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The Joint Committee on Taxation of  
The Canadian Bar Association  
and

Chartered Professional Accountants of Canada

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October 13, 2023

Trevor McGowan  
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Dear Trevor:

**Subject: GAAR Proposals and Self-Help Transactions**

Thank you for the opportunity to provide additional input regarding the proposed amendments to section 245 of the *Income Tax Act* (ITA). Our comments in this letter relate to certain transactions or series of transactions that are commonly implemented to avoid particular tax implications, which may be considered, in some situations, to lack economic substance, but should not be considered to result in a misuse or abuse under the General Anti-Avoidance Rule (GAAR), as proposed to be amended.

We are concerned that the introduction of the preamble in subsection 245(0.1) and the presumption of misuse or abuse where transactions significantly lack economic substance in subsections 245(4.1) and (4.2), will blur the line between acceptable transactions versus abusive transactions. First, the proposed preamble states that GAAR should not prevent taxpayers from obtaining tax benefits “contemplated by Parliament”. However, many tax planning transactions result in, or from, the application of various provisions and regimes in order to accomplish a particular outcome that is not specifically documented in the ITA, nor originally contemplated by Parliament, but are nevertheless considered appropriate by both Finance and the Canada Revenue Agency (CRA). Second, many of these strategies include one or more of the factors listed in subsection 245(4.2).

The Explanatory Notes relating to paragraph 245(0.1)(a) currently provide a very narrow view of tax advantages which are intended by Parliament, by referencing RRSP contributions and accelerated CCA claims. These examples do not reflect the reality that many tax planning strategies utilize various

provisions of the ITA to implement a series of transactions which navigates around otherwise inappropriate tax consequences. The tax advantages resulting from such transactions may not have been specifically intended or contemplated by Parliament, but nevertheless should not be prohibited by GAAR.

While the Explanatory Notes indicate the presumption in subsection 245(4.1) is rebuttable, it should be made clear that certain transactions which may include one or more of the factors listed in subsection 245(4.2) will not be considered to result in a misuse or abuse where they are undertaken to achieve a result which would not be considered to defeat or frustrate the provisions of the ITA. Further, the Explanatory Notes should clarify that there may be tax benefits achieved through transactions undertaken by taxpayers which benefits were not specifically contemplated by Parliament, but which may not be considered to result in a misuse or abuse. It would be helpful if the Explanatory Notes included examples of acceptable transactions. The following list (although not exhaustive) sets out examples of transactions which should be identified as acceptable tax planning strategies:

- 1) The transactions identified in IC88-2 "General Anti-Avoidance Rule - Section 245 of the Income Tax Act" and IC88-2 Supplement 1 "General Anti-Avoidance Rule" (published October 21, 1988 and July 13, 1990 respectively). For completeness, those transactions are listed in Appendix A.
- 2) Post-mortem pipeline transactions. In this regard, it would be helpful to have an explanation of the analytical process that differentiates these transactions from other transactions with similar characteristics that Finance may feel should be caught by the new rules.
- 3) Distributions to non-resident shareholders of a Canadian-resident private corporation by way of PUC returns, including in circumstances where the corporation has retained earnings.
- 4) The use of a Bidco to step-up PUC to fair market value in connection with the acquisition of a Canadian corporation, whether by a domestic or foreign purchaser.
- 5) Acquiring 10.1% of the relevant shares of a corporation so that Part IV tax does not apply under the "bright-line" test in that provision.
- 6) The use of cash damming and other tracing techniques in circumstances where funds-tracing is relevant.
- 7) Debt-slide transactions, similar to those described in ATR-66, "Non-Arm's Length Transfer of Debt Followed by a Winding-Up and a Sale of Shares," April 20, 1995.

We believe that a collection of identified transactions of the nature described above will help formulate a better understanding of the application of the proposed GAAR amendments, particularly the application of the new economic substance test. The Explanatory Notes should also include guiding principles to further assist taxpayers in determining when certain tax-motivated transactions may be acceptable, in order to provide taxpayers with more certainty when planning their affairs.

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Members of the Joint Committee participated in the discussion and preparation of this submission, including:

- Ian Crosbie – Davis Ward Phillips & Vineberg LLP
- Angelo Nikolakakis – EY Law LLP
- Anu Nijhawan – Bennett Jones LLP
- John Oakey – CPA Canada

We would be pleased to discuss this letter with you in further detail at your convenience.

Yours truly,

*Carmela Pallotto*

Carmela Pallotto  
Chair, Taxation Committee  
Chartered Professional Accountants of Canada



Carrie Smit  
Chair, Taxation Section  
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Cc: Robert Demeter, Director General of Tax Legislation Division, Tax Policy Branch, Finance

**Appendix A**  
**IC88-2 and Supplement 1**

- a) Divisive reorganizations (butterflies under paragraph 55(3)(b));
- b) Consolidation of profits and losses in a related/affiliated corporate group
- c) Estate freezes;
- d) Incorporation of a sole proprietorship;
- e) Rollover of non depreciable capital property to an arms length corporation for redeemable preferred shares which are then redeemed and subsection 55(2) applies;
- f) Purification of a corporation to meet qualified small business corporation (QSBC) requirements;
- g) Deferral of payment to a non-arms length individual for services where section 78 of the ITA applies;
- h) Corporation does not pay salary to a non-arms length individual for services provided;
- i) Corporation pays a reasonable salary to a non-arms length individual to reduce its income to the business limit;
- j) Profitable parent company borrows money and subscribes for common shares of non-profitable subsidiary resulting in deductible interest to the parent instead of increased non-capital losses to subsidiary;
- k) Canadian corporation uses a newly incorporated company (Bidco) to finance the acquisition of a target company followed by an amalgamation to offset interest with operating income;
- l) Amalgamation of a corporation and a shell corporation, where the minority shareholders get redeemable preferred shares which are then redeemed for cash;
- m) Crystallizing a taxpayer's capital gains exemption by selling qualifying shares to a non-arm's length company and electing an amount triggering sufficient capital gains to utilize exemption;
- n) One shareholder sets up a new company to buy shares of target held by the other arm's length shareholder followed by a merger of the two companies;
- o) Loss consolidation transactions where Profitco buys shares of Lossco and Lossco lends the funds received back to Profitco.
- p) US company owns shares of a Canadian company with an accrued gain from Canadian real property (shares constitute taxable Canadian property). The Canadian company pays a dividend (subject to withholding tax) equal to its retained earnings reducing its fair market value, followed by a sale of Canadian company shares to an unrelated purchaser for reduced price:
- q) Targetco rolls a business to a new subsidiary before an arm's length acquisition of Targetco allowing the buyer to wind-up or amalgamate with targetco, bump-up the tax cost of the subsidiary shares prior to an arm's length sale of the subsidiary shares;
- r) Shift of paid-up capital to preferred shares created on an amalgamation to give capital gains to preferred shareholder on redemption.