d) Accounts Receivable	673
	(e) Suspended losses	673
11.3.6	Recognition of Accrued Capital Gains and Recapture	674
11.3.7	Foreign Currency Debt	676
11.3.8	Debt Forgiveness	677
11.3.9	Scientific Research and Experimental Development Expenditures	678
11.3.10	Investment Tax Credits	679
11.3.11	Resource Expenses	680
11.3.12	Charitable Donation Deductions and Other Gifts	682
11.3.13	CCPC and Capital Dividend Account	682
11.3.14	Foreign Affiliates	683
11.4	Anti-Avoidance Rules	685
11.4.1	The General Anti-Avoidance Rule	685
11.4.2	Acquiring Control to Recognize Accrued Losses ..	688
11.4.3	Deemed Exercise of Rights	688
11.4.4	Resource Property Acquired Prior to the Acquisition of Control	689
11.4.5	Depreciable Capital Property Acquired Prior to the Acquisition of Control	690
11.4.5	Section 69(11)	691
12	THE ELIGIBLE DIVIDEND REGIME	695
12.1	Legislative Purpose	695
12.2	Essential Components	696
12.3	Eligible Dividends	697
12.3.1	Definition	659
12.3.2	Designation Requirement	697
12.3.3	Non-Resident Shareholders	699
12.3.4	Section 55(2)	700
12.4	GRIP	700
12.4.1	GRIP Definition	700
12.4.2	Opening 2006 GRIP Balance	701
12.4.3	Acquisition of a CCPC	703
12.5	LRIP	704
12.6	Section 89(11) Election	705
12.7	Status Changes (Sections 89(4) and 89(8))	707
12.7.1	Becoming a CCPC	707

12.7.2	Ceasing to be a CCPC	708
12.8	Amalgamations (Sections 89(5) and 89(9))	710
12.8.1	Amalgamated Corporation is a CCPC	710
12.8.2	Amalgamated Corporation is a Non-CCPC	711
12.9	Wind-ups (Sections 89(6) and 89(10)).....	711
12.9.1	Parent Corporation is a CCPC	712
12.9.2	Parent Corporation is a Non-CCPC	712
12.10	EEDD/Part III.1 Tax	712
12.10.1	Liability for Part III.1 Tax.....	712
12.10.2	Calculation of Part III.1 Tax	713
12.10.3	Relief from Part III.1 Tax.....	713
12.10.4	Anti-Avoidance and Part III.1 Tax	714
12.10.5	Shareholder Liability	714
12.10.6	Corporate Filing Obligation.....	715
12.11	Conclusion	715
13	EMPLOYEE STOCK OPTIONS	717
13.1	Overview of Section 7: Employee Stock Options	718
13.2	Tax Consequences to the Employee	719
13.2.1	Grant of Employee Stock Options	719
13.2.2	Exercise of Employee Stock Options.....	719
(a)	Partial Dispositions of Shareholdings.....	720
(b)	Relief from Taxation for Certain Dispositions of Shares	723
13.2.3	Dispositions of Employee Stock Options	726
13.2.4	Death of Employee Holding Employee Stock Option	732
13.2.5	Deduction in Computing Taxable Income.....	733
(a)	Employee Stock Options.....	733
(b)	CCPC Options.....	745
(c)	Charitable Donation of Shares Acquired on Exercise of Employee Stock Options.....	746
13.2.6	Adjusted Cost Base Considerations.....	748
13.3	Tax Consequences to Employer or Issuer.....	752
13.3.1	Consequences in Computing Income.....	752
13.3.2	Withholding Obligations	755
13.4	Employee Stock Options in the Context of Extraordinary Transactions.....	757
13.4.1	Exchanging Employee Stock Options: Section 7(1.4).....	757
(a)	Use of Exchanges under Section 7(1.4)	761
(b)	Interaction Between Section 7(1.4) and Deduction in Computing Taxable Income....	762

xx TABLE OF CONTENTS

	(c) Exchange of Employee Stock Options:	
	Issuer Considerations.....	764
13.4.2	Eliminating Options in the Context of a Cash Takeover Bid, Going Private Transaction, or other Significant Reorganization	764
	(a) Accommodating Exercise of Options	765
	(b) Surrender of Options for Cash.....	767
	(c) Cancellation of Options for No Consideration	773
13.4.3	Repricing Options.....	774
13.4.4	Stock Dividends, Subdivisions and Consolidations	779
<i>Index</i>		783