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SUBJECT: INCOME TAX ACT
Meaning of Arm's Length

REFERENCE: Section 251 (and section 252)

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Explanation of Changes

Application

This bulletin cancels and replaces IT-419R dated August 24, 1995. The effective date of a particular legislative provision discussed in the bulletin may be indicated in the *Explanation of Changes* section (or, in some cases, in the *Discussion and Interpretation* section) of the bulletin. However, where the bulletin is silent with respect to the effective date of a particular provision, such date can be obtained from the legislation itself. Unless otherwise stated, all statutory references throughout the bulletin are to the *Income Tax Act* (the Act).

Summary

This bulletin discusses the criteria used to determine whether or not persons deal with each other at arm's length under the Act. Although the term "at arm's length" is used throughout

the Act, the Act does not contain any precise definition of the term. Section 251, which is the statutory provision for determining arm's length relationships, refers to three categories of persons. This bulletin deals with each category separately. The first category of persons is "related persons", the second category involves personal trusts and their beneficiaries, while the third category includes "persons not related to each other". Persons described in the second and third categories are referred to as "unrelated persons" in this bulletin.

Discussion and Interpretation

RELATED PERSONS

¶ 1. Paragraph 251(1)(a) deems that related persons do not deal with each other at arm's length. This is the case regardless of how they actually conduct their mutual business transactions. Subsection 251(2) defines related persons for the purposes of the Act. Subsections 251(3) to 251(6) clarify and expand on the definitions in subsection 251(2).

Related Individuals

¶ 2. According to paragraph 251(2)(a), individuals connected by blood relationship, marriage, common-law partnership (see ¶ 7) or adoption are related persons.

Blood relationship

¶ 3. Paragraph 251(6)(a) refers to a blood relationship as being that of a parent and a child (or other descendant, such as a grandchild or a great-grandchild) or that of a brother and a sister. Section 252 extends the meaning of those terms to encompass other individuals who might otherwise not be considered to fit the normal use of the term.

¶ 4. In addition to a natural child and an adopted child, subsection 252(1) provides that a child of an individual includes:

- (a) a person who is wholly dependant on that individual for support if the person is or was, before reaching 19 years of age, in law or in fact, under the individual's custody and control;
- (b) a child of the individual's spouse, (e.g., a stepchild) or common-law partner (see ¶ 7); and
- (c) a spouse or common-law partner of the individual's child, e.g., a son-in-law or a daughter-in-law, as well as the spouse or common-law partner of a stepchild, of an adopted child or of an individual considered to be the taxpayer's child as described in (a) above.

On the divorce of an individual's child (whether a natural child, an adopted child, a stepchild, or an individual considered to be a child by reason of paragraph (a) above), the child's former spouse ceases to be the child's spouse and is no longer a child of the individual.

¶ 5. Paragraph 252(2)(b) provides that an individual's "brother" includes the brother of the individual's spouse or common-law partner and the spouse or common-law partner of the individual's sister. It does not include the spouse or common-law partner of the sister or of the brother of the individual's spouse or common-law partner. Similarly, paragraph 252(2)(c) provides that an individual's "sister" includes the sister of the individual's spouse or common-law partner and the spouse or common-law partner of the individual's brother. It does not include the spouse or common-law partner of the brother or sister of the individual's spouse or common-law partner. Therefore, if Mr. A and Mr. B are otherwise unrelated, and they have each married one of two sisters, they are not related by blood according to paragraph 251(6)(a). Similarly, if Mr. X and Mrs. Y are brother and sister, Mrs. X and Mr. Y are not related by blood. However, Mr. A and Mr. B, and Mrs. X and Mr. Y, in the respective examples, are connected by marriage according to paragraph 251(6)(b).

Marriage

¶ 6. According to paragraph 251(6)(b), two persons are "connected by marriage" if one person is married to the other person or to an individual who is connected by blood relationship to that other person. For example, an individual will be connected by marriage to the parents and any siblings of the individual's spouse. However, where an individual's marriage is dissolved by either divorce or the death of the individual's spouse, the individual will cease to be "connected by marriage" or to be "connected by blood relationship" to the parents and any siblings of the individual's former spouse.

Common-law partnership

¶ 7. Paragraph 251(6)(b.1) provides that two individuals are "connected by common-law partnership" if one individual is in a common-law partnership with the other or with a person who is connected by blood relationship to that other person. Subsection 248(1) defines a common-law partnership as the relationship between two persons who are common-law partners of each other. The expression "common-law partner" is also defined in subsection 248(1) and means a person of the opposite or same sex who, at that time, lives with and has a conjugal relationship with the individual. In addition, one of the following conditions must be satisfied:

- (a) the person has been living in a conjugal relationship with the individual for a continuous period of at least one year; or
- (b) the person is the natural or adoptive parent (whether legally or in fact) of the individual's child (see ¶ 4).

Where an individual and another person have been living together in a conjugal relationship, they will be considered, at any time thereafter, to be living together in a conjugal relationship unless the couple have been living apart for a period of at least 90 days that includes the particular time

because of a breakdown of their conjugal relationship. Once a common-law partnership has been established, it will continue to exist unless the parties are living apart and have been doing so for a continuous period of 90 days due to a breakdown in the relationship. For example, Ms X and Mr. Y have been living together in a conjugal relationship beginning in 1997. On January 15, 2001, they begin to live separate and apart as a result of a breakdown in their relationship. On June 30, 2002, they reconcile and resume living together in a conjugal relationship. Ms X and Mr. Y will be common-law partners beginning June 30, 2002 because they have previously lived together in a conjugal relationship for a continuous period of one year.

Note 1: On December 20, 2002, the Minister of Finance released Legislative Proposals and Explanatory Notes Relating to Income Tax, a package of draft technical amendments to the Income Tax Act. One of the proposals is to amend the definition of “common-law partner” in subsection 248(1) to provide that an individual will be considered a common-law partner of another person at a particular time only where they have lived together in a conjugal relationship throughout the 12-month period that ends at the particular time. In the example referred to above, this would have the effect that Ms X and Mr. Y will not be considered common-law partners until June 30, 2003. If enacted as proposed, this amendment will apply for the 2001 and subsequent taxation years.

¶ 8. In determining whether an individual is a parent of their partner’s child, paragraph (b) of the definition of “common-law partner” does not restrict such a determination to the natural child of the partner. Consequently, subsection 252(1) characterizes each individual as a parent of a child when there is a legal or factual adoption of that child. When the facts substantiate that an individual is the adoptive (see ¶ 10) parent of the child of an individual with whom the individual is living together in a conjugal relationship, both individuals would be considered to be the parents of the child and a common-law partnership will be considered to have begun at that time, which could be at the time that the couple began to live together conjugally, or it could be after that time.

For the purposes of paragraph (b) of the definition of “common-law partner”, a child does not generally include a son-in-law or a daughter-in-law. Therefore, for example, a woman who begins to live together in a conjugal relationship with her son-in-law’s father would not be the common law partner of her son-in-law’s father until they have lived together for a continuous 12-month period.

Other relatives

¶ 9. For purposes of the Act, an individual’s niece, nephew, aunt, or uncle is not related by blood, marriage, common-law partnership or adoption to the individual unless such person is also the individual’s child or parent because of the extended meaning of child as described in ¶ 4. Cousins are not related by blood unless one is the child of the other

because of the extended meaning of child (as described in ¶ 4), or is the spouse or common-law partner of the other one’s brother or sister. However, under certain circumstances, cousins may be related by marriage, common-law partnership, or adoption.

Adoption

¶ 10. According to paragraph 251(6)(c), two individuals are “connected by adoption” if one individual is the adopted child of the other. “Adoption” includes a legal adoption and an adoption in fact. In addition, an individual who is related by blood (except a brother or sister) to another individual will be related by adoption to that person’s adopted child. Therefore, individuals are connected by adoption to their adoptive children, parents and grandparents. Whether a factual adoption has occurred at a particular time is a question of fact and has to be determined based on a consideration of the particular circumstances. The fact that an individual is appointed guardian of a child does not, in and of itself, constitute adoption in fact. For a de facto adoption to exist, generally the “adoptive” parent must exercise parental care and guidance on a continuing basis. The factors to look for in determining whether a certain relationship between an individual person and a child constitutes an adoption in fact are actual control and custody, an exercise of parental care and responsibility on a continuing basis, dependency, and proximity to each other.

Corporations and Other Persons

¶ 11. Paragraphs 251(2)(b) and (c) set out the statutory rules for determining when a corporation and another person will be considered to be “related persons” (or persons related to each other) for purposes of the Act. Under paragraph 251(2)(b), a corporation will be related to another person (including another corporation) where:

- (a) that person controls the corporation;
- (b) that person is a member of a related group that controls the corporation; or
- (c) that person is a person who is related to a person described in (a) or (b) above.

In addition, paragraph 251(2)(c) provides that two corporations will be related if:

- (i) the two corporations are controlled by the same person or group of persons;
- (ii) each of the corporations is controlled by one person and the person who controls one corporation is related to the person who controls the other corporation;
- (iii) one of the corporations is controlled by one person and that person is related to any member of a related group that controls the other corporation;
- (iv) one of the corporations is controlled by one person and that person is related to each member

of an unrelated group that controls the other corporation (see Example 1 below);

- (v) any member of a related group that controls one of the corporations is related to each member of an unrelated group that controls the other corporation (see Example 2 below); or
- (vi) each member of an unrelated group that controls one of the corporations is related to at least one member of an unrelated group that controls the other corporation (see Example 3 below).

For the purposes of subsection 251(2), control means *de jure* control, which generally means the right of control that rests in ownership of such number of shares as carries with it the right to a majority of the votes in the election of the board of directors of the corporation. For a detailed discussion of *de jure* control of a corporation, see the current version of IT-64, *Corporations: Association and Control*.

Example 1

A has two adult children, C and D. C has two children, X and Y, and D has one child, Z. A owns all of the issued and outstanding shares of Aco, consequently, A controls Aco. Each of Y and Z owns 50% of the common shares of Opc. Since Y and Z are cousins, they will, for purposes of the Act, be an unrelated group that controls Opc. As A is related to each of Y and Z (i.e. A is their grandparent), Aco and Opc will be related pursuant to subparagraph 251(2)(c)(iv).

Example 2

Same facts as in Example 1, except that each of A, C and D owns 33 1/3% of the common shares of Bco. A, C and D are a related group that controls Bco. Since A is related to each of Y and Z (i.e. A is their grandparent), Bco and Opc will be related pursuant to subparagraph 251(2)(c)(v).

Example 3

Mr. X, Mr. Y and Mr. Z are an unrelated group that controls XYZ Co. Their spouses, Mrs. X, Mrs. Y and Mrs. Z are an unrelated group that controls ZYX Co. As Mr. X is related to Mrs. X, Mr. Y is related to Mrs. Y and Mr. Z is related to Mrs. Z, XYZ Co will be related to ZYX Co pursuant to subparagraph 251(2)(c)(vi).

¶12. The expression “related group” is defined in subsection 251(4) and means a group of persons each member of which is related to every other member of the group. For example, a group consisting of two common-law partners and their children would be a related group. An unrelated group refers to a group of persons that is not a related group. For a group of unrelated persons to constitute a group of persons which controls a corporation, there must be a common link or interest between the persons (which must involve more than their mere status as shareholders) or there must be evidence that those shareholders act together to exert control over the corporation. In the case of a closely-held corporation (i.e. where there are two or three unrelated

shareholders, none of which individually controls the corporation) the CRA considers that there is a presumption that the shareholders of such a closely-held corporation will act together to control the corporation. In order to rebut this presumption, it would be necessary to show that no one is controlling the corporation and that the decision-making process in the corporation is effectively deadlocked.

¶13. Subsection 251(3) provides that where two corporations are each related to a third corporation, they will be considered to be related to each other for the purposes of subsections 251(1) and (2). For example, A and B are sisters and each has an adult child, being C and D, respectively. Each of A, B, C and D owns all of the issued shares of a corporation, Aco, Bco, Cco and Dco, respectively. In this situation, Aco and Bco are related to each other by virtue of subparagraph 251(2)(c)(ii). Also, Aco and Cco are related to each other and Bco and Dco are related to each other by virtue of subparagraph 251(2)(c)(ii). Therefore, Aco and Dco will be related to each other by virtue of subsection 251(3) because each of them is related to Bco. Similarly, Bco and Cco will be related under subsection 251(3) because each of them is related to Aco. However, since subsection 251(3) does not apply for the purposes of a subsequent application of subsection 251(3), Cco will not be related to Dco.

Special Rules

¶14. The provisions of paragraphs 251(5)(a), (b), and (c) apply in the determination of control of a corporation for the purposes of identifying related persons within the meaning assigned by subsection 251(2) and for the purpose of the definition of a Canadian-controlled private corporation in subsection 125(7). When a related group is in a position to control a corporation, paragraph 251(5)(a) deems the corporation to be controlled by the related group even though it may be part of a larger group that in fact controls the corporation. In determining whether two corporations are related, paragraph 251(5)(c) provides that a person who owns shares of more than one corporation shall be deemed, as shareholder of the corporations to be related to himself, herself, or itself.

Options and Rights

Effect of option

¶15. Paragraph 251(5)(b) deems a person to be in the same position, relative to the control of a corporation when, under a contract, in equity or otherwise, that person has the right:

- (a) to acquire shares (or control voting rights of shares) as if that person actually owned the shares;
- (b) to cause the corporation to redeem, acquire, or cancel any shares of its capital stock owned by other shareholders as if the shares were redeemed, acquired, or cancelled by the corporation;
- (c) to (or to acquire or control) voting rights of a corporation’s shares as if that person could exercise those voting rights at that time; or

- (d) to cause the reduction of voting rights of a corporation's shares owned by other shareholders as if the voting rights were reduced at that time.

However, the provisions of paragraph 251(5)(b) will not apply to the extent that one or more of the rights described above is not exercisable at that time because the exercise of the right is contingent on:

- the death,
 - the bankruptcy, or
 - permanent disability,
- of an individual.

Convertible securities

¶ 16. If bonds, debentures or non-voting shares of a corporation are convertible into voting shares, paragraph 251(5)(b) may apply because of the “right” of the owners of those securities to make the conversion. However, whether it will be applicable can depend upon the distribution of such convertible securities. If such securities have been issued to the general public and have wide distribution, they may usually be ignored since it is unlikely that the exercise of such rights will result in any person or group of persons acquiring control of the corporation as a result of the conversion of such securities. However, if large numbers of such securities are concentrated in the hands of a small group of people, their impact will need to be considered. A similar situation can exist, also, when a person has a right in some other form to subscribe for voting shares of a corporation.

Buy-sell agreements

¶ 17. Although the wording in paragraph 251(5)(b) may be broad enough to include almost any buy-sell agreement, this paragraph will not normally be applied solely because of:

- (a) a “right of first refusal”; or
- (b) a “shotgun arrangement” (i.e. an arrangement under which a shareholder offers to purchase the shares of another shareholder and the other shareholder must either accept the offer or purchase the shares owned by the offering party)

contained in a shareholder agreement.

Simultaneous control and deemed control

18. If paragraph 251(5)(b) does apply, it is possible for each of two unrelated persons to be regarded, for the purposes of subsection 251(2), as having control of the same corporation at the same time. For example, one person could have control by means of direct ownership of shares and the other could have control as a result of the application of one of the rules in paragraph 251(5)(b). This provision prevents a person who really controls a corporation from giving the appearance of divesting control by “selling” the controlling shares to some other person while retaining an option to repurchase them.

Paragraph 251(5)(b) does not deny that actual control is held by the person who holds it. If it did so, it would be possible

for a person or other entity which controls a corporation to give the appearance of divesting itself of control by giving to some other person an option that will never be exercised.

Example

S owns a majority of the voting shares in each of Corporations A and B and, therefore, has actual control of Corporations A and B.

J, who controls Corporation C, has an option to purchase from S or from S's estate, the controlling shares in Corporation A.

S and J are not related.

In these circumstances, paragraph 251(5)(b) deems J to have control of Corporation A, but does not deny that S has the actual control of it.

As a result:

- Corporations A and B are related (see subparagraph 251(2)(c)(i)) and are deemed not to deal with each other at arm's length (see paragraph 251(1)(a));
- Corporations A and B are each related to S (see subparagraph 251(2)(b)(i)) and are deemed not to deal with S at arm's length (see paragraph 251(1)(a));
- Corporations A and C are related (see subparagraph 251(2)(c)(i)) and are deemed not to deal with each other at arm's length (see paragraph 251(1)(a));
- Corporations A and C are each related to J (see subparagraph 251(2)(b)(i)) and are deemed not to deal with J at arm's length (see paragraph 251(1)(a)); and
- Corporations B and C are related (see subsection 251(3)) and are deemed not to deal with each other at arm's length (see paragraph 251(1)(a)).

If, however, J's option had been exercisable only after the death, bankruptcy or permanent disability of S, J would not be deemed to have control of Corporation A, because of the exceptions in paragraph 251(5)(b), in which case Corporations A and B would not be related to Corporation C and J would not be related to Corporation A.

UNRELATED PERSONS

Personal Trusts

¶ 19. Paragraph 251(1)(b) provides that a taxpayer and a specified personal trust (see ¶ 20) will be deemed not to deal with each other at arm's length if the taxpayer, or any person not dealing at arm's length with the taxpayer, is beneficially interested in the trust. Pursuant to subsection 248(25), a person who is beneficially interested in a trust includes:

- a person who has any right (whether immediate or future, whether absolute or contingent or whether conditional on or subject to the exercise of any discretion by any person or partnership) as a beneficiary to receive any of the income or capital of the trust either directly from the trust or indirectly through one or more trusts or partnerships;

- a particular person or partnership who is not otherwise beneficially interested in a trust at a particular time but may, by reason of the exercise of discretion by any person or partnership, subsequently become beneficially interested in the trust where any property has been acquired, directly or indirectly in any manner, by the trust from the particular person or partnership;
- a member of a partnership that is beneficially interested in the trust.

The following are examples of situations where an individual is beneficially interested in a trust:

- trust income is payable to the individual;
- income is held in trust and will be paid upon the individual's attainment of a certain age;
- the individual is one for whom a preferred beneficiary election may be made;
- the individual is one of a class who has a remainder interest under the trust;
- the individual has contributed property to the trust (e.g. the settlor of the trust) and may, by virtue of the existence of a power of appointment, be added as a beneficiary of the trust at a later date.

The individual is beneficially interested in the trust in (b) even if the individual's right to receive income ceases if the individual should die before attaining the specified age. Similarly, the individual is beneficially interested in the trust in (c) even if the trustees have full discretionary powers concerning the distribution of the capital or income of the trust so that the individual may in fact receive nothing from the trust.

¶ 20. A personal trust, as defined in subsection 248(1), is either a testamentary trust or an *inter vivos* trust in which no beneficial interest was acquired for consideration payable to the trust or to a person who has made a contribution to the trust. Subsection 108(7) provides that a person (or two or more persons who are considered to be related for the purposes of that subsection) may make a contribution of property to a trust and retain an interest in the trust without causing the trust to lose its status as a personal trust. A specified personal trust as used in ¶ 19 is a personal trust other than an amateur athlete trust, an employee trust, a master trust, a trust governed by a deferred profit sharing plan, an employee benefit plan, an employees profit sharing plan, a foreign retirement arrangement, a registered education savings plan, a registered pension plan, a registered retirement income fund, a registered retirement savings plan or a registered supplementary unemployment benefit plan, a related segregated fund trust, a retirement compensation arrangement trust, a trust whose direct beneficiaries are one of the aforementioned trusts, a health and welfare trust, a trust governed by an eligible funeral arrangement or a cemetery care trust, and a communal organization.

¶ 21. Pursuant to paragraph 251(1)(b), property acquired by a person (i.e. beneficiary) as a consequence of the death of an individual and in accordance with the terms of the will of the

deceased will be acquired from a person with whom the beneficiary is not dealing at arm's length. In addition, paragraph 251(1)(b) will deem two or more specified personal trusts not to be dealing at arm's length where, among other things,

- the same person is a beneficiary of each trust; or
- a person who is a beneficiary of one trust does not deal at arm's length with a person who is a beneficiary of the other trust(s).

Other Unrelated Persons

¶ 22. Paragraph 251(1)(c) provides that, at a particular time, it is a question of fact whether unrelated persons (other than persons described in ¶s 19 and 20) are dealing with each other at arm's length. Sometimes unrelated persons may deal with each other at arm's length, sometimes they may not, depending on all the circumstances. By providing general criteria to determine whether there is an arm's length relationship between unrelated persons for a given transaction, it must be recognized that all-encompassing guidelines to cover every situation cannot be supplied. Each particular transaction or series of transactions must be examined on its own merits. The following paragraphs set forth the CRA's general guidelines with some specific comments about certain relationships.

¶ 23. The following criteria have generally been used by the courts in determining whether parties to a transaction are not dealing at "arm's length":

- was there a common mind which directs the bargaining for both parties to a transaction;
- were the parties to a transaction acting in concert without separate interests; and
- was there "de facto" control.

¶ 24. The courts have held that when one person (or a group of persons) is, in fact, the bargaining agent, or the mind by which the bargaining is directed, on behalf of both (or all) parties to a transaction, then the parties cannot be dealing at arm's length. The courts have expanded this principle to include the concept of "acting in concert" with respect to an element of common interest. Therefore, even when there are two distinct parties (or minds) to a transaction, but these parties act in a highly interdependent manner (in respect of a transaction of mutual interest), then it can be assumed that the parties are acting in concert and therefore are not dealing with each other at arm's length. When a common purpose exists, a transaction is not necessarily a non-arm's-length one when different interests (or independent parties) are also present. In this context, different interests are considered to exist when each party has an independent interest from the other parties to a transaction, notwithstanding the fact that each party may have the same purpose, such as economic gain.

¶ 25. The courts have also held, in certain cases, that excessive or constant advantage, authority or influence can constitute de facto control (i.e., effective without legal control). This situation can bring parties into a non-arm's length-relationship. It is important to note that this advantage need not be exercised to be a factor; the mere ability to do so is sufficient.

¶ 26. Failure to carry out a transaction at fair market value may be indicative of a non-arm's length transaction. However, such failure is not conclusive and, conversely, a transaction between unrelated persons at fair market value does not necessarily indicate an arm's length situation. The key factor is whether there are separate economic interests which reflect ordinary commercial dealing between parties acting in their separate interests. The situation where one party to a transaction is merely accommodating the other party in an attempt to obtain a certain tax result may be a situation where the parties are not dealing at arm's length because they do not have separate economic interests which reflect ordinary commercial dealings between parties acting in their own separate interests.

Partnerships

¶ 27. In circumstances where a partnership owns a majority of the issued voting shares of a corporation, the partnership will not be considered to deal at arm's length with the corporation. In situations when one partner is in a position to control a partnership, either through ownership of a controlling interest or through a mandate vested in that partner by the other partners, that partner is not considered to be dealing at arm's length with the partnership. However, when a partner is not in a position to control a partnership in which the partner has an interest, and that partner has little or no say in directing the operations of the partnership, it is generally recognized that the partner is dealing at arm's length with the partnership. Where a related group of partners owns a controlling interest in a partnership, each member of that related group will not be considered to deal at arm's length with the partnership.

¶ 28. As a general rule, it is presumed that partners, who are not related persons, deal with each other on an arm's-length basis in transactions outside of their partnership activity, although their partnership in business would be a factor to be considered in any other transaction between them.

Trusts

¶ 29. In the situation where a trust owns a majority of the voting shares of a corporation such that the trustees of the trust control the corporation, the trust and the corporation will be related persons by virtue of subparagraph 251(2)(b)(i) and will, pursuant to paragraph 251(1)(a) be considered not to be dealing at arm's length. Also, as discussed in ¶s 19 and 20, a specified personal trust will be deemed not to deal at

arm's length with its beneficiaries or with any person who does not deal at arm's length with any such beneficiary. In any other case, it is a question of fact whether or not a trust and a particular person or group of persons are dealing at arm's length.

¶ 30. Unless the facts indicate otherwise, a trust is considered not to be dealing at arm's length with its settlor; however, unless the settlor has maintained some degree of influence over the trustee this general presumption may be ignored when the trustee of the trust is a professional trustee, (e.g., a public trust company); or if property is settled on a trust and, as a result, the settlor has transferred all of the usual rights of ownership of the property, the settlor might be considered to deal at arm's length with the trust provided that the trustee of the trust is free of any influence exercised by the settlor. However, the CRA generally considers that a transfer of property from a deceased to the estate of the deceased or to a trust created by the will of the deceased is not an arm's length transaction.

¶ 31. According to subsection 104(2), a trust is deemed to be an individual in respect of trust property and, pursuant to the definition in subsection 248(1), an "individual" is a person. Therefore, in section 251, a reference to the word "person" includes a trust.

Shareholders and Corporations

¶ 32. If, by the rules in paragraph 251(2)(b), a shareholder does not control a corporation or is not otherwise related to the corporation, there is a general presumption that the shareholder deals at arm's length with the corporation in which the shareholder holds shares. However, if a sufficient number of minority shareholders act in concert in order to direct the affairs of a corporation, they may be considered not to be dealing at arm's length with the corporation. Acting in concert generally means a predetermined agreement to act in a certain manner. In a widely held corporation, the fact that a majority of shareholders vote collectively to take some business action will not, by itself, indicate that those shareholders are acting in concert and therefore not dealing at arm's length with each other and the corporation. Also, the direct management voice of any minority shareholder who holds an officer's position with a corporation may be relevant in assessing that shareholder's relationship with that corporation.

¶ 33. There may be situations when closely held private corporations (with, in some cases, intercorporate share ownership which is insufficient to create legal control) employ some of the same personnel, occupy the same premises, and to the public eye, appear to be one enterprise. In such situations, the corporations may be considered not to be dealing with each other on an arm's length basis.

Explanation of Changes

Introduction

The purpose of the *Explanation of Changes* is to give the reasons for the revisions to an interpretation bulletin. It outlines revisions that we have made as a result of changes to the law, as well as changes reflecting new or revised interpretations of the CRA.

Overview

We have revised this bulletin primarily to reflect amendments to the *Income Tax Act* enacted by: S.C. 1998, c. 19 (formerly Bill C-28), S.C. 2000, c. 12 (formerly Bill C-23) and S.C. 2001, c. 17 (formerly Bill C-22).

Legislative and Other Changes

The Summary has been revised to include a reference to personal trusts and their beneficiaries as a result of the amendments made to paragraph 251(1)(b) as enacted by S.C. 2001, c. 17, s. 192, applicable after December 23, 1998.

¶ 2 has been revised to include a reference to individuals connected by “common-law partnership” as a result of the amendment to paragraph 251(2)(a) enacted by S.C. 2000, c. 12, Sch. 2, s. 10, applicable after 2000.

Former ¶ 4 has been subdivided into two paragraphs, ¶s 4 and 5. ¶s 4 and 5 have also been revised to change the references to spouse to include a “common-law partner” effective after 2000.

¶ 6 (former ¶ 5) has been revised to delete the references to paragraphs 252(4)(a) and (b) which were repealed by S.C. 2000, c. 12, s. 141(2), applicable after 2000.

¶ 7 is a new paragraph which describes the new definitions of “common-law partner” and “common-law partnership” which were added to subsection 248(1) by S.C. 2000, c. 12, s. 139(2), applicable after 2000. It also describes a proposal to amend the definition of “common-law partner” in subsection 248(1) which is described in *Legislative Proposals and Explanatory Notes Relating to Income Tax*, a package of draft technical amendments to the *Income Tax Act* which was released by the Minister of Finance on December 20, 2002.

¶ 8 (former ¶s 6 and 7) have been revised to delete the references to paragraphs 252(4)(a) and (b) which were repealed and replaced by the definition of “common-law partner” in S.C. 2000, c. 12, applicable after 2000.

¶ 9 (former ¶ 8) has been revised to include references to “common-law partnership” and “common-law partner”.

¶ 10 (former ¶ 9) has been revised to provide additional comments on de facto adoption.

¶ 11 (former ¶ 10) has been expanded to include a discussion of when two corporations will be related by virtue of paragraph 251(2)(c).

¶ 12 is a new paragraph which discusses the meaning of the expressions “related group” and “unrelated group”.

¶ 13 is a new paragraph which discusses subsection 251(3) which deems two corporations to be related in certain circumstances.

Former ¶ 11 has been renumbered as ¶ 14.

¶ 15 (former ¶ 12) has been revised to reflect that the draft legislation referred to in the Note thereto has been enacted as S.C. 1998, c. 19, subsections 242(2) and (3), applicable after April 26, 1995.

¶ 16 is a new paragraph which discusses paragraph 251(5)(b) in the context of convertible securities. These comments have been added since the current version of IT-64 *Corporations: Association and Control*, which was referred to in former ¶ 13, no longer discusses paragraph 251(5)(b).

¶ 17 (former ¶ 13) has been revised to delete the reference to IT-64 *Corporations: Association and Control* which no longer discusses paragraph 251(5)(b).

¶ 18 is a new paragraph which discusses the simultaneous control which may occur where paragraph 251(5)(b) is applicable.

¶s 19, 20 and 21 are new paragraphs which discuss the amendment to paragraph 251(1)(b) as enacted by S.C. 2001, c. 17, s. 192, applicable after December 23, 1998. Amended paragraph 251(1)(b) deems certain personal trusts not to deal at arm’s length with any person who is beneficially interested in the trust or with persons who do not deal at arm’s length with such beneficiaries.

¶ 22 (former ¶ 15) has been amended to change the reference to former paragraph 251(1)(b) to paragraph 251(1)(c).

¶s 23, 24, 25 and 26 (former ¶s 16, 17, 18 and 19) have been renumbered.

¶s 27 and 28 (former ¶s 20 and 21) have been revised to include additional comments with respect to when a partnership will not be dealing at arm’s length with another person.

¶s 29 to 31 (former ¶s 22 and 23) have been revised as a consequence of the new deeming rule applicable to certain personal trusts.

¶s 32 and 33 (former ¶s 24 and 25) have been renumbered.

Throughout the bulletin we have revised some of the wording in order to improve readability without altering the substance.