exigible where the recipient corporation controls the payer corporation or owns more than 10 per cent of that corporation's voting shares having a fair market value of more than 10 per cent of the fair market value of all of the issued share capital. Where dividends are received from a non-Canadian company, other than a foreign affiliate, the dividend must be grossed-up for any tax that was withheld and the full amount included in income. A tax credit may then be claimed for the amount of foreign withholding tax. Where a dividend is received from a foreign affiliate the treatment depends on whether or not the affiliate has been engaged in an active commercial or industrial business and where such business was carried on.

A Canadian corporation pays tax at the general rate on non-dividend investment income earned by the corporation. In the case of a Canadian-controlled private corporation, however, a portion of the tax is refundable on the payment of sufficient taxable dividends to its shareholders.

There is a special provision which deems interest to have been received at a prescribed rate where a Canadian corporation loans money to a non-resident for a term longer than a year, unless the loan bears a reasonable rate of interest or is made to a controlled subsidiary corporation which uses the funds to earn business income. There is no similar exception for loans to non-resident parent corporations.

Capital Gains

One-half of realized capital gains is included in taxable income and is subject to tax in the usual way. There is no separate capital gains tax. In the case of a Canadian-controlled private corporation, however, the taxable portion of a capital gain is treated as investment income and is subject to the same refundable tax treatment that is available in respect of investment income. The non-taxable portion of a capital gain earned by a Canadian-controlled private corporation may be distributed, upon election, as a non-taxable dividend to shareholders.

Inventory

The Income Tax Act provides that individual items in inventory may be valued at the lower of cost or market value. Inventory includes the work in progress of a business that is a profession other than the professional practice of an accountant, dentist, lawyer, doctor, veterinarian or chiropractor. The first-in, first-out (FIFO) and most other established costing methods are acceptable to the taxation authorities, but the last-in, first-out (LIFO) method is not acceptable. An inventory allowance equal to three per cent of tangible moveable property included in the opening inventory of a company is deductible for tax purposes. This allowance is not subject to recapture.

Depreciation

Depreciation for tax purposes (Capital Cost Allowance) must usually be computed by the declining balance method at rates not in excess of the maximum prescribed for various broad classes of assets. In general, the costs of all assets that belong to a particular class are pooled together and a separate dollar balance is kept for each class. The cost of each additional asset acquired for the class will be added to the dollar balance of the class and, similarly, the balance will be reduced by the proceeds from the sale of any asset that formerly belonged to the class. If this process leaves a negative balance in a particular class at the end of the taxation year, that amount is brought into income. Except for classes for which a straight-line treatment is indicated, the basis to which the rates are applied is the net balance in the class at the end of the taxation year. A special rule provides that only 50 per cent of the normal capital cost allowance deduction is available in respect of the net additions to the balance of a class in a year.

The capital cost allowance rates range from 1 to 100 per cent, but the more common rates are 30 per cent for automobiles, trucks, computers, film, and certain mining and logging equipment, 20 per cent for machinery and equipment, and 5 per cent for buildings. Where depreciable assets are rented out to others, there is a general rule which denies capital cost allowance to the extent that it creates or increases a rental loss. In addition, for certain classes of depreciable capital assets used in specific activities, accelerated capital cost allowances may be claimed.

Interest Expense

Generally, any interest expense incurred in the process of earning business or property income or for the purchase of an income producing asset is fully deductible. However, where interest is payable by a corporation to a non-resident who, in conjunction with the other non-arm's length parties, owns 25 per cent or more of any class of the issued shares of the corporation, it will be disallowed to the extent that the indebtedness to the non-resident shareholder exceeds three times the equity of the corporation. Special rules are provided to calculate the equity of the corporation for this purpose.

Bad Debts

In the case of doubtful accounts receivable, a reasonable reserve may be claimed for those debts which are unlikely to be collected. Once a debt is known to be bad, it must be written off. Any recovery on a debt that has been written off is included in income in the year of receipt.

Losses

Non-capital losses for the 1983 and subsequent taxation