Tax Notes

January 2012
Number 588

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WHAT'S NEW

— *David Louis*

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Those of you who are regular readers of this newsletter may have noticed that I haven't done an article in the last few months. At the end of September 2011, a medical issue forced me to temporarily discontinue my writing.

As I left off,[1] I remember there being rather pressing issues: the CRA had given notice that it wasn't going to accept deferred year ends for joint ventures, but it offered little detail. Also, the *Copthorne* case, involving the "series of transactions" issue, had not been released, even though it was heard by the Supreme Court of Canada back in January 2011. But as I resumed reading tax releases, it seemed that, rather than dealing with these issues, the CRA was preoccupied with such matters as SIFT partnerships, as well as various nuances of the *Canada–U.S. Tax Treaty*. When I came across a CRA missive on asteroid mining, I figured I wasn't fully recovered; but it turned out that it was not a hallucination.[2]

Personal Services Business Rules

At the end of October 2011, the Department of Finance released some technical proposals.[3] Buried therein was a change to the personal services business provisions[4] — it seems that, for companies with taxation years beginning after October 31, 2011, personal services business income will no longer qualify for the corporate general rate reduction under subsection 123.4. In effect, there will be a surtax of 13%[5] of personal services business income, compared to other forms of business income. This was the subject of a recent article in *Tax Topics* No. 2071, "Should I Be Taking It Personally?" by Jesse Brodlieb. As the article commented, if the personal services business rules apply, there will now be a serious degree of underintegration.[6] I find this curious — the government had recently taken steps to provide that integration occurs with all major forms of income. Now it seems there will be one notable exception.

So in effect, while income from the incorporation of a personal service business may enjoy a significant element of deferral, if the "personal services business" rules apply — basically, if an employer–employee relationship would exist but for the corporation — there will be serious penalties.[7] Thus, pre-existing arrangements that could trigger the new rules should be reconsidered; clients should understand the downside risks. In many cases, the applicability of the personal services business rules will be unclear, leading taxpayers and their advisers to avoid the downside risks — presumably that's the point of these harsh proposals. One may also expect a spate of CRA ruling requests.[8]

RRSPs and Bill C-13

Also during my hiatus, a further round of legislation to implement certain portions of the 2011 federal Budget[9] came out.[10] I commented on the changes that would apply to RRSPs in my last article.[11] By and large, there are few changes to the RRSP legislation. However, one notable change is the extension of the deadline for "swapping" RRSP investments that would otherwise trigger the new RRSP penalties under Part XI.01 of the Act (for example, trading personally held investments for prohibited RRSP investments that would trigger the advantage tax on income or gains). The deadline for such swaps has been extended from the end of 2012 to 2021.[12] In addition, if the investment was a prohibited investment on March 23, 2011, the tax break on transitional prohibitive investment benefits will likewise apply to income earned or gains realized to the end of 2021, rather than 2017 as was previously proposed.[13]

One word of warning: other than the limited exceptions, the process of swapping — trading personally held investments[14] with your RRSP — will bring about the confiscation of 100% of the increase in value of investments in your RRSP attributable to swap transactions.[15] I used to recommend swapping as an expeditious way to realign RRSP investments — for example, swapping high-tax personally held investments so that they are held by your RRSP, in return for low-tax investments from your RRSP (a recommendation still repeated on some Web sites). Unfortunately, this tax planning avenue is all but foreclosed — I guess because some bureaucrat or academic saw a ghost.

Also, as noted in my last article, it appears that certain changes to the Regulations indicate that, if a corporation ceases to be a "specified small business corporation",[16] the investment will become a prohibited investment if it was acquired after March 22, 2011. In other words, this seems to mean that constant monitoring of the investment's status[17] to make sure it is onside with the Regulations will be required. Since no changes have been made to the Regulations, this issue appears to be "live". When private corporations were first allowed as qualified investments, a similar requirement had to be met, so that monitoring for qualified investment status was required. In many or most cases, this requirement jeopardized the viability of private corporations as investments in RRSPs — until the rules were liberalized some years later. It appears that we may be back to the future on this scenario.

Joint Ventures

But what about additional detail on the joint venture revisions? The release of the *Copthorne* case? In a document dated November 29, 2011,[18] the CRA released further details on the new administrative policy regarding deferred fiscal year ends for joint ventures. The release itself indicates that, for joint venturers with taxation years ending after March 22, 2011, it will be required that income from joint ventures be calculated for each participant taxpayer based on the fiscal period of that particular taxpayer — that is, deferred joint venture year ends will not be recognized. However, transitional relief similar to the partnership rules[19] will potentially apply, so that a deferral will be offered.

The income that may generally apply for this transitional relief will be based on actual additional income for the stub period to the extent that the amount would not otherwise have been included in income (that is, under the pre-existing administrative policy) for the first taxation year that ends after March 22, 2011. The CRA goes on to observe that, like the partnership proposals, this transitional relief would generally result in no additional income being included for the first taxation year of the participant taxpayer. Instead, the participant taxpayer will bring in the additional income over the next five years.[20]

The release goes on to say that, in order to avail itself of this transitional relief for the first taxation year ending after March 22, 2011, a participant taxpayer will be required to file an election in writing, on or before the filing due date for that taxation year, by attaching a letter to their return for that taxation year.[21] If a return has already been filed, or if the return is filed electronically, an eligible participant will be required to send a letter to their Taxation Centre indicating their election to benefit from this administrative policy. But a failure to report *all* of the accrued income in a participant's first taxation year that ends after March 22, 2011, in accordance with this administrative policy, will render the participant taxpayer ineligible for transitional relief. Note also that the release says that policies similar to the above will apply where a partnership is a participant in a joint venture.

This administrative policy raises some important questions. For one thing, it would be impractical, if not impossible, for many joint venturers (for example, minority participants with small interests) to calculate income based on the joint venturer's particular taxation year. The release makes no mention of doing an approximation based on principles similar to the new partnership rules (that is, estimating the current income based on the previous year's partnership income, subject to subsequent adjustments), even though in many cases there would be no practical alternative to using this method.[22] The release says that failure to report "all of the accrued income in a participant's first year that ends after

March 22, 2011" will result in the taxpayer's ineligibility for transitional relief. If an approximation (for example, using principles similar to the proposed partnership rules) turns out to be an underestimation of this income, query whether the taxpayer will be ineligible for transitional relief.[23]

Copthorne

Finally, after months of waiting, the *Copthorne*[24] case has come out — nearly a year after it was heard by the Supreme Court. Based on recent experience, I find that the longer it takes for the top court to produce a judgment, the less favourable it is. *Copthorne* was no exception.

But I'm getting ahead of myself. *Copthorne* involved an offshore strip of paid-up capital ("PUC") facilitated by earlier "set up" transactions involving the conversion of a would-be vertical amalgamation of two corporations to a horizontal amalgamation, which had the effect of increasing PUC.[25] The later transactions (that is, the actual offshore strip) in fact had depended on unforeseen legislation at the time the transactions were set up, so that the set up transactions, which were observed to effect a "double count" of some $67 million in PUC, were "just in case".

In effect, the CRA used hindsight to reassess the offshore strip transactions as *part of the series* of transactions — a prerequisite for applying GAAR. Many tax practitioners had come to view the case as a heroic campaign against the "empire" (as it were — no less a luminary than Richard Pound, of international Olympic fame, argued the case).

But those looking for new hope in the future of GAAR were, no doubt, disappointed: holding against the taxpayer, the Supreme Court affirmed the "series of transactions" interpretation, which included an expansive interpretation of subsection 248(10) that allows the CRA to "tack on" transactions "contemplated" by the taxpayer. More precisely, the Supreme Court affirmed that you can "contemplate backwards". That is, the CRA can assess subsequent transactions (in this case, offshore strip) as part of the series if they were undertaken "because of"[26] a pre-existing series,[27] even if the particulars of the subsequent transactions were unforeseen at the time of the original series.[28]

Because of previous cases, the *Copthorne* decision is not new law, although it does reinforce the "contemplating backwards" test, which gives the CRA authority to use hindsight to reassess transactions based on the "series" concept. Besides GAAR itself, will the CRA use this ammunition to attack, say, a purification transaction? For example, otherwise tax-exempt intercorporate distributions of excess assets can become taxable, per subsection 55(2) of the Act, if the series of transactions involving the purification includes a third-party sale. So is the subsequent sale part of the same series as the purification, even if its particulars were unforeseen at the time of the purification?[29] The question may really be whether a specific victory in *Copthorne* — close to a case on point — will broaden the CRA's assessing activity.

I have dwelt on the "contemplating backwards" issue for a reason: years ago, in a discussion with a tax lawyer who I greatly respect, we concluded that you can't contemplate backwards — that is, the act of contemplating is a perspective concept. You are probably thinking the same thing, and at least one recent leading article holds the same view. But courtesy of scholarly dissertations, previously decided cases, and so on, the Supreme Court of Canada has decreed you can indeed contemplate backwards.

Some releases on the *Copthorne* case have put a favourable spin on it, focusing on its supposed restrictions and limitations on when GAAR will apply.[30] But I am struck by the simplicity of the fact situations in the last two cases to come before the Supreme Court — both of which the taxpayers lost. In *Copthorne*, rather than do a vertical amalgamation of two companies held by an offshore parent, the first-tier subsidiary transferred the second-tier subsidiary to the offshore parent, and the two companies in question were amalgamated horizontally, so as to attempt to preserve the second-tier subsidiary's PUC. The second case (*Lipson v. The Queen*, 2009 DTC 5015) involved a "spousal flip": a wife took out a loan to buy shares from her husband to get an interest deduction.[31] Both of these fact situations brought the wrath of the highest court in the land. The fact that some commentators find solace in the fine print gives me little comfort.

My Rick Perry Moment

A belated correction to my last article. I confused the date of the release of legislation in respect the spring federal Budget proposals (August 16, 2011) with the date of the foreign affiliate proposals (released on August 19, 2011). In the latter, there is a two-year repayment deadline before offside loans from foreign affiliates are subject to the new tax penalties outlined in the foreign affiliate proposals.[32] I mentioned that, for "pre-Budget" loans, the clock on the

two-year period starts ticking on the date of the Budget. Obviously, the foreign affiliate rules were not in the Budget — they were in the August 19 release — so the two-year clock starts ticking on August 19, 2011.

Notes:

[1] See "New Tax Proposals: Summer Overload" and "Partnership Anti-Deferral Rules — The Clock Is Ticking", *Tax Notes* No. 585, October 2011.

[2] See Doc. No. 2011-0407961E5, September 27, 2011.

[3] *Legislative Proposals Relating to Income Tax and Sales and Excise Taxes*, October 31, 2011.

[4] A "personal services business," defined in subsection 125(7), means a business of providing services in which an individual (the "incorporated employee") (a) is a specified shareholder of the corporation, (b) provides services on behalf of the corporation to another person, and (c) would reasonably be regarded as an officer or employee of the person or partnership to whom or to which the services were provided, but for the existence of the corporation. An exception exists if the corporation employs more than five full-time employees.

[5] Applicable to taxation years commencing January 1, 2011. To the extent that days in the corporation's taxation year fall before this date, the corporation will lose the benefit of an 11.5% general rate reduction.

[6] That is, a degree of "double taxation" will arise when corporate-level earnings are distributed as dividends, as compared to the tax rate that would apply if such income was directly earned at the personal level.

[7] Under pre-existing rules, a personal services business is ineligible for the small business deduction, and the expenses it can deduct for tax purposes are severely restricted, in general, to the salary and wages that it pays to an incorporated employee.

[8] The efficacy thereof may be another matter.

[9] Originally released on August 16, 2011.

[10] Bill C-13, which received Royal Assent on December 15, 2011.

[11] "New Tax Proposals: Summer Overload", *supra*.

[12] Previously, a swap transaction did not include the transfer of a prohibited investment from an RRSP where the annuitant was entitled to a refund under subsection 207.04(4) on the transfer — this refers to the refund of the 50% tax on non-qualifying or prohibited investments. Now this exclusion is extended to the transfer of a non-qualified investment as well.

[13] The consequence of having the status of a transitional prohibited investment benefit was changed slightly, from a tax rate of 43.9% to having the benefit included in income.

[14] Or those of non-arm's length entities, e.g., a corporation controlled by a family member.

[15] The CRA has the ability to waive the tax in certain circumstances.

[16] The difference between a "small business corporation" and a "specified small business corporation" is that, rather than requiring CCPC status, per the "small business corporation" definition, the corporation must be a Canadian corporation that is not directly or indirectly controlled by one or more non-residents.

[17] E.g., to ensure that "small business corporation" status is maintained, e.g., the corporation doesn't have "offside" assets.

[18] See Doc. No. 2011-0429581E5; the document appears to supplement a question in the 2011 CRA Round Table at the Canadian Tax Foundation on the same date. A similar notice, "Joint ventures — Elimination of fiscal period", has appeared on the CRA's Web site.

[19] I.e., the relief in section 34.2.

[20] I.e., in a manner similar to the reserve mechanism provided for under section 34.2.

[21] The letter should indicate that the participant taxpayer is including income from the joint venture for which it is seeking transitional relief.

[22] One recent article indicates that taxpayers with joint venture interests should consider carefully whether such structures are still manageable in light of this new policy. But for pre-existing joint ventures, query how one copes with the rules; for example, converting the joint venture into a partnership may have a number of complexities.

[23] In addition, as stated previously, if a return has already been filed, a letter will be required to be sent to the CRA indicating that the taxpayer elects to be eligible for the transitional relief. However, no deadline is indicated for this letter.

[24] *Copthorne Holdings Limited v. Canada*, 2011 SCC 63; released December 16, 2011.

[25] Offshore parent (Big City) held Sub 1 (Copthorne I), which in turn held Sub 2 (VHHC II), a company whose PUC far exceeded its value. Rather than merge Sub 1 and Sub 2 in a vertical amalgamation and lose Sub 2's high PUC of some $67 million, Sub 1 transferred Sub 2 to Offshore Parent, followed by a horizontal amalgamation of Sub 1 and Sub 2, a transaction which preserved both companies' PUC. The CRA reassessed the offshore strip on the grounds that the tax benefit was the avoidance of the withholding tax on the offshore strip (i.e., due to the high PUC), and that the avoidance transaction was the share transfer by Sub 2 to Offshore Parent, which allowed a horizontal amalgamation of Sub 1 and Sub 2 and preserved Sub 2's $67 million of PUC. This was an abuse of paragraph 87(3)(*a*) governing PUC on amalgamations, which specifically excludes, from the computation of the PUC of the amalgamated corporation, the PUC of a share (i.e., Sub 2) held by any other predecessor corporation (i.e., Sub 1).

The transaction was aggressive in that it involved the double count of PUC. But it was also quite simple.

[26] In the sense that the earlier transaction was taken into account as a relevant consideration when the decision was made to undertake the later transaction.

[27] As to the degree of remoteness, the Court's remarks were limited; see para. 47, reproduced in footnote 11 of the following article.

[28] As the Supreme Court observed, that's the way the *Canada Trustco* (2005 SCC 54) case went (i.e., the case supports that subsection 248(10) may be applied both prospectively and retrospectively), and given this, the Court will not entertain lightly the reversing of a recent case (see para. 57).

[29] I.e., a spinout transaction of non-qualified assets to a transferee corporation may involve would-be deemed dividends (on the redemption of cross-shareholdings between the transferor and transferee corporations). If, however, this is part of a series of transaction involving the third-party sale of shares of the transferor corporation, deemed capital gains status will apply instead, under subsection 55(2).

In the past, the CRA has stated that it would be difficult for a taxpayer to maintain that it had no intention of ever selling the purified shares at the time of a purification reorganization and, as a consequence, the deemed dividends realized on the purification transaction and an eventual sale of the Opco shares would not be part of the same series of transactions. The CRA's reasoning for this position was set out in Doc. No. 5-7939, June 30, 1989, quoted below:

> It is in our view unlikely that such a situation would occur, however, since in most situations a shareholder who causes a reorganization to be carried out for the purpose of causing shares to qualify as QSBC shares does so in order that a deduction under subsection 110.6(2.1) of the Act will be available to him upon a disposition of the shares. In such cases the shareholder would have some intention at the time of the reorganization of eventually selling the shares.

Now, it appears open to use the *Copthorne* case to link (by contemplating backwards) the ultimate sale of the shares with the precedent spinout transaction.

[30] Several releases take comfort in the Court's statements, such as these: determining the rationale of the relevant provision in the Act should not be conflated with a value judgment of what is right or wrong, nor with theories about what tax law ought to be or ought to do (for example, in this case, the Supreme Court did not examine whether there was a general policy against surplus stripping in the Act); GAAR can only be applied to deny a tax benefit when the abusive nature of the transaction is clear; it is only when a reorganization is primarily for a tax purpose and is done in a manner found to circumvent a

provision of the *Income Tax Act* that it may be found to abuse that provision; it is the obligation of the Minister who wishes to overcome the countervailing obligations of consistency and predictability to demonstrate clearly the abuse he alleges.

[31] In that simple situation, the attribution rules provide that the husband gets the deduction. The Supreme Court held that the attribution rules had been "misused and abused" so that GAAR applied.

[32] Note that this differs from subsection 15(2), in that the latter limitation period is based on two years from the end of the taxation year of the lender in which the loan was made.

COPTHORNE — WHAT'S THAT SMELL?

— Michael Goldberg

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A lot has been written about the SCC decision in *Copthorne*[1] last month. It appears that most writers were not surprised about the result in *Copthorne* (the taxpayer lost again), were impressed with Justice Rothstein's written reasons on behalf of a unanimous Court (9-0), and ultimately were disappointed that the SCC appears to have added little to the jurisprudence — at least by way of guidance to taxpayers, their advisers, and the Minister on when GAAR should be applicable.

Yes, the SCC reaffirmed that the general GAAR guidelines set out in *Canada Trustco*[2] are to be followed by courts in making GAAR determinations.[3] Yes, the SCC reaffirmed that the GAAR is to be a provision of last resort.[4] Yes, the SCC reaffirmed that the principles in *Duke*[5] continue to permit taxpayers to engage in tax planning.[6] And yes, the SCC admonished lower courts against seeking "overriding policies" in the Act where none exist and against applying their olfactory senses when applying GAAR.[7]

On the other hand, the guidelines set out in *Canada Trustco* continue to leave lots of room for courts to make judgment calls in respect of what constitutes an "abuse". In this regard, the SCC reaffirmed its prior comments in *Lipson*[8] and continued to distance itself from its comments in *Canada Trustco*, in which it stated that "Parliament must . . . be taken to seek consistency, predictability and fairness in tax law", by finding here that by its very nature the GAAR creates "uncertainty" for taxpayers.[9] To this writer anyway, this seems to leave the question of when an abuse will exist in any situation open to considerable debate and, on a practical basis, leaves tax court judges to try and cover the smell with reasoning as sound as possible.

Before delving into what can be learned from the *Copthorne* decision, I'll provide a very brief reminder of what was at stake in the decision.

Copthorne in a Nutshell

In *Copthorne,* the taxpayer was undertaking a strategy to consolidate its corporate group through an amalgamation, so that a profitable corporation could use the capital losses of another corporation in the group. The taxpayer recognized that the amalgamation would wipe out a valuable tax pool, nearly $70 million of paid-up capital ("PUC") of a subsidiary corporation, if the amalgamation was done without planning (using a vertical amalgamation), but it recognized too that the tax pool could be preserved with a bit of planning (using a horizontal amalgamation). A few years later, the taxpayer's advisers found a use for the preserved PUC — they hoped to use it to strip an extra $70 million out of Canada without any taxes.

The removal of $70 million from the CRA's coffers tax-free is a lot of money, and the Minister was not amused. As a result, the Minister assessed the taxpayer, not only seeking to collect withholdings on a deemed dividend in respect of the removal of the $70 million from the taxpayer, but intending to apply penalties as well. GAAR served as the sole basis of the Minister's complaint at all levels of trial, and the Minister was successful (for differing reasons) at all levels of the courts — though the application of penalties against the taxpayer was vacated.

The taxpayer's counsel made many worthy arguments, not the least of which was this: why would a taxpayer plan its affairs in a way that would waste a valuable tax pool when, with a bit of planning, the pool could be preserved?

The SCC's response was that GAAR was properly applied in the circumstances of *Copthorne*. Using the *Canada Trustco* GAAR guidelines to analyze the provisions in the Act dealing with PUC preservation, and the particular text in the wording of subsection 87(3) (which apparently contains a code on PUC preservation transactions in its parenthetical comments), the Court found that the GAAR was properly applied to deny *Copthorne* the benefit of its otherwise properly preserved PUC.

Are All PUC Preservations Transactions Caught by GAAR?

Interestingly, it appears that not all transactions that might result in PUC preservation will be abusive. In fact, it was not the transactions involving the preservation of the PUC that the SCC found to be abusive; rather, it was the taxpayer's use of the PUC that gave offence. In particular, the SCC stated that:

> [126] It is true that the text of s. 87(3) recognizes two options, the horizontal and vertical forms of amalgamations. It is also true that the text does not expressly preclude a taxpayer from selecting one or the other option. However, I have concluded that the object, spirit and purpose of s. 87(3) is to preclude the preservation of PUC, upon amalgamation, where such preservation would allow a shareholder, on a redemption of shares by the amalgamated corporation, to be paid amounts without liability for tax in excess of the investment of tax-paid funds.

In this regard, the SCC noted that the benefit of PUC will not be lost by a purchaser of shares if there is no avoidance transaction, as will be the case in many arm's length sale situations.

Although the SCC did not expressly deal with this, it might have been instructive to consider what would have happened if, instead removing the PUC all at once,[10] the taxpayer had slowly removed the PUC from Canada over time. Would the transaction still have been abusive?

In this regard, the SCC's comments on when an avoidance transaction exists and, in particular, its comments on when a "series of transactions" will be found to exist will be of great interest to taxpayers and their advisers. To that end, the SCC confirmed that the concept of series is an extremely broad one — though it is not endlessly broad.[11]

Based on the SCC's comments in *Copthorne,* a strong argument could be made that the return of the preserved PUC would have attracted GAAR no matter how much time had passed between the transactions, though, as noted by the SCC, it may be possible to imagine other situations that would not attract GAAR, such as situations in which intervening events caused an end to the original series.[12]

Of Parenthetical Statutory Legislation

It appears that *Copthorne* has clarified that in-house PUC preservation transactions intended to allow non-arm's length parties to utilize the preserved PUC by side-stepping subsection 87(3) will likely be subject to GAAR.

Does this mean that all transactions that preserve a tax pool or reduce tax will be subject to GAAR? Does the outcome depend on a judicial search for a parenthetical remark buried in the Act — or does it depend on something else?

For example, will planning that defers tax through the use of a professional corporation attract GAAR? What about planning that doesn't just defer tax but saves it, for example, by shifting one's personal investment income to a CCPC? Does GAAR apply to purification planning that preserves capital gains exemption treatment?

Clearly each of these planning techniques will result in tax benefits and, based on the broad meaning of "series" adopted by the SCC, it would be difficult to argue that such planning does not constitute an avoidance transaction or transactions. As a result, in all cases, tax advisers will be left scratching their heads, fussing over the uncertain prospect of whether such planning is abusive. In paragraph 123, the SCC suggested that:

> This uncertainty underlines the obligation of the Minister who wishes to overcome the countervailing obligations of consistency and predictability to demonstrate clearly the abuse he alleges.

Not entirely helpful.

If one steps back and compares the transactions I've noted above to *Copthorne,* one might conclude that these and other types of "relatively benign" planning just shouldn't be abusive.[13] It is likely that a court would reach the same conclusion and that the CRA wouldn't bother trying to challenge such planning, so no one is likely to search the Act for parenthetical remarks supporting the existence of an abuse.[14]

Notwithstanding all of the excellent analysis by the SCC, one might also conclude that there was just too much money at stake in *Copthorne* to let the tax planning stand.[15] As such, tax advisers are advised that before implementing transactions they should breathe deeply — through their noses.

Notes:

[1] *Copthorne Holdings Ltd. v. R.*, 2011 SCC 63.

[2] *Canada Trustco Mortgage Co. v. Canada*, 2005 SCC 54.

[3] Paragraph 33 of the decision is reproduced below:

> In *Trustco* this Court set out the three questions to be decided in a GAAR analysis:
>
> (1) Was there a tax benefit? (para. 18);
>
> (2) Was the transaction giving rise to the tax benefit an avoidance transaction? (para. 21); and
>
> (3) Was the avoidance transaction giving rise to the tax benefit abusive? (para. 36).

Paragraph 57 is also instructive as to what it will require for the SCC to overturn a decision that is as recent as *Canada Trustco*.

[4] See paragraph 66.

[5] *Commissioners of Inland Revenue v. Duke of Westminster*, [1936] A.C. 1.

[6] See paragraph 65 (with the caveat that the planning is permitted so long as it is not abusive).

[7] See paragraph 118.

[8] *Lipson v. Canada*, 2009 SCC 1, [2009] 1 S.C.R. 3.

[9] See paragraph 123.

[10] Which appears to have taken place in response to certain legislative changes.

[11] See paragraphs [46] and [47], the latter of which is reproduced below.

> [47] Although the "because of" or "in relation to" test does not require a "strong nexus", it does require more than a "mere possibility" or a connection with "an extreme degree of remoteness" (see*MIL (Investments) S.A. v. R.*, 2006 TCC 460, [2006] 5 C.T.C. 2552, at para. 62, aff'd 2007 FCA 236, 2007 DTC 5437). Each case will be decided on its own facts. For example, the length of time between the series and the related transaction may be a relevant consideration in some cases; as would intervening events taking place between the series and the completion of the related transaction. In the end, it will be the "because of" or "in relation to" test that will determine, on a balance of probabilities, whether a related transaction was completed in contemplation of a series of transactions.

The Court also confirmed its view that the phrase "in contemplation of" as used in this definition is both a "prospective" and "retrospective" concept.

[12] As noted in paragraph 47, which was reproduced in the last footnote, such determinations are fact-driven, and little guidance was provided to assist a future court in making such a determination.

[13] A judgment call in and of itself.

[14] But what about other less conventional but not necessarily aggressive planning techniques, such as surplus stripping, ATR-66, and other loss utilization or anti-debt parking strategies?

[15] Similar admonitions against courts applying a smell test have been put forward since *Canada Trustco*, and yet it seems that the lower court decisions in *Copthorne* would have been decided on this basis rather than the more principled basis that was applied by the SCC (see paragraphs 26, 27, and 31).

BILL C-13 RECEIVES ROYAL ASSENT

On December 15, Bill C-13, *Keeping Canada's Economy and Jobs Growing Act*, received Royal Assent and is now law as S.C. 2011, c. 24. Bill C-13 implements the income tax resolutions from the 2011 federal Budget. This includes new and revised tax credits for individuals, measures to limit the deferral of tax using corporate partnerships, anti-avoidance rules for RRSPs, and measures concerning charities. It also includes amendments to the *Income Tax Act* concerning the Saskatchewan Pension Plan and amendments contained in Resolutions 15–17 of the 2010 federal Budget concerning the scholarship exemption and the education tax credit. CCH's *Income Tax Act* and Regulations will be updated as soon as possible on CCH online to incorporate these amendments.

EXTENSION OF TIME FOR PARTNERSHIP ELECTION

On December 16, 2011, the Department of Finance announced that it would extend the time to file an alignment election for corporate partnerships under the corporate partnerships deferral rules described in Bill C-13. A portion of this News Release, No. 2011-138, is reproduced below:

> The corporate partnership tax deferral rules allow corporate partners to elect to align the fiscal period of their partnership with the taxation year of one of the corporate partners or, in the case of a tiered-partnership structure, to a common fiscal period for all partnerships in the structure. The time period provided in the *Keeping Canada's Economy and Jobs Growing Act* for filing this election means that some corporate partners would have had to file the election as early as September 23, 2011.
>
> The Government intends to recommend a change that treats late alignment elections as having been filed on time if the election is filed on or before January 31, 2012.

PRESCRIBED INTEREST RATES — FIRST QUARTER OF 2012

The prescribed interest rates for the first quarter of 2012 were released by the Canada Revenue Agency on December 15, 2011. They are unchanged from the fourth quarter of 2011 and are noted below.

- 1% to calculate a deemed interest taxable benefit on subsidized employee and shareholder loans;
- 1% on refunds of income tax overpayments paid to corporate taxpayers;
- 3% on refunds of income tax overpayments paid to non-corporate taxpayers; and
- 5% on payments of overdue income taxes, insufficient income tax instalments, unremitted employee source deductions, CPP contributions or EI premiums, and unpaid penalties.

These rates will be in effect from January 1, 2012, to March 31, 2012.

2012 EMPLOYMENT INSURANCE PREMIUMS

The CRA has released the figures for the 2012 Employment Insurance premiums (see T4127-JAN — 95th Edition (Draft)). The 2012 maximum insurable earnings is $45,900 (up from $44,200 in 2011). The premium rate is 1.83% (up from 1.78% in 2011) for a maximum annual premium of $839.97. The employer rate is 1.4 times the employee rate. The 2012 premium rate for Quebec is 1.47% (up from 1.41% in 2011), for a maximum annual premium of $674.73. See *Tax Topics* No. 2070, dated November 10, 2011, for the Canada Pension Plan maximum pensionable earnings for 2012 that were released by the CRA on November 1, 2011.

TAX NOTES

Published monthly by CCH Canadian Limited. For subscription information, contact your CCH Account Manager or call 1-800-268-4522 or (416) 224-2248 (Toronto).

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Notice: *Readers are urged to consult their professional advisors prior to acting on the basis of material in this newsletter.*

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PUBLICATIONS MAIL AGREEMENT NO. 40064546
RETURN UNDELIVERABLE CANADIAN ADDRESSES TO CIRCULATION DEPT.
330–123 MAIN ST
TORONTO ON M5W 1A1
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