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TAX LAW BULLETIN

Borden Ladner Gervais

NEW "FOREIGN AFFILIATE DUMPING" RULES CONSTITUTE MAJOR CANADIAN TAX POLICY CHANGE

Relevant to: Foreign-controlled Canadian corporations that own or acquire shares of a foreign corporation; foreign purchasers of Canadian corporations that own shares of a foreign corporation.

Issue: Analysis of major change in Canadian international tax policy announced in the Canadian government's March 2012 budget and enacted into law December 14, 2012.

On December 14, 2012, Bill C-45 received Royal Asset and was proclaimed into force. This legislation includes various amendments to the *Income Tax Act* (Canada) from the March 2012 federal budget, including the sweeping "foreign affiliate dumping" (FAD) rules applicable to any Canadian corporation that is (or becomes) controlled by a non-resident corporation. The FAD rules apply to treat virtually any "investment" made by a foreign-controlled Canadian corporation (Canco) relating to a foreign affiliate of Canco as a distribution made by Canco to its foreign parent: in effect, payments "down" the corporate chain by Canco (even value-for-value payments) are treated as if they were distributions "up" the chain by Canco to its foreign parent (either a deemed dividend or a return of share capital). An "investment" by Canco includes any acquisition of shares or debt of the foreign affiliate, any capital contribution to or conferral of a benefit on the foreign affiliate, certain "indirect" acquisitions of shares of the foreign affiliate, and certain other transactions. The FAD rules apply whether or not the transaction is arm's-length or intra-group, and whether or not the "investment" has any tax avoidance motive or generates any tax deductions in Canada.

The FAD rules represent a major shift in Canada's international tax policy. Careful consideration and planning is required to avoid the inadvertent application of these complex rules, which may result in double taxation in various instances. Multinational groups with a Canadian member that owns shares of a foreign corporation should be reviewing the potential impact of these rules, which apply to transactions occurring after March 28, 2012 (there is no grandfathering for existing foreign affiliates already in place beneath Canco). In certain cases planning and/or elections may mitigate the adverse impact of the FAD rules.

Steve Suarez of BLG's Tax Group has prepared a detailed analysis of the FAD rules, published in the December 17th edition of *Tax Notes International*, the world's leading international tax journal. This analysis sets out the operation of the FAD rules, describes the consequences of their application and illustrates the various ways in which they can go beyond their stated objectives, using decision trees and examples to create a non-technical user's guide to the FAD rules that can help those potentially affected navigate their way around them.

See **here** for Steve's article.

AUTHOR

Steve Suarez
Toronto
416.367.6702
ssuarez@blg.com

TAX LAW GROUP

National Leader

Stephen J. Fyfe	Toronto	416.367.6650	sfyfe@blg.com

Regional Leaders

Rick Bennett	Vancouver	604.640.4105	rbennett@blg.com
Pamela L. Cross	Ottawa	613.787.3559	pcross@blg.com
Lindsay Holmes	Calgary	403.232.9605	lholmes@blg.com
Brian M. Schneiderman	Montréal	514.954.3120	bschneiderman@blg.com
Craig J. Webster	Toronto	416.367.6149	cwebster@blg.com

Borden Ladner Gervais

BORDEN LADNER GERVAIS
LAWYERS I PATENT & TRADE-MARK AGENTS

Calgary
Centennial Place, East Tower
1900, 520 – 3rd Ave S W
Calgary, AB, Canada T2P 0R3
T 403.232.9500
F 403.266.1395
blg.com

Toronto
Scotia Plaza, 40 King St W
Toronto, ON, Canada M5H 3Y4
T 416.367.6000
F 416.367.6749
blg.com

Montréal
1000, rue De La Gauchetière Ouest
Suite 900
Montréal, QC, Canada H3B 5H4
Tél. 514.879.1212
Téléc. 514.954.1905
blg.com

Vancouver
1200 Waterfront Centre
200 Burrard St, P.O. Box 48600
Vancouver, BC, Canada V7X 1T2
T 604.687.5744
F 604.687.1415
blg.com

Ottawa
World Exchange Plaza
100 Queen St, Suite 1100
Ottawa, ON, Canada K1P 1J9
T 613.237.5160
F 613.230.8842 (Legal)
F 613.787.3558 (IP)
ipinfo@blg.com (IP)
blg.com

Waterloo Region
Waterloo City Centre
100 Regina St S, Suite 220
Waterloo, ON, Canada N2J 4P9
T 519.579.5600
F 519.579.2725
F 519.741.9149 (IP)
blg.com