CANADIAN TAX Highlights

Editor: Vivien Morgan, LL.B.

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## GST Due Diligence Policy

Earlier this year, in Policy no. P-237, Revenue finally recognized a due diligence defence to the penalty portion of GST assessments. (The defence does not affect the interest portion.) That defence was accepted in numerous TCC decisions and confirmed by the FCA on September 29, 1998 in *Consolidated Canadian Contractors*; the policy is effective from the date of that decision. Revenue says in the policy that it "accepts that [if it] determines that a person has exercised due diligence, the penalty is not exigible." In view of the jurisprudence, Revenue may be obliged to accept the defence, the availability of which is not predicated solely on Revenue's determinations. A careful reading of the policy suggests that Revenue's acceptance may be tempered by setting an unduly high standard to establish the defence.

The onus of establishing that due diligence was exercised is on the claimant. Because the defence is fact-specific, the policy does not set out any criteria, but says that a person must demonstrate that he or she made a sincere and demonstrable attempt that a reasonably prudent person would have made in similar circumstances to comply with GST payment or remittance obligations. It appears that Revenue is of the view that an incorrect assumption based on genuine uncertainty regarding the application of the Act must have prevented compliance. For example, there is no defence if the failure arose because of computation errors or because of errors due to a failure to maintain adequate records. One might expect even a reasonably prudent person to sometimes make calculation errors; due diligence is not perfect diligence. Revenue says that there is no defence for late remittance and generally none for late payment. Nor is reliance on incorrect advice from a third party an excuse, in Revenue's view, unless actions taken by a person's "authorized representative" lend support to the defence; a person's level of sophistication may also be a relevant factor.

The policy sets out four specific examples to illustrate Revenue's position; one involves errors by an outside bookkeeping firm used for GST accounting and return preparation. Revenue says that no due diligence defence exists because the "bookkeeping firm does not provide any credible evidence to demonstrate that any particular action [it took] on behalf of the registrant lends support to the registrant's due diligence defence," although there is no indication that the registrant knew or ought to have known of the errors. Was there not a sincere and demonstrable attempt that a reasonably prudent person in similar circumstances would have made to comply with GST obligations? Is the use of a bookkeeping firm rather than an accounting firm critical? Should the issue of cost in the light of the size and sophistication of the business be relevant?

Of the four examples in the policy, Revenue says that only one raises a sustainable defence. The item in issue is an "energy bar" (a candy bar, in Revenue's view) sold by the sole proprietor of a weight-training equipment store. A number of steps are taken to determine the product's tax status, including contacting Revenue's local office, reviewing publications, and obtaining a professional opinion. The example suggests that the defence requires the taxpayer to make significant efforts and expenditures on professional fees. The very low small-supplier registration threshold means that the many small businesses that must register to collect and remit GST lack the resources to retain professional advisers to resolve difficult tax questions, particularly ones concerning items like the "energy bar" that probably do not generate significant revenue. The TCC in *Skylink Voyages* commented that tax provisions should be drafted so that ordinary people can readily understand them without excessive expenditures of time or money.

Overall, the policy is a helpful development. But the examples indicate an extremely high standard of care, and in some cases the fact that an error was made seems proof that the standard was not met. It is hoped that the acceptance of the defence signals a shift in the

### In This Issue



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practice of field audits and at the objection stage: in the past, due diligence arguments met with no success outside the courts.

*James Warnock*
McMillan Binch, Toronto

## Complete That Application

The IRS recently revised its procedures allowing a foreign person who disposes of a US real property interest to obtain a withholding certificate to reduce US tax withheld. Foreign persons are subject to US tax on gains from dispositions of interests in US real property as if those gains were derived from a US trade or business. Generally, the US tax withheld from the proceeds can be reduced or eliminated if the foreign person obtains a withholding certificate from the IRS before the transfer.

Modifications to the application procedure require reporting about any tax returns filed with respect to the US real property interest being transferred; a statement of the contract price; the identification of prior non-recognition transactions involving the property; information pertaining to an exemption available to foreign governments; and specific identification of the property covered by certain agreements. The revisions also include certain clerical matters. The IRS warns that substantially incomplete applications will be rejected—for example, those that omit a specific or estimated transfer date. To ensure completeness, all applications should incorporate the changes and rely on the sample applications in the revised procedure. Rev. Proc. 2000-35 is effective 30 days after August 28, 2000.

*Paul Hickey*
KPMG LLP, Toronto

## US FSC Successor

On July 27, 2000, the US House Ways and Means Committee favourably reported on the FSC Repeal and Extraterritorial Income Exclusion Act of 2000. Earlier this year, the World Trade Organization (WTO) made a final determination that the FSC regime for US exporters constituted a prohibited export subsidy under articles 3.1(a) and 3.2 of the WTO Agreement on Subsidies and Countervailing Measures and articles 10.1 and 8 of the WTO Agreement on Agriculture. The act represents the US government's response.

The proposals' repeal and replacement of FSCs affect both US exporters and certain foreign producers of goods sold outside the United States. The act is expected to be taken up by both houses of Congress in September and, if passed, to be signed by the president before October 1; changes before enactment are quite possible. A new general rule provides that gross income does not include "extraterritorial income"—gross income attributable to foreign trading gross receipts other than non-qualifying foreign trade income. Deductions and foreign tax credits are denied if they are allocable to extraterritorial income that is excluded from gross income. Only some extraterritorial income may be excluded: 30 percent of income from foreign sale and leasing, 1.2 percent of foreign trading gross receipts, or 15 percent of foreign trading income. Excludible income under the 1.2 percent method may not exceed 2 times 15 percent of foreign trading income.

The act is effective October 1, 2000, and no new FSCs may be established as of that date. Existing FSCs may continue to operate under a transition rule until December 31, 2001, or until the expiration of a previously effective and binding contract under which the FSC is acting. FSC users must determine when their FSC rights end and, along with non-US manufacturers and distributors of qualifying property, must assess their eligibility under the new rules.

*James J. Tobin*
Ernst & Young LLP, New York

## New Facts, Same Story?

Statistics Canada has changed the way it measures economic activity in Canada. In its national income and expenditure accounts, employee and employer contributions to government-run employee pension plans are no longer considered direct taxes on persons, and plan spending is no longer treated as government spending: instead, the basic operations of the funds are taken into the personal sector. Not surprisingly, this changes the ratio of taxes collected to gross domestic product (GDP).

Under the new system, taxes collected in 1999 by all levels of government equalled 37.0 percent of GDP, down fractionally from last year's all-time high of 37.1 percent (37.9 percent as recorded under the old system of accounting). The new figures reinforce the fact that taxes have remained high in relation to GDP despite substantial economic growth and some personal income tax reductions. (See "Now That's Elasticity!" *Canadian Tax Highlights*, November 23, 1999, at 82.)

The 1998 and 1999 budgets reduced federal personal income tax (PIT) rates, cuts that may have partly contributed to the reduced 1999 ratio of federal PIT to GDP, down to 8.5 percent from the high of 8.8 percent in 1998, and just a tick above the recession high of 8.6 percent. Provincial PITs have been less volatile, but at 5.5 percent of GDP in 1999 they are only one-tenth of one percentage point below 1991's all-time high. Employment insurance premiums dropped from a high of 2.6 percent of GDP in 1992 to a low of 1.9 percent in 1999, offsetting the increase in CPP and QPP collections, which rose from 1.7 percent in 1992 to 2.2 percent in 1999.

The corporate share of the income tax burden has risen dramatically since the recession. As the losses of the early 1990s were used up in later tax years, and as the tax reform measures of the late 1980s took hold, the federal take rose to 2.5 percent of GDP in 1999, the highest since 1984. Provincial corporate income tax collections equalled 1.4 percent of GDP in 1999, the highest ever recorded.

As restraint and tax freezes became popular at the local level, the post-recession period has seen local tax revenue (mainly property tax) drop from 4.1 percent of GDP in 1992 to 3.4 percent in 1999. In 1998 and 1999, the growth in local tax collected was very close to 1 percent, less than the rate of inflation.

**Tax Revenue of All Levels of Government, 1988, 1992, and 1999 (as a Percentage of GDP)**

| | 1988 | 1992 | 1999 |
|---|---|---|---|
| Federal | | | |
| Personal income tax | 7.6 | 8.6 | 8.5 |
| Corporate income tax | 1.9 | 1.4 | 2.5 |
| Employment insurance | 1.9 | 2.6 | 1.9 |
| Indirect taxes | 4.3 | 4.4 | 3.8 |
| Other taxes | 0.3 | 0.2 | 0.3 |
| Provincial | | | |
| Personal income tax | 5.1 | 5.3 | 5.5 |
| Corporate income tax | 0.9 | 0.6 | 1.4 |
| Contributions to social insurance | 0.9 | 0.8 | 0.7 |
| Indirect taxes | 6.1 | 6.7 | 6.9 |
| Local government taxes | 3.4 | 4.1 | 3.4 |
| CPP and QPP | 1.3 | 1.7 | 2.2 |
| Total | 33.6* | 36.5 | 37.0 |

* Total differs due to rounding.

Each year, the release of up-to-date national income and expenditure account data provides a glimpse of where our tax system is going. The remarkable economic growth over the last five years has not been accomplished by reducing the tax take or by old-fashioned economic policy; it occurred while government revenues were constant or growing and spending was restrained. Prosperity came as the Canadian government sector moved from a deficit equal to 9.2 percent of GDP in 1992 to a surplus of 2.2 percent in 1999.

*David B. Perry*
Canadian Tax Foundation, Toronto

## BARBADOS' GLOBAL NEWSLETTER

In July 2000, the government of Barbados introduced a new "Barbados Global E-Letter" to provide commentary and news on issues relevant to Barbados and the partners of CARICOM (the Caribbean community). The first issue indicates that Barbados' policy is to attract businesses of substance. As part of a much larger vehicle to assist parties in applying to do business there, Barbados is developing a Web site (expected to come online in 2001) to allow interested parties access to the newsletter, which Barbados can currently transmit by e-mail. Further information can be obtained by contacting the Ministry of Industry and International Business at (246) 430-2200.

The newsletter also says that Barbadian officials have corresponded with the OECD concerning its report on harmful tax competition. That report placed Barbados on a list of tax havens and threatened sanctions against listed countries that do not eliminate harmful tax practices. The minister indicated that Barbados continues to provide the OECD with information on Barbados to facilitate its accurate processing, but said that Barbados cannot bind itself to principles whose parameters have not yet been articulated by the OECD. Barbados is not an OECD member—and thus has neither rights nor obligations under the OECD model treaty, charter, and other instruments—but supports the views enshrined in international agreements such as those of the World Trade Organization (WTO). Although the government of Barbados will consider OECD recommendations, like many OECD members it cannot circumscribe its own parliamentary process. The minister also referred to a statement from the Global Conference on the Development Agenda for Small States, which noted that the OECD study caused concern for a number of small states "because of the lack of adequate consultation on the matters being addressed. . . . It is important for all these issues to be considered in international fora where small states themselves have a voice so that their multilateral institutions can study issues and look for solutions that pay proper regard to the interests of small states as well as [to] the need to foster stability in the global financial system."

The newsletter also noted US proposals to repeal FSCs and the concern in the European Union that they may not satisfy the United States' WTO obligations. The newsletter recited the US House Ways and Means Committee's view that the proposals' tax benefits related to foreign sales are not export-contingent and apply whether the goods are manufactured abroad or domestically. The proposals are said to exclude tax on certain extraterritorial income, which is the US general rule: because no tax is forgone, there is no subsidy. The proposals address the issues of using low- or no-tax jurisdictions and eliminate administrative pricing rules that are said by the European Union to violate the arm's-length pricing provisions of the WTO agreement. The Barbadian ministry has held meetings with the Barbadian business community concerning these developments and will continue to treat them as a priority matter.

**Note**: The WTO ruled that the FSC program was an illegal trade subsidy and gave the United States until October 1, 2000 to remedy the situation. In late August, the EU trade commissioner told the deputy US treasury secretary that the US proposals are still offside because they continue to depend on exports and the transitional rules extend the FSC rules well beyond the WTO deadline. Sources say that the European Union may return to the WTO after the deadline to seek a ruling if the new rules are enacted, and will probably seek the right to impose trade sanctions on at least $4 billion of US goods.

*John Haag and John Jakolev*
Ernst & Young LLP, Toronto

## US Offshore Trust Regs

In August 2000, the US Treasury issued more proposed regs that follow several rounds of proposed and final regs to implement 1996 income tax legislation related to US citizens or residents connected with offshore trusts. The proposed regs continue to tighten the rules and bode a continuing focus in this area.

The latest regs, like earlier ones, are drafted broadly to cast the tax web further and are primarily concerned with section 679 grantor trusts: a foreign (non-US) trust created by a US person (a US citizen or resident) and with one or more US-person beneficiaries. The US person who creates or transfers assets to such a trust—the grantor—is treated as owning the trust assets and is taxable on trust income, even if he or she is not a trust beneficiary or is a beneficiary not in receipt of trust distributions.

One of the key determinants of section 679 trust status is the existence of a US beneficiary, a test made annually. A foreign trust is treated as having a US beneficiary unless during the year no part of the income or corpus of the trust may be paid or accumulated to or for the benefit of, directly or indirectly, a US person, and no part thereof may be so paid if the trust is terminated during the year. Actual payments or accumulations are not required; the US person's trust interest may be contingent, unless it is so remote as to be negligible. In establishing these facts, reference is made not only to the trust instrument but also to other written or oral agreements or understandings relating to the trust. For example, a simple contrary declaration in the trust instrument that no US person may benefit does not override the fact that a trust can be amended to provide a US beneficiary; that the parties to the arrangement may be "reasonably expected" to disregard the trust's terms; or that a US beneficiary may benefit indirectly, for example, through a corporation or a partnership, via an intermediary, through the use of a debit or credit card or by "any other means may obtain an actual or constructive benefit from the trust."

The proposed regs also characterize a transfer by a US person broadly—for example, if a US person transfers indirectly through an intermediary or guarantees a foreign trust's obligation. A transfer by a US person to an entity owned by a foreign trust may be recharacterized as a transfer to the trust, unless the US person demonstrates that the actual transfer relates to his or her ownership interest in the entity. Generally, an FMV exception applies, but an obligation issued by the trust or a related person must be a qualified obligation: reduced to writing, with a term not exceeding five years, payments denominated in US dollars, and a yield to maturity in the range of 100 to 130 percent of the US applicable federal rate. Other conditions must be met, including an annual loan status report by the US grantor on IRS form 3520 while the loan is outstanding.

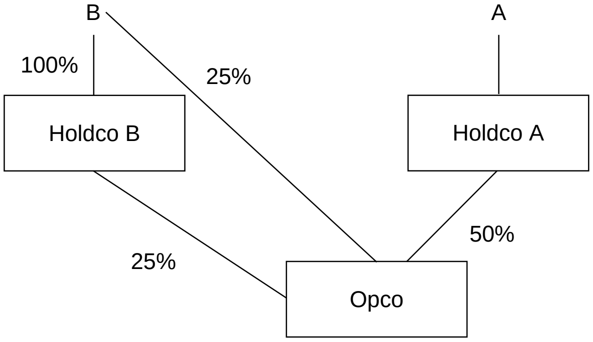
The proposed regs also cover pre-immigration trusts. A non-resident alien individual who becomes a US person within five years after directly or indirectly transferring property to a foreign trust is deemed to have made the transfer on the day his or her US residency starts. Within 90 days of that date, the individual assumes reporting obligations relating to the deemed transfer and is taxed on trust income if US persons are trust beneficiaries.

*Carol A. Fitzsimmons*
Hodgson Russ Andrews Woods & Goodyear LLP, Buffalo

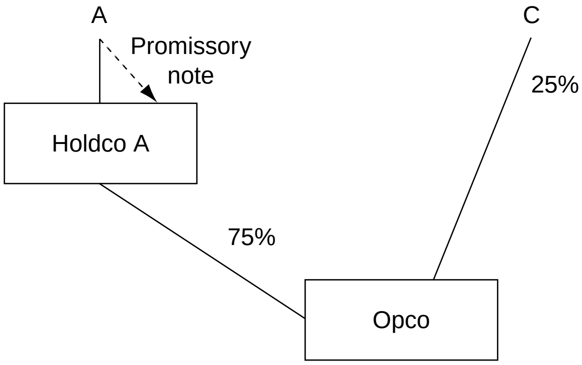
## Specific Shares: Section 84.1

In a recent technical interpretation, Revenue says that for the purposes of section 84.1 a taxpayer may specifically identify the shares in respect of which a capital gains exemption (CGE) was claimed by a non-arm's-length person.

Assume that Mr. A acquires the 25 percent of Opco shares held by his brother, Mr. B (who claims a CGE) and the 25 percent held by Holdco B, which is owned by




Mr. B. Mr. B's and Holdco B's cost bases are nominal: thus their gains both equal the full proceeds. Mr. A then sells 25 percent of Opco's shares to an unrelated person, Mr. C, and transfers 25 percent to his own corporation (Holdco A) in exchange for a promissory note.




If the shares acquired from Mr. B are transferred to Holdco A, Mr. A is deemed to have received a dividend in the amount of the promissory note. But if the shares acquired from Holdco B were so transferred, no deemed dividend results: the ACB of those shares equals the amount of the promissory note. For the purposes of section 84.1, a taxpayer's ACB of a share acquired from a non-arm's-length person is reduced by the CGE claimed by that person on the share's previous disposition, or such lesser amount as is established by the taxpayer. The technical interpretation says that the onus of establishing such a "lesser amount" is on the taxpayer. However, if the taxpayer holds other shares that are identical properties, the Act does not specify a procedure for determining which particular shares were the subject of a CGE claim. There is no clear prohibition against earmarking shares as not tainted by a CGE claim and no obvious reason why such a selection should not be available; Revenue therefore concludes that a taxpayer may identify the shares to which the previously claimed CGE attaches by including a designation in the form of a written statement in his or her return. Revenue considers the designation binding.

*Wayne Tunney and Lori Dunn*
KPMG LLP, Toronto

## Reciprocal Insurance and GST

In *Healthcare Insurance Reciprocal of Canada*, the TCC concluded that an unincorporated body that was not a registered insurer had supplied exempt insurance services and therefore need not charge GST and could not claim input tax credits (ITCs).

Healthcare was an unincorporated group of healthcare institutions across Canada, most of which were hospitals. The group was established so that its members would be permitted under insurance legislation to exchange mutual or self-insurance. Excess liabilities of such an organization, a reciprocal, are generally funded by open-ended assessments against each subscriber member. The reciprocal vehicle has been described as "a sophisticated form of not-for-profit self/mutual insurance requiring a structure and professional expertise not unlike an insurance company." For the purposes of the Ontario Insurance Act, the subscriber-members are

SHOE *by Jeff MacNelly*

not insurers, but the reciprocal must be licensed. Healthcare engaged in monitoring and arranging for the defence and settlement of claims, administering funds, coordinating and implementing the interexchange of insurance between the members, risk management, regulatory compliance, and accounting and record-keeping services. Healthcare was licensed as a reciprocal or interinsurance exchange under various provincial insurance statutes, but was not provincially or federally registered to sell insurance to the public.

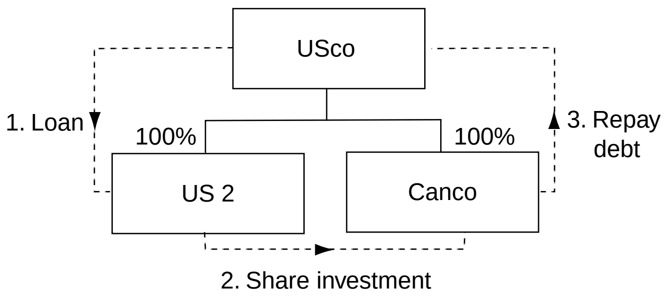
Healthcare's tax advisers indicated that its supplies to the hospitals were taxable for GST purposes. Healthcare registered and began charging GST and claiming ITCs. Revenue concluded that Healthcare was engaged exclusively in exempt financial supply insurance services and could not claim ITCs. Healthcare argued that it had not issued the insurance contract and was not an insurer as defined under the Excise Tax Act (ETA)—a person licensed or otherwise authorized federally or provincially to carry on an insurance business; it held its licences merely as a medium for the exchange of self-insurance by its members. The minister said that provincial licensing as a reciprocal was enough, and the court agreed. The court cited Ontario case law that said that a reciprocal had the capacity to sue in its own name. The court said that Healthcare implicitly took on risk under its arrangements with the hospitals even though they ultimately underwrote those risks: the court held that in substance Healthcare carried on an insurance business and was an insurer under the Ontario Insurance Act and the ETA. Each of the following factors was important: (1) the hospitals could only function as an insurance organization through Healthcare; (2) the hospitals did not have legal title to or responsibility for Healthcare's investments; (3) Healthcare was a licensed and audited entity with liabilities, reserves, accounts payable, premium taxes, etc., and had underwriting revenue and underwriting profit; and (4) the hospitals paid premiums to Healthcare for claims, adjusting and defence costs, reinsurance, premium taxes, reserves, operating expenses, etc. Without further elaboration, the court said that Healthcare's activities fell within the definition of "financial services": "the issue, granting, allotment, . . . renewal, [or] processing . . . of an [insurance policy], payment . . . of a claim arising under an insurance policy, or agreeing to provide, or arranging for" a financial service. The court also noted that Healthcare had described itself in its 1997 report as "the largest health care liability insurer in Canada" and as providing, inter alia, comprehensive insurance coverage to its subscribers.

Why did Revenue take the position that GST did not apply to Healthcare's activities? Hospitals are not required to charge GST on their own services, and may obtain an 83 percent rebate of any GST paid to Healthcare under the Public Service Body Rebate regulations. Thus, only 17 percent of the value of Healthcare's services was ultimately subject to GST, and Healthcare was taking ITCs on all its inputs. If Healthcare was denied ITCs, more GST was probably ultimately remittable.

*Rob Kreklewetz*
Millar Wyslobicky Kreklewetz, Toronto

## Not Comfortably in Debt

Further to the February 1998 federal budget, interest income may be imputed to Canadian-resident corporations on indirect loans that remain outstanding for one year or more. (See "Foreign Debt, Take Three," *Canadian Tax Highlights*, April 20, 1999, at 27.) Inappropriate results continue to surface.




Assume that USco owns 100 percent of Canco. USco financed Canco with both debt and equity in compliance with the existing 3-to-1 thin capitalization ratio. The ratio's proposed reduction to 2-to-1 prompts the following steps: USco lends funds (with or without interest) to US 2, a wholly owned subsidiary; US 2 invests in treasury shares of Canco; Canco then uses the proceeds to repay a portion of its existing debt to USco. The result? Canco is taxed on imputed interest on the USco-US 2 loan if it remains outstanding for more than a year. It is reasonable to conclude, as the indirect loan rules require, that USco made the loan to US 2 in anticipation of Canco's transfer of property—a cash repayment of its debt to USco. Canco's cash transfer is not exempt: it is made to a related person. The indirect loan provisions continue to apply in situations totally outside the policy intent of the original budget proposal. Until Finance revisits and revamps the provisions, all structures involving intercorporate debt between non-residents should be carefully tested.

**Non-resident trust and foreign investment entity (FIE) proposals.** Finance announced that the consultation period is extended to year-end and implementation deferred to taxation years beginning after 2001. Further changes include exclusion of interests in US regulated investment companies (RICs) from FIE rules; modest restriction of the "investment property" definition; and a review of the term "carrying value" to ensure fairness and "facilitate [taxpayers'] use" of the rules.

*Allan R. Lanthier*
Ernst & Young LLP, Montreal

## Shall I Compare Thee?

*Information Circular* 87-2R, dated September 27, 1999, says that Revenue may assess using "third-party comparable information" in transfer-pricing disputes. Such information is confidential and disclosure is prohibited, subject to certain noted exceptions. Revenue is expected to issue soon a technical memorandum addressing the subject of secret comparables.

The use of such confidential information may present problems, particularly concerning its comparability in fact. For example, does geographic location affect comparability? The method of accounting for costs—direct costing versus absorption costing—may be critical and may require an analysis of each party's cost of goods sold. The period covered must also be comparable, and not just in terms of its length. For high-tech and pharmaceutical firms, the level of SR & ED expenditures incurred by the third party should also be comparable. How comparable is the third party's capital structure, its mix of equity and debt? How comparable are the accounting principles that are applied? Are there one-time gains or losses included in gross profit? Because the third-party information is confidential, the taxpayer cannot conduct its own comparison. Without sufficient information or answers to these and similar questions, taxpayers may have good reason to be skeptical about comparability. For third-party comparables to be meaningful, there must be sufficient similarity of qualitative and quantitative characteristics, and adjustments may be required to provide consistency between the taxpayer's and the third party's financial data. But the lack of opportunity to scrutinize the so-called comparable that establishes the benchmark may place the taxpayer in the unusual and uncomfortable position of not knowing the case it has to meet.

*Richard M. Wise*
Wise Blackman, Montreal

## Don't Waste Capital Dividends

The reduction in capital gains rates may affect the structuring of corporate-owned life insurance buy-sell arrangements.

| | Capital dividend to estate | |
|---|---|---|
| | Full | One-third |
| Redemption price ....... | $1,000,000 | $1,000,000 |
| Less PUC ............. | (100) | (100) |
| Deemed dividend ....... | $ 999,900 | $ 999,900 |
| Capital dividend ......... | (999,900) | (333,300) |
| Taxable dividend ........ | nil | $ 666,600 |
| Tax to estate on taxable dividend (32%) ........ | nil | $ 213,312 |
| Redemption price ....... | $1,000,000 | $1,000,000 |
| Less deemed dividend ... | (999,900) | (999,900) |
| Proceeds .............. | $ 100 | $ 100 |
| Less ACB ............. | (1,000,000) | (1,000,000) |
| Capital loss otherwise determined ........... | ($ 999,900) | ($ 999,900) |
| Less stop-loss (capital dividends: $999,900 and $333,300 respectively) minus ⅓ of lesser of capital gain on death and capital loss otherwise determined ($333,300) | 666,600 | nil |
| Capital loss ........... | ($ 333,300) | ($ 999,900) |
| Taxable capital gain to estate ($1,000,000 proceeds – $100 ACB) × ⅔ ....... | $ 666,600 | $ 666,600 |
| Allowable capital loss carried back .......... | (222,200) | (666,600) |
| Net taxable capital gain ... | $ 444,400 | nil |
| Tax to deceased (47% assumed) ....... | $ 208,868 | nil |
| Net receipt to estate ($1,000,000 – $208,868 and $213,312 respectively) ......... | $ 791,132 | $ 786,688 |
| Capital dividend available to survivor ............. | nil | $ 666,700 |

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Canadian Tax Foundation
595 Bay Street, Suite 1200
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Internet: http://www.ctf.ca

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Assume that a corporation pays the premiums for life insurance and is the beneficiary. The proceeds will be used to purchase the deceased's shares for cancellation. The life insurance was acquired after April 26, 1995 and thus is not grandfathered from the stop-loss rule in subsection 112(3.2). The deceased's shares are deemed disposed at death and are not rolled to a spouse but are purchased for cancellation in the estate's first taxation year; an election under subsection 164(6) carries back the capital loss to reduce the gain on death. The example shown in the table assumes that the deceased owned half of Opco's issued shares and had already used his capital gains exemption; the surviving 50 percent shareholder is unrelated. Both the FMV at death and the share price under the buy-sell are $1 million. The shares' ACB and PUC are both $100. On the basis of these assumptions, it is not tax-efficient to designate more than one-third of the available capital dividend in respect of the deemed dividend on the shares' purchase for cancellation. Declaring additional capital dividends does not appreciably enhance the estate's after-tax receipt, and the surviving shareholder may later benefit from a declaration in his favour of a tax-free capital dividend equal to two-thirds of the insurance proceeds.

*Jack Bernstein*
Aird & Berlis, Toronto

# Foreign Tax News

## Treaties

Treaties with **Algeria**, **Austria**, **Bulgaria**, **Japan**, **Jordan**, **Kyrgyzstan**, **Lebanon**, **Luxembourg**, **Portugal**, and **Uzbekistan** received royal assent on June 29, 2000. (See the treaty table in "Foreign Tax News," *Canadian Tax Highlights*, August 29, 2000, at 64.) Finance will advise as notice of ratification is received from treaty partners.

## Slovak Republic

The republic has been invited to become the 30th member of the OECD upon depositing its instruments of accession to the OECD convention with the French government. Until then it is invited to participate as an observer in the work of all OECD bodies.

To attract foreign investment, a new Slovak agency will process investment applications and negotiate incentives for a 10-year tax holiday and employment subsidies for foreign entities that invest at least SKK 100 million in Slovakia. A qualified foreign investor is a Slovak entity with at least 75 percent of its paid-up capital from non-Slovak sources throughout the subsidy period.

## Mexico

Ten percent withholding on interest payments to foreign entities, scheduled to expire on January 1, 1999 and later extended to December 31, 1999, is further extended to December 31, 2000.

## OECD

The technical advisory group has finalized its report characterizing e-commerce payments for treaty purposes. The report includes comments on the March draft report and covers issues such as business profits, royalties, provision of services, technical fees, and mixed payments.

*Carol Mohammed*
Canadian Tax Foundation, Toronto