Are You Ready for the Upstream Loan Rules?

Ken J. Buttenham***

For many years, “upstream loans” have been a popular repatriation technique used by Canadian taxpayers to defer foreign withholding taxes and expedite corporate distributions. However, recently enacted amendments to the Income Tax Act have introduced new restrictions on the use of upstream loans as a repatriation technique, specifically in respect of loans from or indebtedness owing to a foreign affiliate from a related entity other than another foreign affiliate that is controlled by the Canadian taxpayer. The new rules represent a significant change in policy that will affect both Canadian multinational corporations and foreign multinationals with Canadian subsidiaries and foreign affiliates.

This article provides an overview of the new upstream loan provisions and a framework for determining when they will apply. It also highlights some of the uncertainties inherent in the legislation and offers suggestions for adapting to, and managing the consequences of, the new rules.

**KEYWORDS:** LOANS ■ FOREIGN AFFILIATES ■ SERIES ■ REPATRIATION ■ MULTINATIONALS ■ SURPLUS

** CONTENTS **

Introduction 748
Overview of the New Rules 749
   Income Inclusion—Subsection 90(6) 749
   Exceptions—Subsection 90(8) 750
   Deductions—Subsection 90(9) 750
   Downstream Surplus—Subsection 90(11) 751
   Repayment of Loan—Subsection 90(14) 751
   Back-to-Back Loans—Subsection 90(7) 752
   Applicable Dates 752

---

* Of PricewaterhouseCoopers LLP, Montreal.

** Of PricewaterhouseCoopers LLP, Toronto.

*** Of PricewaterhouseCoopers LLP, Toronto. The author would like to thank Eric Lockwood and Karina Yiu, both of PricewaterhouseCoopers LLP, Toronto, for their excellent assistance in the preparation of this article. Any errors that remain are my own.
INTRODUCTION

On August 19, 2011, the Department of Finance released long-awaited proposals relating to the taxation of Canadian multinational corporations with foreign affiliates.1 As well as setting out many expected revisions to the foreign affiliate rules, the proposals included new provisions governing arrangements referred to as “upstream loans.”2 The upstream loan rules have since been enacted with the passage of Bill C-48.3

The upstream loan rules can result in income to a Canadian-resident taxpayer when a certain person or partnership (a “specified debtor,” discussed below) receives a loan from or becomes indebted to a foreign affiliate of the taxpayer.

The explanatory notes to the 2011 proposals describe this new rule as being necessary to protect the integrity of both the taxable surplus regime and the new hybrid surplus regime.4 The introduction of the upstream loan rules represents a significant change in policy.5 Previously, taxpayers and advisers relied on pronouncements from

---

1 Canada, Department of Finance, Legislative Proposals in Respect of Foreign Affiliates (Ottawa: Department of Finance, August 2011) (herein referred to as “the 2011 proposals”) and accompanying Explanatory Notes—Foreign Affiliate Amendments (Ottawa: Department of Finance, August 2011) (herein referred to as “the 2011 explanatory notes”).

2 In this article, the term “upstream loan” generally refers to both a loan from or indebtedness owing to a foreign affiliate of a Canadian-resident taxpayer where such loan or indebtedness is made to or owed by a “specified debtor.”


4 2011 explanatory notes, supra note 1, at 1.

5 Although these rules represent a significant change in policy as it relates to the use of upstream loans, one could argue that the introduction of the new provisions is consistent with a broader policy trend over the last number of years toward ensuring that profits earned either in Canada or by a foreign affiliate are repatriated back through Canada and not redeployed using Canada’s
the Canada Revenue Agency (CRA) confirming that certain lending arrangements between foreign affiliates and Canadian residents would not attract unwanted tax consequences. As a result, Canadian corporations routinely repatriated earnings from foreign affiliates using upstream loans to defer taxes and minimize administrative costs. The new rules are relevant not only to Canadian multinational corporations but also to any multinational group that includes a Canadian corporation that owns shares of a foreign affiliate.

With the enactment of the upstream loan provisions, companies are focused on assessing the effect on their current structures and the need to unwind certain loans by the relevant dates. Therefore, this article focuses on certain interpretive and practical issues that taxpayers may encounter when evaluating the risks associated with their current treasury arrangements.

OVERVIEW OF THE NEW RULES
The essential features of the new rules are described below. (A more detailed analysis of the rules is beyond the scope of this article.)

INCOME INCLUSION—SUBSECTION 90(6)
Subsection 90(6) of the Income Tax Act requires a Canadian-resident taxpayer to include in income a “specified amount” in respect of an upstream loan made by a foreign affiliate of the taxpayer to a “specified debtor.” Both terms are defined in subsection 90(15).

“Specified debtor” identifies the borrower that would be subject to the upstream loan rules. A specified debtor includes the taxpayer, a person with which the taxpayer does not deal at arm’s length (other than a controlled foreign affiliate as defined in section 17), and a partnership the members of which include the taxpayer or such non-arm’s-length person.

If the specified debtor is a foreign affiliate, the “specified amount” (the amount to be included in income under subsection 90(6)) is determined by multiplying the amount of the upstream loan by the excess of the taxpayer’s surplus entitlement...
percentage\(^{10}\) (SEP) in the creditor affiliate (the lender) over its SEP in the specified debtor. Otherwise, the specified amount is the amount of the upstream loan multiplied by the taxpayer’s SEP in the creditor affiliate.

**Exceptions—Subsection 90(8)**

By virtue of subsection 90(8), there is no income inclusion under subsection 90(6) if the upstream loan is repaid within two years of the day on which the loan was made (other than as part of a series of loans or other transactions and repayments) or if the loan arose in the ordinary course of business of the creditor and bona fide arrangements were made for repayment within a reasonable time.\(^{11}\) These two exceptions are similar to those in the shareholder loan rules in subsection 15(2).

**Deductions—Subsection 90(9)**

To provide relief from the upstream loan rules, subsection 90(9) allows a deduction equal to the total of certain deductions that could have been claimed had the specified amount in respect of an upstream loan been instead distributed as a dividend (or a series of dividends) to the taxpayer. Conceptually, this provision allows a taxpayer to continue to repatriate funds via an upstream loan without Canadian tax implications if, solely because of foreign tax or legal considerations, a loan is made instead of payment of an actual dividend.

Any deduction taken under subsection 90(9) must be included in income in the following taxation year under subsection 90(12), but the income inclusion could be offset by a new deduction under subsection 90(9) if all the conditions continue to be met. A deduction under subsection 90(9) is available in respect of a specified amount that is included in income under subsection 90(6) or (12) if all of the following conditions are met:

- **Paragraph 90(9)(a).** If, at the time the loan is made, the taxpayer can demonstrate that if the specified amount had instead been received by the taxpayer as a dividend (a “notional dividend distribution”), the taxpayer would be entitled to deductions under subsection 113(1) or 91(5) in respect of exempt surplus,\(^{12}\) hybrid surplus where there is sufficient underlying foreign tax (UFT),\(^{13}\) taxable surplus where there is UFT,\(^{14}\) preacquisition surplus to the

---

\(^{10}\) See the definition of “surplus entitlement percentage” in regulation 5905(13).

\(^{11}\) See paragraphs 90(8)(a) and (b), respectively. There is a third exception, in paragraph 90(8)(c), that may apply to upstream loans made in the ordinary course of carrying on a life insurance business outside Canada; however, that exception is not addressed in this article.

\(^{12}\) Clause 90(9)(a)(i)(A) refers to the deduction available under paragraph 113(1)(a).

\(^{13}\) Clause 90(9)(a)(i)(B) refers to the deduction available under paragraph 113(1)(a.1) to the extent that the entire hybrid surplus is fully covered by the grossed-up balance of hybrid underlying taxes.

\(^{14}\) Clause 90(9)(a)(i)(C) refers to the deduction available under paragraph 113(1)(b) to the extent of the grossed-up UFT balance.
extent of the adjusted cost base (ACB), and amounts previously taxed as foreign accrual property income (FAPI).

- **Paragraph 90(9)(b).** The same amount of surplus or ACB may not be used during the period in which the loan is outstanding to support a claim for a subsection 90(9) deduction in relation to any other upstream loan, or any deduction under subsection 91(5) or 113(1) in respect of an actual dividend. This condition prevents double-counting of the surplus and/or ACB.

- **Paragraph 90(9)(c).** The same amount of ACB cannot be used to determine the taxability of any other distribution, again to prevent double-counting—in this instance, in respect of other distributions, such as a qualifying return of capital under subsection 90(3).

No deduction is available under subsection 90(9) in respect of the portion of a notional dividend distribution that would be deductible under paragraph 113(1)(d) if the specified debtor is a non-arm’s-length non-resident.

**Downstream Surplus—Subsection 90(11)**

Similar to the situation for an election under subsection 93(1), in determining the amount of surplus available to a taxpayer as a deduction under subsection 90(9), surplus balances downstream of the creditor foreign affiliate are taken into account on the basis of the operation of regulation 5902(1)(a). Under regulation 5902(1)(a), the amount of surplus is equal to the surplus that would be included had dividends been paid starting from the lowest-tier affiliate up to the creditor foreign affiliate. Therefore, in computing this amount, deficits of any foreign affiliate above the lowest-tier affiliate may reduce or eliminate the amount of surplus available.

**Repayment of Loan—Subsection 90(14)**

A deduction is available in the year in which the loan is repaid (other than as part of a series of loans or other transactions and repayments) to the extent of the amount that was included in income under subsection 90(6). This is similar to the deduction available under paragraph 20(1)(j) for a repayment of a shareholder loan. In the year of repayment, by virtue of subsection 90(13), the deduction under subsection 90(9) is not available to prevent a double deduction.

---

15 Clause 90(9)(a)(i)(D) refers to the deduction available under paragraph 113(1)(d) to the extent of the ACB in the shares of the top-tier foreign affiliate in the chain.

16 Subparagraph 90(9)(a)(ii) refers to the deduction available under subsection 91(5). This deduction is available only if the specified debtor is a non-arm’s-length non-resident.

17 While any double-counting of surplus or ACB results in a loss of the ability to claim a subsection 90(9) deduction, it appears that this condition can be satisfied if surplus is moved up the foreign affiliate chain but is not used to support another subsection 90(9) deduction, and no dividends are paid to the Canadian taxpayer such that any deductions are claimed under subsection 91(5) or 113(1).
**Back-to-Back Loans—Subsection 90(7)**

Pursuant to subsection 90(7), certain back-to-back loans are collapsed into one loan for the purposes of the application of the upstream loan rules, to the extent of the lesser of the amount of the loans. This provision is modelled on subsection 17(11.2).

**Applicable Dates**

The upstream loan rules generally apply to loans or indebtedness incurred after August 19, 2011. Loans or indebtedness incurred on or before August 19, 2011 are grandfathered, whereby any amount that remains outstanding on August 19, 2014 is deemed to be a separate loan or indebtedness issued on August 20, 2014. Therefore, upstream loans in existence on or before August 19, 2011 are entitled to a minimum five-year grace period instead of the regular two-year repayment period provided by subsection 90(8).

**Working with the Upstream Loan Rules**

As mentioned above, the focus of this article is on certain of the interpretive and practical considerations that may be encountered by taxpayers attempting to operate within the upstream loan rules. To help taxpayers approach the application of these rules to their own situations, a four-step general framework is presented and a flow chart is included as an appendix.

**Step 1: Identify All Loans to and Indebtedness from a “Specified Debtor”**

The upstream loan rules apply each time a specified debtor receives a loan from, or becomes indebted to, a creditor that is a foreign affiliate of a taxpayer resident in Canada. Because these rules apply loan by loan, or indebtedness by indebtedness, the first step is to identify all upstream loans.

This may be a straightforward exercise if a Canadian multinational corporation owns relatively few creditor foreign affiliates. In such cases, all upstream loans will be centralized in the Canadian multinational group, and the Canadian multinational corporation should have ready access to the necessary information regarding all relevant amounts. However, in certain structures this initial step may be more of a challenge. Consider a large foreign multinational corporation with many global subsidiaries, including a group of Canadian companies that in turn own a large group of foreign affiliates. In this instance, the quantity of potential upstream loans can be multiplied significantly, and the Canadian taxpayer may not have ready access to the necessary information to fully assess the application of the upstream loan rules.

When identifying upstream loans, it is important not to overlook day-to-day intercompany transactions, such as trade receivables. If the parties transact on an

---

18 Subsection 90(6). Assuming that subsections 15(2) and 90(8) do not apply.
arm’s-length basis, it is expected that the ordinary course of business exception would be met for trade receivables or, at the very least, that these amounts would be repaid within two years of the date of the original loan and would therefore meet the repayment exception in subsection 90(8). However, if intercompany accounts are not settled on a fairly regular basis, trade or other intercompany receivables could be subject to the upstream loan rules.

In determining whether a specific amount has been repaid within two years (other than as part of a series of loans or other transactions and repayments), the CRA has indicated that it is willing to accept, in certain circumstances, a first-in, first-out (FIFO) approach to track the origination and settlement of multiple debts that may arise from intercompany transactions.19 This position will be helpful in situations where lump-sum repayments against upstream loans are made on a fairly regular basis; however, companies will have to ensure that the necessary tracking processes and policies are put in place to settle intercompany accounts regularly.

In some cases, specific intercompany amounts may not be settled on a regular basis because receivables from and payables to foreign affiliates are managed on a net basis. For financial statement reporting purposes, receivables from and payables to a particular specified debtor may be offset—effectively treating payables to a particular specified debtor as a repayment of all or a portion of the receivable from that specified debtor. However, for the purposes of identifying upstream loans, receivables from specified debtors should not be automatically netted against payables to the same specified debtors without ensuring the legal right to offset.20

---

19 See CRA document no. 2013-0483751C6, May 23, 2013. In comments made during the CRA round table presentation at the 2013 International Tax Seminar of the International Fiscal Association (IFA) (Canadian branch), held in Montreal on May 23, 2013, the CRA confirmed that it would accept this FIFO approach with respect to receivables that have identical terms. In situations where there are substantial differences in the terms of the receivables, the CRA believes that it would be necessary for the debtor to specify which specific receivable balance was being paid. The CRA’s comments were made in the context of the foreign affiliate dumping rules in section 212.3; however, there is no reason to believe that those comments would not have equal application in the context of the upstream loan rules. Further support for this approach can be found in the examples in Interpretation Bulletin IT-119R4, “Debts of Shareholders and Certain Persons Connected with Shareholders,” August 7, 1998. The examples in IT-119R4 clearly illustrate that repayments can be considered to apply first to the oldest loans outstanding (citing the FIFO basis) unless the facts clearly indicate otherwise.

20 See CRA document no. 2003-0033915, February 17, 2004, which sets out the CRA’s view for the purposes of subsection 15(2), that debts between a shareholder and a particular person do not generally offset in determining whether a shareholder has “become indebted to” or “received a loan from” a particular person in the first instance or whether that indebtedness or loan was repaid. Also see, for example, Johnston’s Estate v. MNR, 64 DTC 204 (TAB), which supports the position that for a debt or loan to have been repaid for the purposes of subsection 15(2), there must have been a repayment of the loan or indebtedness in the form of money or money’s worth. For the reasons discussed later in this article, the CRA’s view on these matters in relation to the upstream loan rules is expected to be consistent with its views on subsection 15(2).
Taxpayers must be aware of these situations. They may want to take the necessary steps to legally offset receivables and payables, so as to eliminate or reduce amounts subject to the upstream loan rules to the extent possible.

Cash Pooling

Cash pool arrangements create numerous interpretive issues related to the upstream loan rules. They are used by multinational companies to efficiently manage global cash resources and foreign exchange risks. Applying the upstream loan rules to a cash pool arrangement requires an understanding of the following:

- the type of cash pool mechanism employed and the legal relationships created;
- the members of the cash pool (for example, whether they include the Canadian taxpayer, other non-arm’s-length Canadian companies, foreign affiliates, and/or any other non-arm’s-length non-resident entities that are not foreign affiliates); and
- the specific participation of each member in the cash pool (for example, each member’s debit or credit position at various points in time).

This analysis becomes more difficult where the members of the cash pool may change over time and where any one member’s participation in the cash pool arrangement may change often—perhaps even daily. If no specified debtors are members of the cash pool or the foreign affiliate members of a cash pool are all consistently net borrowers from the cash pool, one would expect that there should be no upstream loans. Otherwise, upstream loans could exist, depending on the legal relationships created by the cash pool agreement.

There are numerous types of cash pool arrangements. At one end of the spectrum is a “notional” cash pool. In a notional cash pool, the members of the pool maintain separate bank accounts with a financial institution. However, the calculation of interest received or paid is usually based on the consolidated balance of all members, including both positive and overdraft positions. The interest is then allocated to the separate bank accounts according to a formula.

If the terms of a specific notional cash pool do not create loans or indebtedness between the members of the cash pool because the pooling is only from the perspective of the financial institution with respect to the calculation of interest, a foreign affiliate that is a member of the notional pool and that has a positive cash balance should not be considered to have made an upstream loan where one or more specified debtors are also members of the cash pool. Further, depending on the relevant facts, including in part the business reasons for the foreign affiliate’s participation in the notional pool, it may be difficult for the CRA to apply the general anti-avoidance rule to such arrangements on the basis of a back-to-back recharacterization of the actual legal relationships.

21 Section 245.
At the other end of the spectrum, “zero balance” or “cash concentration” cash pool arrangements usually require the physical transfer of funds to or from each member of the pool to the account of a member that is designated as the “pool head” or “concentrator.” It is generally recognized that these types of arrangements create intercompany payables and receivables between each pool member and the pool head.\textsuperscript{22} If the pool head is a specified debtor, a foreign affiliate’s positive balance in such a pool likely would constitute an upstream loan.

The generic types of cash pooling briefly touched on above are only two of numerous possibilities. Many taxpayers will have arrangements somewhat different from the examples above, because each arrangement is designed to address taxpayers’ specific structures, currency risks, and liquidity requirements. In practice, it may be challenging for taxpayers and the CRA to determine the correct application of the upstream loan rules when cash-positive foreign affiliates are members of a cash pool that also includes specified debtors.\textsuperscript{23} Owing to the nature of cash pool arrangements, not only is it difficult to determine whether an upstream loan exists, but it can also be difficult to track repayments (and maintain that they are not part of a series of loans or other transactions and repayments), as well as to determine when a “new” upstream loan is made.\textsuperscript{24}

It seems unreasonable that foreign affiliates with working capital funds on deposit in a cash pool should be subject to these rules. Nevertheless, no general carve-out is available for these cases. It is hoped that the CRA will agree that the two-year repayment exception should generally apply in the case of a foreign affiliate with a continuous positive balance in a cash pool where the balances represent funds required for working capital.\textsuperscript{25}

\textbf{Identifying the Relevant Creditor Affiliate}

In most cases, it will be relatively straightforward to identify the relevant creditor foreign affiliate associated with a specific upstream loan; however, care should be taken when back-to-back loans exist. Subsection 90(7) applies to collapse back-to-back loans and deem an upstream loan made by an “intermediate lender” to the “intended borrower” to have been made by the “initial lender” to the intended

\textsuperscript{22} See Arthur Andersen Inc. v. Toronto-Dominion Bank (1994), 17 OR (3d) 363 (CA), which held that end-of-day transfers of amounts between related corporations in a mirror concentration arrangement were legally effective as between the corporations.

\textsuperscript{23} There may not be any ultimate income inclusion under these rules if one of the exceptions in subsection 90(8) applies or if a full deduction can be claimed under subsection 90(9); however, where an upstream loan exists, the potential application of these relieving provisions will have to be considered.

\textsuperscript{24} It also may be difficult to assess whether an upstream loan resulting from the participation in a cash pool can be grandfathered.

\textsuperscript{25} Although the balance would be consistently positive, this positive balance could arguably be viewed as the cumulative result of many deposits and withdrawals over any given period. This position is supported by the FIFO approach discussed above (supra note 19 and the related text).
borrower.\textsuperscript{26} For subsection 90(7) to apply, there must be a causal link between the back-to-back loans (that is, the loan from the intermediate lender to the intended borrower must have been made \textit{because} the intermediate lender received a loan from the initial lender). Identifying the correct creditor affiliate is important because the availability of certain exceptions and deductions under the upstream loan rules is based on the actions and attributes of the creditor affiliate.

\textbf{Step 2: Determine When the Upstream Loan Rules Apply}

Once all upstream loans have been identified, it is necessary to determine how the coming-into-force rules may apply to each specific loan. The upstream loan rules apply to loans received and indebtedness incurred after August 19, 2011 and to any portion of a particular loan received or a particular indebtedness incurred on or before August 19, 2011 (a “grandfathered loan”) that remains outstanding on August 19, 2014. Furthermore, a grandfathered loan is treated as if it were a separate loan or indebtedness that was received or incurred on August 20, 2014 (in the same manner and on the same terms as the grandfathered loan) for the purposes of the upstream loan rules.\textsuperscript{27}

While grandfathered loans receive a much more generous grace period than an upstream loan arising after August 19, 2011, grandfathering applies only if the original loan remains outstanding (that is, it is not replaced by a “new” loan). In this context, no “series of loans or other transactions and repayments” language can be relied on (in the taxpayer’s favour) to ensure that a repayment of a grandfathered loan followed by the making of a new upstream loan (as part of a series) is ignored. If transactions undertaken after August 19, 2011 give rise to a new loan (or new indebtedness) under common-law principles, the upstream loan rules will apply to the new upstream loan and grandfathering will be lost.\textsuperscript{28} Therefore, care should be taken to identify any grandfathered loans and to ensure that they are not inadvertently replaced by new upstream loans.\textsuperscript{29}

\textsuperscript{26} The terms “intermediate lender,” “intended borrower,” and “initial lender” are defined in subsection 90(7). The amount of such deemed loan is the lesser of (1) the amount of the loan made by the initial lender to the intermediate lender, and (2) the amount of the loan made by the intermediate lender to the intended borrower. If the taxpayer so elects, the back-to-back loan provisions in subsection 90(7) do not apply in respect of all loans received and indebtedness incurred on or before October 24, 2012.

\textsuperscript{27} This addition to the coming-into-force rules for grandfathered loans is a welcome change from the original upstream loan proposals, which deemed an upstream loan existing on August 19, 2011 to have been advanced on that day, thereby effectively providing the same two-year grace period as is provided for all loans made after August 19, 2011.

\textsuperscript{28} Although the upstream loan rules will not apply to the grandfathered loan that ceases to exist (assuming that the “new” upstream loan is created prior to August 19, 2014).

\textsuperscript{29} Changes to the terms of an existing loan or indebtedness may result in the termination of that loan or indebtedness and the creation of a new loan or indebtedness. In \textit{General Electric Capital}
The ability to claim a reserve against an income inclusion pursuant to the upstream loan rules depends on, among other things, the amount of exempt surplus available in the foreign affiliate chain that includes the foreign affiliate that has the upstream loan. This is discussed below. In the case of a grandfathered loan that is deemed to arise on August 20, 2014 for the purposes of the upstream loan rules, a taxpayer has the benefit of three additional years of earnings available to support a reserve against any income inclusion.\textsuperscript{30}

**Step 3: Decide Whether the Upstream Loan Is To Be Repaid Within Two Years**

As noted above, one of the exceptions to the application of the upstream loan rules is for an upstream loan that is repaid within two years of the day it was made, other than as part of a series of loans or other transactions and repayments (“a series”).\textsuperscript{31} If a taxpayer plans to rely on this exception, it will be critical to ensure that any repayment is not considered to be part of a series so that the repayment will be respected for the purposes of the upstream loan rules.\textsuperscript{32}

In this regard, the upstream loan rules have clearly and deliberately been modelled on the provisions in subsection 15(2.6) and paragraph 20(1)(j) in respect of the shareholder loan rule in subsection 15(2). The revised explanatory notes issued in October 2012 specifically state that the upstream loan rules are modelled on

\textit{Finance Inc. v. Canada}, 2001 FCA 392, the Federal Court of Appeal considered whether for the purposes of the application of former subparagraph 212(1)(b)(vii), a new debt obligation was created by reason of the modifications made to the debt. The court looked to what it considered to be the fundamental terms of a debt obligation, namely, (1) the identity of the debtor, (2) the principal amount, (3) the amount of interest payable, and (4) the maturity date. On the facts in \textit{General Electric}, three of the four fundamental terms had been changed: the maturity date, the principal amount, and the interest rate. The court found that these changes were substantial changes made to the fundamental terms of the debt obligation that materially altered the terms of that obligation, and that as a result a new debt obligation had been created. The court did not, however, provide clear guidelines as to the extent of the changes required to find that a new debt obligation has been created. In \textit{Interpretation Bulletin IT-448, “Dispositions—Changes in Terms of Securities,” June 6, 1980, at paragraph 7, the CRA provided a list of changes to debt obligations that (unless carried out pursuant to an authorizing provision in the original terms of the debt obligation) it considers “to be so fundamental to the holder’s economic interest in the property that they almost invariably precipitate a disposition.” For a discussion of the Federal Court of Appeal decision in \textit{General Electric}, see Monica Biringer, “When Is an Obligation New?” (2001) 9:4 Corporate Finance 906-10.

\textsuperscript{30} Of course, the foreign affiliate could also sustain losses in the intervening period unless planning is undertaken to mitigate.

\textsuperscript{31} Paragraph 90(8)(a).

\textsuperscript{32} It is also important to ensure that a repayment is not part of a series in order to claim a deduction under subsection 90(14) where the repayment occurs more than two years after the day on which the upstream loan arose.
subsection 15(2) in the domestic context (modified as required). Therefore, it seems appropriate to refer to the relevant jurisprudence and the CRA commentary relating to subsection 15(2.6) (and its predecessor in former paragraph 15(2)(b)) to determine the meaning of the term “series of loans or other transactions and repayments” as used in subsections 90(8) and (14).

Meaning of “Series”

The courts have interpreted “series,” on the basis of accepted dictionary definitions, to mean succession, sequence, or continued course (of action or conduct, of time, life, etc.). The determination of whether or not a series existed in the context of the shareholder loan rules was considered in Meeuse v. The Queen. This case involved a taxpayer who had borrowed various sums from her husband’s company. Each of the loans had been entered into for a separate and distinct purpose. The CRA assessed the taxpayer on the basis that the loan entered into to finance the construction of a storage building should be included in her income pursuant to subsection 15(2) and the subsequent repayment of that loan should be ignored. Bowman J held that the amount fell within the exception set out in paragraph 15(2)(b) (as it then read) for loans repaid within one year and did not form part of a “series of loans or other transactions and repayments.” In the course of his analysis of whether or not the various loans that had been entered into by the taxpayer formed

33 Canada, Department of Finance, Explanatory Notes Relating to the Income Tax Act, the Excise Tax Act and Related Legislation (Ottawa: Department of Finance, October 2012) (herein referred to as “the October 2012 explanatory notes”), at 152.
34 This approach has judicial support. In Canada Trustco Mortgage Co. v. MNR, 91 DTC 1312 (TCC), the court, in interpreting the words “active business” in section 95, applied jurisprudence that had developed concerning the meaning of this term in the context of section 125, thereby employing the established principle of interpretation that words should be given the same interpretation or meaning wherever they appear in a statute. (Also see Thomson v. Canada (1992), 89 DLR (4th) 218, at 243 (SCC): “Unless the contrary is clearly indicated by the context, a word should be given the same interpretation or meaning whenever it appears in an Act.”) The CRA confirmed in its comments during the round table presentation at the 2013 IFA seminar, supra note 19, that it will generally look to the administrative policies for the application of subsection 15(2) for guidance on the application of the upstream loan rules.
35 See, for example, Kates v. MNR, 84 DTC 1605 (TCC).
36 94 DTC 1397 (TCC).
37 For example, one loan was used to finance the acquisition by the taxpayer of a new automobile, another for the purpose of erecting a storage building on a parcel of land that the taxpayer owned, and a third to allow the taxpayer to acquire a coffee shop franchise.
38 The minister contended that the repayment was not a bona fide repayment, or alternatively that it was part of a series of loans and repayments. Presumably this is based on the fact the taxpayer obtained a new loan (for the coffee shop franchise) just weeks after the repayment in question.
part of a series, Bowman J emphasized that each loan had been entered into “for a wholly different purpose.”

Bowman J sensibly interpreted the term “series” contextually, in light of the purpose underlying the particular provision before him. This is particularly appropriate given the Supreme Court of Canada’s endorsement in Canada Trustco of a “textual, contextual and purposive” approach to statutory interpretation. In Meeuse, Bowman J was careful to avoid adopting an overly broad interpretation of “series.” On balance, the case law suggests that for transactions to constitute a series, they require a common purpose.

The CRA seems to be in agreement with this view. It has stated that

[j]t is acceptable to have a repayment of an older loan and to make a new loan in the same year around the same time if the facts support the transactions. Given a situation where an earlier loan is made for a specific purpose, say to purchase equipment, and is to be repaid on or before a given date and subsequently another loan is made for a specific purpose, say to purchase land, around the date the earlier loan is repaid, we would accept this as being a repayment of an earlier loan and a new loan having been made, rather than insisting that it is part of a series of loans and repayments. On the other hand, if there are numerous non-specific loans and non-specific payments, it would be considered as part of a series of loans and repayments, in which case the increases in a particular year-end balance would be treated as a loan in that year and a decrease in a year-end balance would be treated as a repayment.

Thus, the CRA seems to agree that a repayment of a loan made for a specific identifiable purpose followed shortly by another loan made for a different specific identifiable purpose should not be considered to be part of a series. Conversely, the CRA seems to be of the view that repayments made in the course of a series of upstream loans for non-specific reasons and repayments that are clearly of a temporary nature should be treated as being part of a series.

Furthermore, in the case of successive loans, there is support for the argument that an intervening taxable event (such as payment of a dividend or a return of capital) should delink the loans such that they are not considered part of a series. In

39 Supra note 36, at 1400. In his decision, Bowman J stated, ibid., “Where we have a bona fide borrowing for a genuine business purpose[,] a repayment of the funds from an independent source[,] and an unrelated subsequent borrowing for a wholly different purpose[,] I do not think that this is the type of abuse at which the concluding words of [paragraph] 15(2)(b) are aimed.”


41 CRA document no. 9219115, October 5, 1992.

42 Ibid. See also chapter 24 of Canada Revenue Agency, Audit Manual (Ottawa: CRA) (“Transactions Involving Related Persons, Corporations and Shareholders, Dividends, etc.”), and comments in IT-119R4, supra note 19.
Attis v. MNR\textsuperscript{43} and Hill v. MNR,\textsuperscript{44} the Tax Court of Canada dealt with the situation where shareholders received loans from their respective corporations during a year, which were later repaid in whole or in part by the declaration of dividends or bonuses. In Attis, the taxpayer’s indebtedness to his corporation as at August 31, 1985 (the year-end of the corporation) was repaid in full by the payment of bonuses and dividends in early 1986. His indebtedness to the corporation as at August 31, 1986 was likewise repaid in full by the payment of bonuses and dividends in January 1987. The taxpayer asserted that subsection 15(2) had no application because any loan made by the corporation in a particular year had been completely repaid within one year from the end of the corporation’s fiscal year in which the loan was advanced. The minister argued that the taxpayer could not rely on the exception because the new advances in the following year made any repayment part of a series of loans or other transactions and repayments. The court concluded that Parliament could not have intended subsection 15(2) to operate in circumstances where the repayments involved a series of payments that were required to be included in the taxpayer’s income under specific provisions of the Act. A similar conclusion was reached in the Hill case.

In Income Tax Technical News (ITTN) no. 3, the CRA confirmed that, consistent with these cases, bona fide repayments of shareholder loans that are the result of the declaration of dividends, salaries, or bonuses should not be considered to be part of a series of loans or other transactions and repayments.\textsuperscript{45}

Therefore, when determining whether a specific repayment should be respected (as not being part of a series), it is important to consider the tax treatment of all transactions undertaken to fund the repayment, as well as the tax treatment of any new upstream loans that may come into existence.

It is a question of fact whether a repayment of a loan is part of a series of loans or other transactions and repayments. Because the taxpayer must establish that a repayment is not part of such a series, the facts and circumstances of each loan or indebtedness should be reviewed. In summary, on the basis of the discussion above, the following questions should be considered to determine whether a specific repayment to a creditor affiliate should be respected under subsections 90(8) and (14):

- What did the creditor foreign affiliate use the repayment funds for? Was another upstream loan (a “new” upstream loan) made to that or another specified debtor?
- How much time passed between the repayment and the making of the new upstream loan, and what did the creditor foreign affiliate do with the funds in the intervening period?

\textsuperscript{43} 92 DTC 1128 (TCC).

\textsuperscript{44} 93 DTC 148 (TCC).

If a new upstream loan was made, to what extent have the following changed when comparing the upstream loan that was repaid with the new upstream loan: debtor, creditor, principal amount, and, most importantly, the use by the specified debtor of the funds advanced under the new upstream loan?

If the creditor foreign affiliate has changed, what was the nature of the transactions undertaken to transfer the funds for the new upstream loan to the new creditor? If an upstream loan has been settled, what was the nature of the transactions undertaken between the creditor foreign affiliate and the specified debtor on settlement?

Is any new upstream loan that arises as part of the repayment specifically acknowledged and treated differently under the provisions of the Act?

**Failure To Repay the Loan**

If an upstream loan is not repaid within two years of the day on which the upstream loan was made (or deemed to have been made), the exception in subsection 90(8) will not apply, and an amount in respect of the upstream loan (equal to the specified amount) will be required to be included in the income of the Canadian taxpayer.46 The income inclusion pursuant to subsection 90(6) occurs in the taxation year that includes the time the upstream loan was made. Therefore, upstream loans repaid (other than as part of a series) after the two-year period will be subject to an income inclusion in the earlier year, with no offsetting deduction available until the subsequent taxation year in which the repayment is made. In this case, interest and penalties will be owing in respect of the specified amount.47 Therefore, if a taxpayer plans to rely on the two-year repayment exception to avoid the application of the upstream loan rules, it will be imperative to ensure that the repayment is made on time and that it is respected (that is, it is not considered to be part of a series) in order to avoid interest and, potentially, penalties.

**Transactions Subsequent to Upstream Loan**

The application of subsection 90(6) and other upstream loan rules is based on the relationships and tax attributes that exist at the time an upstream loan arises, with no reference to, or relief provided for, any subsequent changes in relationships. This becomes an issue if, for example, foreign affiliates of a Canadian taxpayer are

---

46 Assuming that neither the “ordinary course of business” exception nor the “ordinary course of an insurance business” exception (in paragraphs 90(8)(b) and (c), respectively) is met.

47 See CRA comments made during the roundtable presentation at the 2013 IFA seminar, supra note 19. The CRA was asked whether it would apply its administrative positions in respect of the shareholder loan rules to the upstream loan rules. As noted above, the CRA stated that it generally will look to the administrative policies for the application of subsection 15(2) for guidance on the application of the upstream loan rules; however, it specifically indicated that it would not be applying its administrative position set out in paragraph 38 of IT-119R4, supra note 19. The CRA’s intent is to enforce interest and penalties if there is a subsection 90(6) inclusion in a past taxation year and a repayment in a subsequent year.
disposed of to a foreign parent company during the first two years after an upstream loan arises (and before its repayment), or if a specified debtor ceases to be a specified debtor (in situations where the specified debtor is not the Canadian taxpayer or a non-arm’s-length Canadian entity) prior to a repayment.48

If a foreign affiliate that has made an upstream loan is disposed of for proceeds equal to fair market value, it does not seem equitable for the rules to continue to apply after the disposition. In this scenario, the upstream loan has been indirectly repaid in the form of proceeds (and if the sale is at the Canadian taxpayer level, the funds have also effectively been repatriated to Canada). As well, it is unclear how the Canadian taxpayer will be able to enforce or have any knowledge of the ultimate repayment of the upstream loan once the upstream loan is between two related non-residents.

The CRA is aware of this inequitable result;49 however, for the time being, planning will be required to ensure that transactions subsequent to the initiation of an upstream loan will not create adverse results pursuant to the upstream loan rules.

**Step 4: Decide If a Subsection 90(9) Deduction Can Be Claimed**

Once all upstream loans have been identified and it is clear that subsection 90(6) (or (12)) will require an income inclusion in respect of a specific upstream loan, taxpayers will want to determine whether a deduction can be claimed under subsection 90(9). According to the October 2012 explanatory notes, the purpose of this provision is to allow taxpayers to make loans rather than pay dividends when there is no tax benefit in doing so.50 To determine the amount deductible under subsection 90(9), a notional dividend (or dividends, if the creditor affiliate is lower-tier) is presumed to have been paid at the lending time by the lending affiliate up the chain to the taxpayer, and the deductions that would be available under paragraphs 113(1)(a), (a.1), (b), and (d) and subsection 91(5) are assessed. Paragraphs 90(9)(b) and (c) contain rules to ensure that tax attributes “used” in this manner to shelter an income inclusion relating to an upstream loan cannot also be used to shelter a different loan or an actual distribution.

48 The latter situation may be less likely to arise, because upstream loans are likely to be repaid prior to a third-party sale of the specified debtor or the upstream loan may be purchased by the acquirer. The sale of an upstream loan to a third party does not seem to meet the repayment requirement under the upstream loan rules.

49 See CRA comments made during the round table presentation at the 2013 IFA seminar, supra note 19. The CRA indicated that it agrees that this appears to be an inequitable result and is in consultations with the Department of Finance to determine the best way to proceed. See also CRA document no. 2013-049106, where upstream loans were required to be repaid immediately prior to the fair market value sale of all creditor affiliates to avoid the application of the upstream loan rules.

50 Supra note 33, at 153.
To quantify the amount of a subsection 90(9) deduction that may be claimed in respect of an upstream loan, it is necessary to have calculated certain tax attributes, including surplus balances for all foreign affiliates in the creditor affiliate chain, and, potentially, previously taxed FAPI amounts and the Canadian taxpayer’s cost base in the shares of its first-tier foreign affiliate. Furthermore, this information is required as at the date on which the applicable upstream loan arose (or was deemed to arise), since the subsection 90(9) deduction amount is calculated as if the notional dividend were paid on that date. This means that surplus earned or other attributes arising subsequent to making an upstream loan will not allow for an additional deduction under subsection 90(9), even though the deduction may be claimed on an annual basis. As discussed below, where a creditor affiliate makes multiple upstream loans at different times, each notional dividend under subsection 90(9) will have to take into account each such dividend that came before it.

Uncertainties Associated with Reserve Calculations

The operation of subsection 90(9) raises a host of unanswered questions and is probably what will create the most uncertainty as taxpayers apply the rules. This uncertainty stems from a lack of clarity concerning the relationship between the rules applicable to a notional dividend and the basic distribution rules that apply to actual dividends.

The two sets of rules will often give different results. For example, subsection 90(11) considers the net surplus of the creditor affiliate for the purposes of the notional dividend to include the net surplus of all lower-tier affiliates. That is not the case for actual dividends. On the other hand, a deduction is available under paragraph 113(1)(a.1) in respect of the hybrid surplus component of an actual dividend whether there is any associated hybrid UFT or not. With respect to the notional dividend, a deduction is permitted only if there is sufficient hybrid UFT to result in the hybrid surplus dividend being fully sheltered. Yet another difference relates to the deduction under subsection 91(5) for previously taxed FAPI. This is available in respect of a notional dividend only if the specified debtor is a non-resident.

There are many other situations that the upstream loan rules do not address. The question for taxpayers in these cases is whether the normal distribution provisions can be relied on or not. The following paragraphs touch briefly on four of the more pressing questions.

51 See clause 90(9)(a)(i)(B).

52 See subparagraph 90(9)(a)(ii). At the 2013 IFA seminar, supra note 19, the CRA was asked to comment on whether a reserve would be available under subsection 90(9) in respect of previously taxed FAPI if Canco were the specified debtor; the CRA said that it may be prepared to develop an administrative position that an election can be made to change the ordering so that the notional dividend is considered to be a distribution coming out of preacquisition surplus.
The 90-Day Rule
Assume that a foreign affiliate (FA) makes an upstream loan of $1,000 when it has no net surplus. Further assume that the loan was advanced more than 90 days from the beginning of FA’s taxation year and that FA earns net exempt earnings of $1,000 in that taxation year. The 90-day rule in regulation 5901(2) will apply to characterize an actual dividend as being paid from FA’s exempt surplus, making a full deduction available under paragraph 113(1)(a). However, it is not clear that a similar result arises under subsection 90(9). Clause 90(9)(a)(i)(A) refers to the exempt surplus of the affiliate in respect of the taxpayer at the lending time. At the lending time, there is no exempt surplus balance, unless the provision is read expansively to incorporate the operation of the 90-day rule.

As noted above, the premise behind subsection 90(9) appears to be to put a taxpayer in a similar position as if a dividend were paid rather than a loan made. From that perspective, it is consistent with the policy rationale of the upstream loan rules to allow taxpayers to take the 90-day rule into account when calculating the amount of a subsection 90(9) deduction.

Distribution Elections
The Act includes a number of elections that provide taxpayers with considerable flexibility in managing the consequences of actual dividends, including the following:

- the election in regulation 5900(2) that deems a dividend to be paid from taxable surplus ahead of exempt surplus;
- the election in regulation 5901(1.1) that deems a dividend to be paid from taxable surplus ahead of hybrid surplus;
- the preacquisition surplus election in regulation 5901(2)(b) that deems a dividend to be paid from preacquisition surplus; and
- the disproportionate election in respect of UFT under paragraph (b) of the definition of “underlying foreign tax applicable” in regulation 5907(1).

The question for taxpayers is whether these elections are available to them as notional elections when assessing the deductions available under subsection 90(9) in respect of notional dividends. Subsection 90(9) does not address this question. However, the October 2012 explanatory notes make it clear that the Department of Finance intended that the disproportionate election be taken into consideration when determining the hypothetical deduction under paragraph 113(1)(b).

53 Comparable language in respect of hybrid, taxable, and preacquisition surpluses is contained in clauses 90(9)(a)(i)(B), (C), and (D), respectively.
54 Supra note 33, at 153.
Similar to the application of the 90-day rule, it seems consistent with the policy rationale of the upstream loan rules to allow taxpayers to take these elections into account, unless the specific rules in subsection 90(9) provide otherwise.\textsuperscript{55}

Unlike the other elections listed above, the preacquisition surplus election must be filed jointly by all related Canadian corporate taxpayers that have a surplus entitlement in the lender foreign affiliate. Thus, it may also be appropriate to require all such related Canadian taxpayers to take a consistent position in their tax filings related to the upstream loan rules.

**Capital Gains Pursuant to Subsection 40(3)**

Assume that Canco owns 100 percent of the shares of FA 1, and FA 1 owns 100 percent of the shares of FA 2. FA 2 makes a loan to Canco of $1,000 when FA 1 has a net exempt surplus balance of $750 and FA 2 has nil net surplus. Also assume that the ACB of FA 1 in the shares of FA 2 is nil.

If FA 2 were to pay an actual dividend of $1,000 up the chain to Canco, FA 1 would experience a gain of the same amount pursuant to subsection 40(3). This gain would have surplus consequences for FA 1 that would depend on whether the shares of FA 2 were excluded property or not. Those surplus consequences could also affect the character of future dividends received by Canco.

This example raises two questions:

1. Is surplus upstream of the lending affiliate available for the purposes of subsection 90(9)?
2. Are downstream subsection 40(3) gains ignored for the purposes of subsection 90(9)?

On the basis of the examples in the October 2012 explanatory notes, the answer to both questions appears to be yes.

From the explanatory notes, it appears that the intention is for the surplus balances (or deficits) in the entire foreign affiliate chain of investment, extending from the taxpayer down to the lender affiliate, to be taken into account in determining the amount deductible under subsection 90(9). There is no mention of other tax attributes that would be relevant if an actual dividend were paid. In example 1 in the explanatory notes,\textsuperscript{56} FA 2 does not have sufficient surplus to support a hypothetical dividend of $800. A portion of the dividend hypothetically paid to FA 1 in that example would be from preacquisition surplus. The example also states that there is no ACB in the shares of FA 2. Consequently, an application of the entire foreign affiliate regime when assessing the implications of this hypothetical dividend would result

---

\textsuperscript{55} On the basis of comments made at the 2013 IFA seminar, supra note 19, the CRA may be open to this suggestion, at least as it relates to a regulation 5901(2)(b) election.

\textsuperscript{56} Supra note 33, at 156-58.
in a subsection 40(3) gain to FA 1. The example does not address that possibility, but concerns itself only with the movement of surplus from affiliate to affiliate. On the basis of this example, ACB appears to be relevant only when the notional dividend is paid from a top-tier affiliate to a taxpayer, at which point a notional deduction under paragraph 113(1)(d) becomes a consideration.

**Reorganizations**

The upstream loan provisions lack rules to deal with situations where loans are transferred within a foreign affiliate group as a result of certain reorganization transactions. For example, assume that Canco owns 100 percent of the shares of FA 1, and FA 1 owns 100 percent of the shares of FA 2. FA 2 makes a loan to a specified debtor in year 1. In year 2, FA 2 liquidates into FA 1.

As a consequence of the liquidation, the specified debtor becomes indebted to FA 1 in year 2. Thus, it appears that both subsections 90(6) and (12) apply with respect to the same loan, resulting in a double income inclusion. A deduction under subsection 90(9) should be available in year 2, but there does not seem to be a way to eliminate the second income inclusion. In particular, the loan owing to FA 2 has not been repaid to FA 2, and in fact can no longer be repaid to FA 2.

The issue described above could arise through any form of assignment of the loan that results in a new creditor. Similar issues may occur when there has been an assumption resulting in a new debtor. It is suspected that these situations will be common.

It is hoped that the CRA will agree to provide administrative relief in situations, such as those described above, where subsection 90(6) could apply more than once to the same loan or debt.57

**Surplus Accounting Implications**

It is fair to say that most taxpayers prepare surplus calculations only to the extent necessary to justify deductions claimed under subsection 91(5) or 113(1). They will now also have to prepare surplus calculations to support deductions claimed under subsection 90(9). These calculations must also address the rather severe requirements imposed by paragraphs 90(9)(c) and (d), under which surplus and cross-border ACB earmarked for a particular upstream loan must not be used to support any other loan or any actual (or deemed) dividend. The October 2012 explanatory notes confirm that this is an all-or-nothing condition—any amount used twice, no matter

---

57 The CRA does currently provide administrative relief in similar situations involving the shareholder loan rules. In CRA document no. 2005-0129551E5, June 21, 2005, the CRA concluded that the assignment of a loan from Lendco to a related corporation would not result in a new loan or indebtedness under subsection 15(2), provided that there was no novation of the loan and the terms and conditions of the loan remained unchanged.
international tax planning

how small, will result in a loss of the subsection 90(9) deduction in all future years in respect of that particular upstream loan.58

In straightforward situations, where there are few upstream loans with stable balances, it may be sufficient to merely add a note or addendum to the existing surplus calculations. In more complex situations, parallel calculations will be required, especially if there are actual dividends to track as well. For example, if certain of the distribution elections are claimed for the purposes of subsection 90(9), the remaining tax attributes for this purpose may differ markedly from the actual surplus balances. Transactions subsequent to the lending time that result in changes in the SEP in the lending affiliate will also cause differences between actual and notional surplus, since the notional surplus will continue to be based on the tax attributes available at the time of the loan.

Fluctuating upstream loan balances will also present a difficult challenge. Incremental increases typically would be treated as new loans requiring a determination of surplus balances at the time of each increase.

CONCLUSION

The introduction of the upstream loan rules is a significant change in policy. Even though the upstream loan provisions are modelled on the shareholder loan rules, many interpretive and practical questions remain. Taxpayers should expect a long process consisting of technical amendments, ruling requests, technical interpretations, and perhaps jurisprudence before any certainty is gained with respect to the application of the new rules. In the meantime, decisions need to be made regarding existing upstream loans as well as the effect of the new rules on future planning and cash flow requirements.

This article has provided a framework for approaching the application of the upstream loan provisions to specific situations, together with a discussion of some of the uncertainties inherent in the rules. With respect to existing upstream loans, taxpayers will want to ensure that a comprehensive review is undertaken to identify and act on problem loans. Taxpayers will also need to develop policies and procedures (often working internally with their treasury groups) for identifying and monitoring upstream loans. From a planning perspective, some taxpayers may look at options such as restructuring their foreign affiliate group to minimize the effect of the rules.

58 Supra note 33, at 154.
APPENDIX  DETERMINING WHETHER THE UPSTREAM LOAN RULES APPLY

Did a “specified debtor” receive a loan from a foreign affiliate (FA) of the Canadian-resident taxpayer?

Yes  No

A grandfathered loan is a loan received or indebtedness incurred on or before August 19, 2011.

Is an FA of the taxpayer a member of a cash pool arrangement?

Yes  No

Did the nature of the cash pool arrangement create an intercompany receivable from a specified debtor to an FA?

Yes  No

Did the specified debtor incur any other type of indebtedness owing to an FA (such as trade accounts payable, other intercompany payables)?

Yes  No

Was the loan or indebtedness “grandfathered”?

Yes  No

Did the grandfathered loan remain outstanding on August 19, 2014?

No  Yes

Was the grandfathered loan repaid (other than as part of a series of loans or other transactions and repayments) on or before August 19, 2016?

No  Yes

Did the indebtedness arise in the ordinary course of the business of the creditor or was the loan made in the ordinary course of the creditor’s money-lending business?

Yes  No

Were bona fide arrangements made for repayment within a reasonable time?

Yes  No

Upstream loan rules do not apply

A “specified debtor” is

■ the Canadian-resident taxpayer or a person not dealing at arm’s length with the taxpayer (other than a controlled foreign affiliate as defined in section 17), or
■ a partnership that includes either of the above among its members.

Note: The exception in paragraph 90(8)(c), relating to amounts arising in the ordinary course of carrying on a life insurance business outside Canada, is not included in this decision tree.