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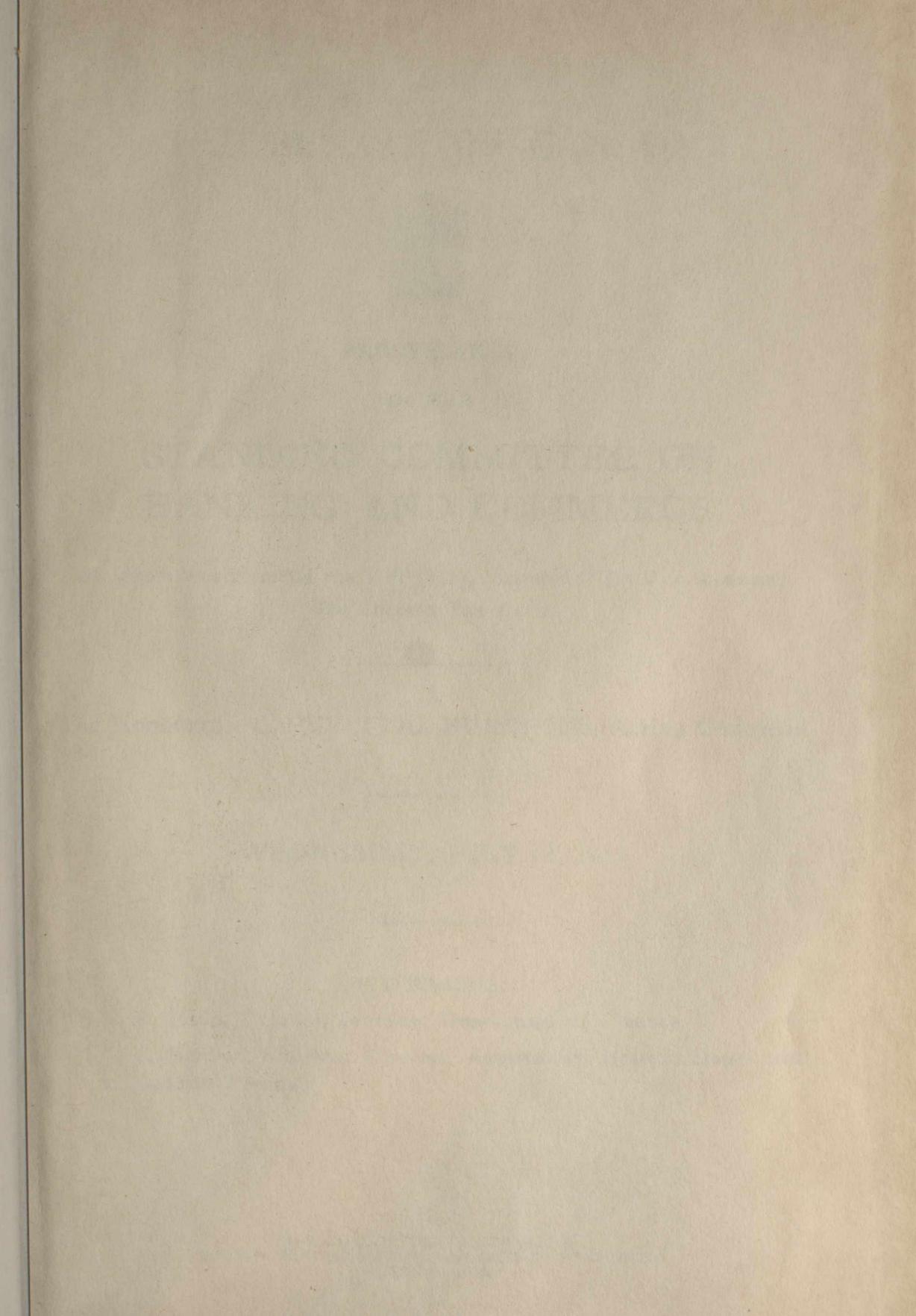
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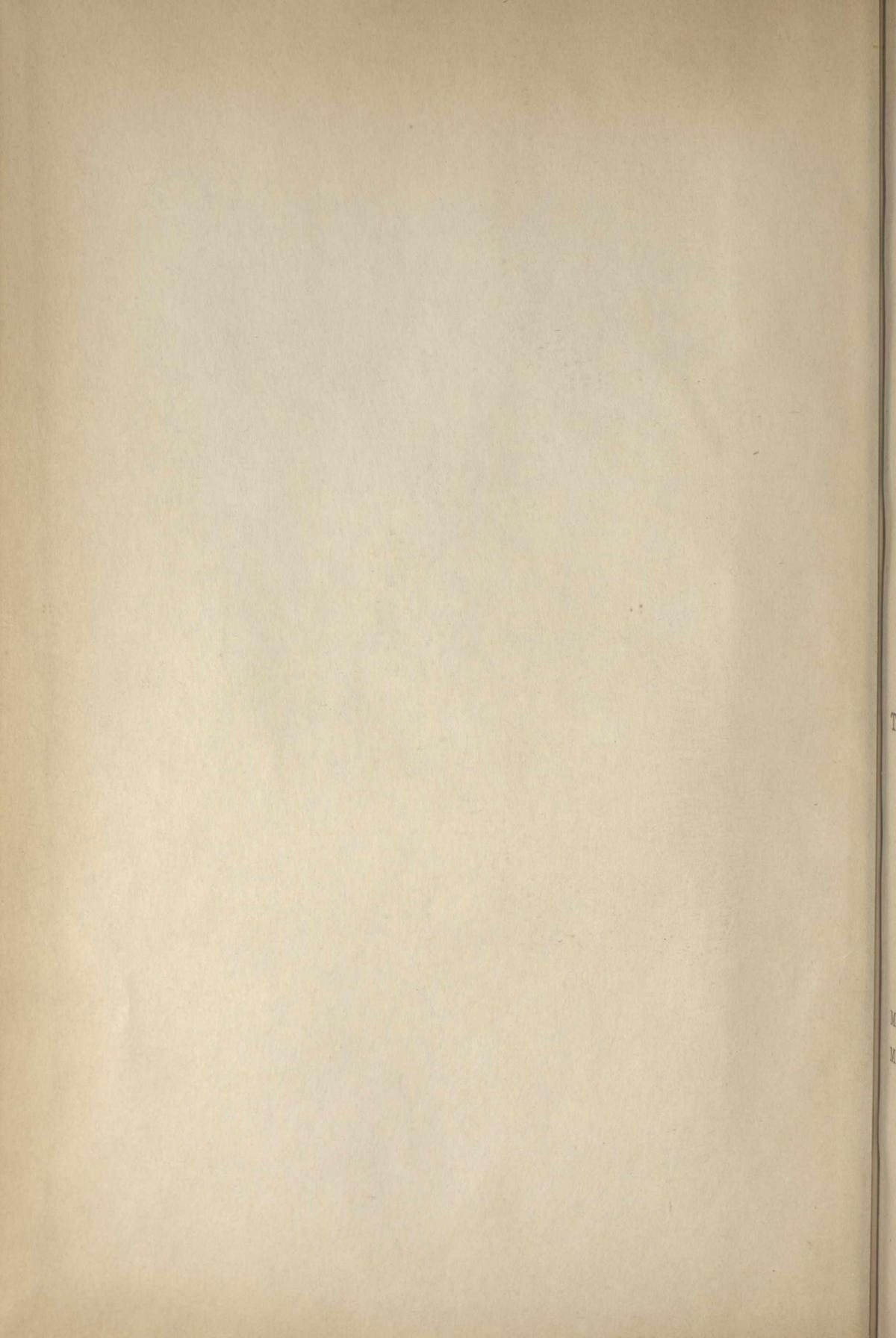
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1955

THE SENATE OF CANADA



PROCEEDINGS
OF THE
STANDING COMMITTEE ON
BANKING AND COMMERCE

To whom was referred the Bill (417), intituled: "An Act to amend
The Income Tax Act".

The Honourable G. PERCIVAL BURCHILL, Acting Chairman

WEDNESDAY, JULY 13, 1955

WITNESSES:

Mr. F. R. Irwin, Taxation Division, Department of Finance.

Mr. J. F. Harmer, Assistant Director, Assessments Branch, Department
of National Revenue.

EDMOND CLOUTIER, C.M.G., O.A., D.S.P.
QUEEN'S PRINTER AND CONTROLLER OF STATIONERY
OTTAWA, 1955.

BANKING AND COMMERCE

THE HONOURABLE SALTER A. HAYDEN, CHAIRMAN

THE HONOURABLE SENATORS

Aseltine	Hawkins	McLean
Baird	Hayden	Nicol
Beaubien	Horner	Paterson
Bouffard	Howard	Pirie
Burchill	Howden	Pratt
Campbell	Hugessen	Quinn
Crerar	King	Reid
Davies	Kinley	Roebuck
Dessureault	Lambert	Taylor
Euler	*Macdonald	Turgeon
Fallis	MacKinnon	Vaillancourt
Farris	McDonald	Vien
Gershaw	McGuire	Wilson
Gouin	McIntyre	Wood
*Haig	McKeen	Woodrow
Hardy		

**ex officio member.*

ORDER OF REFERENCE

Extract from the Minutes of Proceedings of the Senate for Thursday, 7th July, 1955.

“Pursuant to the Order of the Day, the Honourable Senator Connolly moved that the Bill (417), intituled: “An Act to amend the Income Tax Act”, be now read the second time.

After debate, and—

The question being put on the said motion, it was—
Resolved in the affirmative.

The said Bill was then read the second time, and—
Referred to the Standing Committee on Banking and Commerce”.

L. C. MOYER,
Clerk of the Senate.

WEDNESDAY, July 13th, 1955.

Pursuant to adjournment and notice the Standing Committee on Banking and Commerce met this day at 10.30 a.m.

Present: The Honourable Senators:—Aseltine, Beaubien, Bouffard Burchill, Campbell, Dessureault, Gershaw, Gouin, Howard, Hugessen, Kinley, Lambert, McLean, Pratt, Roebuck, Taylor, Turgeon and Woodrow—18.

In the absence of the Chairman the Honourable Senator Burchill was elected Acting Chairman.

In attendance: Mr. John F. MacNeill, Q.C., Law Clerk and Parliamentary Counsel, and the Official Reporters of the Senate.

Bill 417, an Act to amend the Income Tax Act, was read and considered clause by clause.

Mr. F. R. Irwin, Taxation Division, Department of Finance, and Mr. J. F. Harmer, Assistant Director, Assessments Branch, Department of National Revenue, were heard in explanation of the Bill.

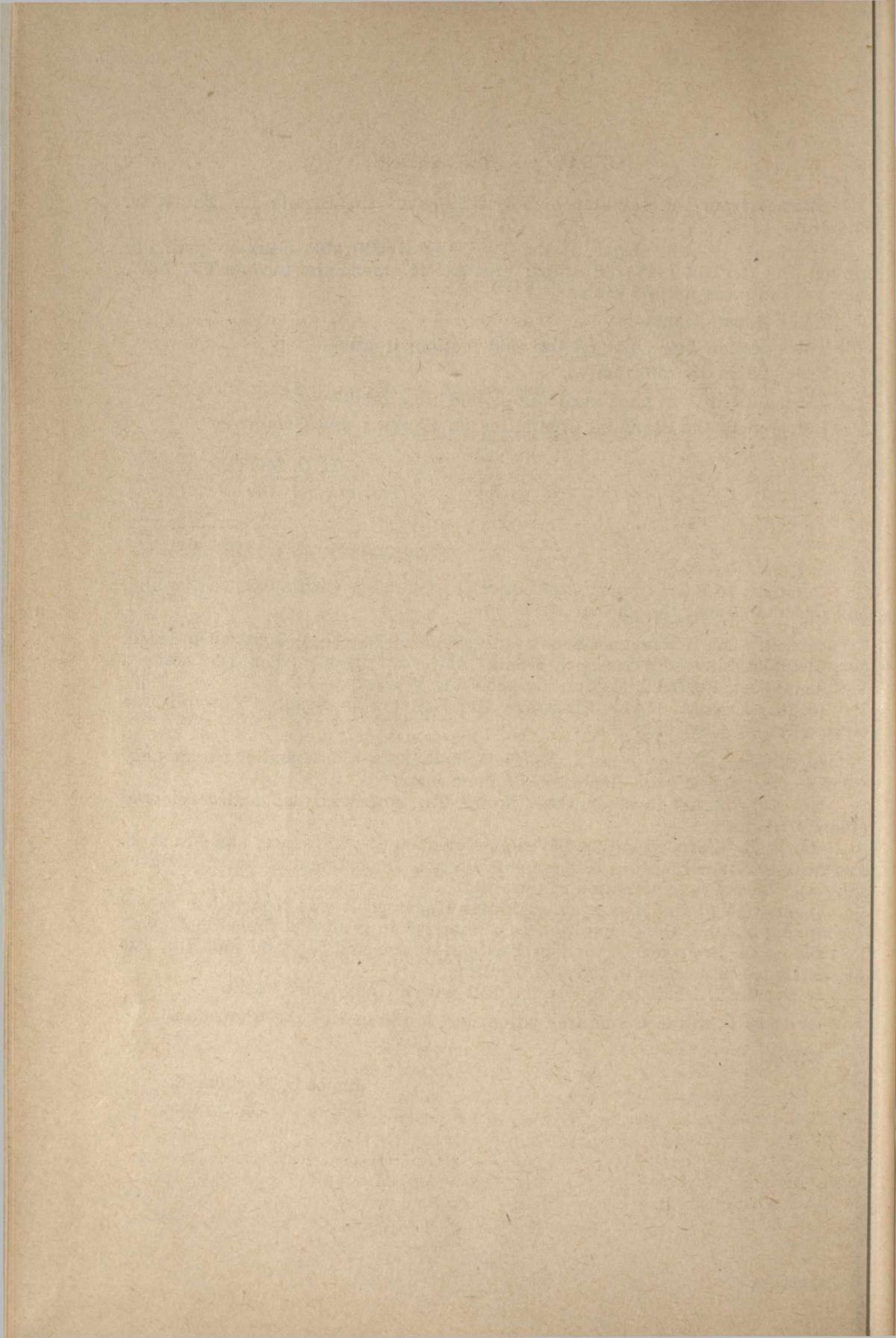
On motion of the Honourable Senator Hugessen it was resolved to report recommending that the Committee be authorized to print 500 copies in English and 200 copies in French of their proceedings on the said Bill, and that Rule 100 be suspended in relation to the said printing.

It was RESOLVED to report the Bill without any amendment.

At 12.30 P.M. the Committee adjourned to the call of the Chairman.

Attest.

James D. Macdonald,
Clerk of the Committee.



THE SENATE

STANDING COMMITTEE ON BANKING AND COMMERCE

OTTAWA, Wednesday, July 13, 1955

EVIDENCE

The Standing Committee on Banking and Commerce, to whom was referred Bill 417, an Act to amend the Income Tax Act, met this day at 10.30 a.m. Senator Burchill in the Chair.

The ACTING CHAIRMAN: Is it the wish of the committee that the proceedings of the committee on this bill be reported verbatim?

Senator HUGESSEN: I think it is usual to do so, Mr. Chairman. It would form a rather valuable record of the proceedings that have taken place, containing the explanations of the witnesses on certain sections and what is contended by them by the Income Tax Department.

The ACTING CHAIRMAN: We will need authority to print our proceedings. I think the usual number is 500 copies in English and 300 copies in French.

Senator HUGESSEN: I so move.

Carried.

The ACTING CHAIRMAN: Now, gentlemen, when moving second reading of the bill in the house Senator Connolly gave a very clear explanation of it. How does the committee wish to proceed now?

Senator GERSHAW: Clause by clause, I would suggest.

The ACTING CHAIRMAN: We have two officials with us this morning, Mr. F. R. Irwin, a Finance Officer of the Department of Finance, and Mr. J. F. Harmer, of the Department of National Revenue. Both Mr. Irwin and Mr. Harmer will please come forward and sit at the head table.

Mr. Irwin, have you anything to say in a general way, any opening remarks?

Mr. IRWIN: Mr. Chairman, this is the usual bill to amend the Income Tax Act. Every year it is a fairly large bill because of the number of representations pointing out matters which taxpayers feel need correcting and which the officials of the Department of National Revenue in their work have felt needed some change.

The Minister of Finance explained the bill very fully in committee of the whole House of Commons, and we have tried in the explanatory notes to explain each section in the bill. Perhaps the most important parts of the bill taxwise are the reductions in the rates, both for individuals and corporations.

The ACTING CHAIRMAN: Now, gentlemen, we will take up consideration of section 1—expense of issuing shares or borrowing money.

Senator HUGESSEN: There are two parts to this section. Subsection 1 deals with the expenses of persons issuing securities does it not? I gather what is intended to be covered there is that a corporation which issues shares or borrows money in the course of the year can deduct the expenses incurred in connection with the issue of shares or borrowing as an expense of the company during the year within which the issue of shares or borrowing was made, that is, it can deduct the cost of printing and engraving of stock certificates, legal fees

and all that sort of expense, but it cannot deduct commissions paid to underwriters or any expenses of that kind. Is that the meaning of the subsection?

Mr. HARMER: That is right, senator.

Senator BOUFFARD: When a corporation issues shares there is usually a broker involved, and his payment takes the form of a commission, and in that the broker includes most of the cost of advertising, the printing of prospectuses and, in fact, nearly all the expenses in connection with the issue, and if that commission is not deductible it means that most of the expenses for the issue of shares is not deductible. The broker pays income tax on the profit he makes out of that issue, though.

Mr. IRWIN: It was not felt that we could go so far as to allow a deduction of commissions.

Senator BOUFFARD: Could you not allow the deduction of the commission in so far as the expense of the broker is concerned?

Mr. HARMER: Those are allowable to the broker as deductions.

Senator BOUFFARD: But the company does not benefit. In the end the company pays for it.

Mr. HARMER: That is right.

Senator HUGESSEN: Would not that be allowed as an expense for the broker?

Senator BOUFFARD: It will be allowed as an expense of the broker, but the company pays for it, and the company has not any allowance for it.

Senator HUGESSEN: You cannot allow it twice,—both for the broker and the company.

Senator BOUFFARD: No, that is right. You cannot allow it twice—there is no doubt about that—but the company, which is the main party, that pays for the commission and for the expense, has not got any benefit out of it. The broker pays the tax, and takes it out of the commission, but the company, which pays for the expense and pays also for the issue, does not get any benefit. It seems to me that the company should at least have the benefit of the expense allowed for the broker, because it pays for it.

Senator CONNOLLY: It appears to me that the big item on this is the decision as to whether or not the commission which is payable by the company that issues the shares or the debentures or bonds should not be allowed as an expense to that company. It is in fact an expense.

Senator BOUFFARD: It is an expense for the full amount of the commission that it pays.

Senator CONNOLLY: However, that is the financial policy.

The Acting CHAIRMAN: Have you any comment to make on that?

Mr. IRWIN: No.

The Acting CHAIRMAN: Any further comment on section 1?

Senator HUGESSEN: No, that is all. As far as it goes, it is a very valuable concession.

Senator KINLEY: It depends on who pays the bonus or commission.

Senator BOUFFARD: It is not that I want to make an amendment to the bill. I do not think we can. But I wanted to express my opinion on that, so that the Department might look into the matter and see whether they could not find some formula by which the company could at least deduct the real expenses which are made for the issue. Although the expense of the printing of the prospectus, the advertising, and the sending of the prospectus to the clients, is made by the broker, the company pays for it. It may be that the Department, in a study

of this matter, might find some solution by which a company might benefit to a certain extent at least, on the expenses. That is the only purpose of my remarks.

The ACTING CHAIRMAN: Shall the section carry?

Some Hon. SENATORS: Carried.

Senator KINLEY: There is another part to this section.

The ACTING CHAIRMAN: I included both. Do you want to say something?

Senator KINLEY: "Where an approved superannuation fund or plan contains a provision under which the taxpayer may provide superannuation or pension benefits." How is that approved? By the statute?

Mr. HARMER: By the Minister of National Revenue.

Senator KINLEY: Suppose a man retires, and you do not have a pension plan, and a pension plan is established for \$25 a month or \$50 a month, would not that be an expense of your operation?

Mr. HARMER: Yes.

Senator ROEBUCK: What is the change from the previous arrangement? Previously the fund had to be approved and these payments into the fund by the manufacturer or other employer were exempt. What is the change?

Mr. HARMER: This change deals only with what is called terminal funding. Where ordinarily an employer has a pension fund or plan, he sets up year by year as the employee is employed a fund for providing a pension when the employee retires. But there are a few who do not do that as employment exists. They wait until the employee is ready to retire, at which time they then set up a fund to provide for his pension. There were certain conditions under which that second kind of employer could get a reduction in setting up a terminal funding plan for his employees' pensions. Those conditions in the present law were that he could only get a deduction if he paid such an amount at the time when the employee retired or at the time when he was eligible to retire even though he did not retire until some time later. There were certain cases in practice where employees wanted to cease their employment before that date occurred and become employees with somebody else. In those circumstances, in certain of these plans, he still had a right to a deferred pension which would become payable at the ordinary date of eligibility, and the law was faulty in that it did not allow the employer a deduction in respect of those kinds of payments.

Senator CONNOLLY: In other words, the payment can be made into the fund by the employer at the time of the severance of the employment by the employee?

Mr. HARMER: That is right.

Senator CONNOLLY: At the time an employee leaves his employment his terminal payment can now be made by the employer into the pension fund. Is this in relief of the employee?

Mr. HARMER: No, it is in relief of the employer.

Senator CONNOLLY: But there is a benefit conferred on the employee?

Senator HUGESSEN: No, it is on the employer. As I understand it, it extends the time in which the employer can make this terminal payment.

Mr. HARMER: Yes.

Senator HUGESSEN: It is really a benefit to the employer in respect to the date in which he can make his terminal payment.

Senator ROEBUCK: Does this make possible the benefit the garment makers have in Toronto where all manufacturers are in one association and employees can go from one employer to the other and take their retiring benefits with them?

Mr. HARMER: I am afraid I do not know that plan, sir. I do not think it would affect it.

Senator ROEBUCK: I know there was difficulty connected with that, and I was wondering if this was solving it.

The ACTING CHAIRMAN: Are there any other questions on this section, gentlemen?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 2—Insurance proceeds?

Senator GOUIN: I should like to start by asking a question with respect to the proceeds of a fire insurance policy. Supposing there is a fire on the second floor, say, of my house and it is completely destroyed and \$3,000 has been paid and received by me as the taxpayer. Are such proceeds taxable?

Mr. HARMER: No, they are not taxable, although they are said by the law to have to be included in income, but only for the purpose of offsetting the cost of repairing the damage to that second floor. But this amendment does not deal with that, because you have mentioned a case where there is only a partial loss of property. This is a case where there is complete destruction of a property, and the present law provides that in that case the whole insurance proceeds must come into income in the year of destruction, and if you rebuild the property in that same year no harm is done, because one offsets the other; but the trouble was that that was not always possible. Sometimes the fire happens right near the end of the year—you may have to bring in your whole insurance proceeds in that year and not rebuild till the next year, and therefore you had a big tax to pay one year, and something against it, but not till a year later. The only object of this is to give you that extra year after the fire in order to get that offset.

Senator ROEBUCK: If you do not rebuild within the two years do you pay tax on the insurance?

Mr. HARMER: Not necessarily, although it comes into your income, and if that is the only asset that you had in that particular class then it could be that part or all of those proceeds will end up as being taxable, but if there are other buildings, or whatever kind of property it is, in the same class of depreciable property, again it offsets the other. It just reduces your base for future depreciation of those properties.

Senator ROEBUCK: I do not see why it should ever become taxable because it is a capital asset.

Mr. HARMER: It is all part of the scheme of recapture of depreciation, senator.

Senator ROEBUCK: Oh, I understand.

Senator CONNOLLY: That is the question you asked me in the Senate the other day.

Senator ROEBUCK: Yes.

Senator ASELTINE: If I have a building destroyed by cyclone on my farm—which sometimes happens—and I have tornado insurance, and I collect that insurance, how much of that is taxable, just the undepreciated portion, or the whole amount of the insurance?

Mr. HARMER: Just the portion representing what you previously took in depreciation.

Senator ASELTINE: But if I rebuild that farm it is not treated as taxable income?

Mr. HARMER: No, the one again offsets the other. You bring in the whole cost of rebuilding the barn on one side, and bring in against that the insurance—

Senator ASELTINE: Is that expense charged to income—the building of that barn again?

Mr. HARMER: No, it is the cost of the depreciable property.

Senator ASELTINE: But I would be paying income tax on the insurance I have been paying and would only be allowed depreciation at the rate of 5 per cent a year.

Mr. HARMER: No, the one offsets the other. They are both put in the same account. The cost goes on one side, and the insurance on the other.

Senator BEAUBIEN: If I have a crop which is insured against hail, and my crop is damaged by a hail storm, either partially or whole, and then I get my insurance, is that taxable?

Mr. HARMER: That is right.

The ACTING CHAIRMAN: Any further questions on section 2? Then, does section 2 carry?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 3—Husband and wife.

Senator HUGESSEN: That is a relieving section, also, is it not?

Mr. HARMER: No, sir, not entirely. It is just a clarification.

Senator HUGESSEN: It is more than a clarification.

Mr. HARMER: Well, it is in law, but not as regards practice. I do not think it changes the practice from what it has been.

Senator HUGESSEN: It brings the Act in conformity with the practice?

Mr. HARMER: That is right.

Senator GOUIN: In the province of Quebec gifts can be made to a wife only by marriage contract, in trust. I don't object to the clause, but I don't think it changes anything.

Senator McLEAN: Has the taxpayer always been able to give away part of his taxable income to his family?

Mr. HARMER: No, not and escape taxation.

Senator McLEAN: But he is allowed up to \$4,000 as an amount which he may pass around among his family, is he not?

Mr. HARMER: He can make a gift up to \$4,000 without having to pay a gift tax, but if he makes a gift to a member of his family he still has to pay the tax on the income from the property so transferred.

Senator TURGEON: Does the exemption from income tax apply to gifts given outside the immediate family?

Mr. HARMER: Yes.

Senator TURGEON: That is, to distant relatives?

Mr. HARMER: Every gift of up to \$1,000 to any person, regardless of the relationship, is exempt; and in addition to that, a total of \$4,000 or half of the income after deduction of income tax, is exempt.

Senator McLEAN: That is, it is exempt from the gift tax?

Mr. HARMER: From the gift tax.

Senator McLEAN: Is this something new?

Mr. HARMER: No; this does not touch the gift tax.

Senator McLEAN: But is there not something new about the tax being paid by the giver?

Mr. HARMER: No; that has been in the law as far back as I can remember.

Senator McLEAN: Then why is it being put in again, just for clarification? I see it goes back as far as August 1, 1917.

Mr. HARMER: The only part that is new is that which is underlined in lines 11, 12 and 13.

Senator McLEAN: That is, "during the lifetime of the transferor while he is resident in Canada and the transferee is his spouse."

Mr. HARMER: Before this amendment the act inferred that if a transfer was made to a wife, the husband would remain taxable on the income from that property forever, even after the death of the transferor, or if he left the country, or if he was divorced. All this section says is that any of those three events shall put a stop to the effect of this section—that is, after his death, or after he has left Canada, or after he is divorced, the income from that property is no longer his income and becomes the income of his wife.

Senator BEAUBIEN: Before this section carries, I would like to get one point clear. If I want to give some money to my children, how much am I allowed to give? Is there any limit?

Mr. HARMER: No, there is no limit; but if you give more than \$1,000 to any of them, or a total of \$4,000 or half your income of the year before the gift, then you will have to pay a gift tax; and if your children are under nineteen years of age when you give the gift to them, you remain taxable on the income from that property until they reach that age.

Senator BEAUBIEN: I am not talking about property; suppose I give them cash.

Mr. HARMER: By "property" I mean cash, real estate, bonds, mortgages, or anything else.

Senator BEAUBIEN: In other words, I can give my children \$1,000 each, provided I have paid my income tax on the amounts that I have earned.

Mr. HARMER: Yes.

Senator BEAUBIEN: But would they have to pay taxes on what they get?

Mr. HARMER: You would have to pay taxes on the income from that \$1,000 until such time as they reach the age of nineteen years. After that they become taxable on the income.

Senator GOUIN: It is not necessary to pay tax twice.

Mr. HARMER: Just once.

Senator McLEAN: Are you not allowed anything for a wedding or a birthday gift?

Mr. HARMER: Not in the law.

Senator McLEAN: Even Customs will let you put such things through.

Senator BEAUBIEN: Supposing I give my children \$1,000 each, is the amount they get taxable? That is, do they pay tax on the amount they get from me?

Mr. HARMER: No, not on the \$1,000 they get from you, but if that \$1,000 is in such form as to produce income or profit, the tax is payable—

Senator BEAUBIEN: Suppose they squander it—I think probably they will.

Mr. HARMER: That is all right.

The Acting CHAIRMAN: Shall Section 3 carry?

Some Hon. SENATORS: Carried.

The Acting CHAIRMAN: Section 4—Transfers to Minors.

Senator McLEAN: That is the same as the previous section?

Mr. HARMER: Yes, section 4 relates to the children's part of that problem we were talking about, and section 3 deals with the wife.

Senator KINLEY: What is the significance of the words "during the lifetime of the taxpayer while he is resident in Canada"? Does it mean that if he ceases to be a resident of Canada this section does not apply?

Mr. HARMER: It ceases to apply to him.

The Acting CHAIRMAN: Shall Section 4 carry?

Some Hon. SENATORS: Carried.

The Acting CHAIRMAN: Section 5—Persons wholly dependent upon more than one taxpayer.

Senator ASELTINE: I would like an explanation on this section, Mr. Chairman. I do not see how it is going to be decided which of the group is going to claim the exemption.

Senator GOUIN: That is the way it appears to me.

Mr. HARMER: That is up to the group to decide amongst themselves, and if they cannot decide, no one gets it.

Senator ASELTINE: Do I understand that if they cannot decide, nobody gets the exemption?

Mr. HARMER: That is correct.

Senator ASELTINE: That does not seem fair to me.

Mr. HARMER: Would you put us in the position of having to arbitrate these family quarrels?

Senator GOUIN: If they can't agree, I would think that somebody should have the right to decide who should obtain the exemption.

Senator ASELTINE: I suppose that each one wants it.

Senator GOUIN: Yes.

Senator CONNOLLY: I wonder whether it could not be done in a practical way by paying each other off. Even if the department did not know it, I suppose in practice they could do that, and let one of them get the exemption.

Senator ASELTINE: I have known that to happen.

The Acting CHAIRMAN: Shall section 5 carry?

Some Hon. SENATORS: Carried.

Senator ASELTINE: On division.

The Acting CHAIRMAN: Section 6?

Senator CONNOLLY: There is something in section 6 about the removal of the surtax on rental income, but I suppose that is quite clear.

Senator HUGESSEN: That means, in effect, rental income from taxable property is no longer considered an investment income for the purpose of investment tax.

Senator ASELTINE: That is to say, if I have property on which I obtain a rental, I do not pay any surtax on that amount, provided it amounts to more than \$2,400 or the amount of my exemptions, whichever is the greater, is that right?

Mr. HARMER: Yes.

Senator KINLEY: That is a change.

Mr. HARMER: Yes, sir.

Senator KINLEY: And a good change.

The Acting CHAIRMAN: Shall Section 6 carry?

Some Hon. SENATORS: Carried.

The Acting CHAIRMAN: Section 7?

Senator CONNOLLY: I understand that section 7 simply implements the statement made in January by the Prime Minister in the House of Commons with reference to provincial income taxpayers, is that right?

Mr. IRWIN: That is correct.

Senator CONNOLLY: There was a question raised in the Senate the other day as to the availability of this section in provinces other than Quebec. I understand that this section would be available to any taxpayer in Canada, no matter where he lived, if he had to pay a provincial income tax. Is that correct?

Mr. IRWIN: That is correct, although it should be pointed out that this section is only made applicable for two years, for 1955 and 1956, and during those two years the remaining provinces have agreed under the tax rental agreements not to impose personal income taxes.

Senator CAMPBELL: But that is not the point Senator Connolly was asking about. Suppose a person resident in the province of Ontario and that part of his income derived in the province of Quebec, from which there is a deduction at the source of a tax payable to the province of Quebec, what deductions, if any, can he make from his Dominion income tax in respect of the tax payable in Quebec?

Mr. IRWIN: That is covered in the subsection. If he has a proportion of his income from the province of Quebec he can deduct from his federal tax the proportion which is the same as the proportion of his income in Quebec to his total income. There are various rules spelled out in this section to cover that situation.

Senator CONNOLLY: And is the proportion this way: the relation that his Quebec income tax bears to his total income tax, and that much up to 10 per cent?

Mr. IRWIN: That is the general rule.

Senator CONNOLLY: For 1955 and 1956 anyway.

Mr. IRWIN: Yes.

Are there any further questions on section 7?

Shall the section carry?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: We will now take up section 8. Are there any questions?

Senator ASELTINE: Could we have an explanation of section 8?

Mr. IRWIN: The first part of this section deals with employees profit-sharing plans. The general scheme of the law is that amounts allocated under a profit-sharing plan should be taxable to the employee in the year allocated and not taxable in the year in which he withdraws the proceeds from the plan. In some cases when proceeds are withdrawn from a plan a certain proportion of these proceeds may not have been subject to tax in previous years when allocated, and would then become taxable in the year in which he withdraws his proceeds from the plan, and this might be a very substantial sum. Now, part of this section provides a means of alleviating the tax on that lump sum by giving it the same treatment as lump sum withdrawals from approved pension plans.

Senator CONNOLLY: The special tax that is applied in a case like that, I understand, is the average tax that he paid on his normal income for the previous three years.

Mr. IRWIN: That is right.

Senator CONNOLLY: Now just one more question that arose in my mind in that connection. That amount is taxable as an independent unit and then the rest of the normal income is taxed at the usual graduated rate, I suppose. In other words, there is a special tax applied to that, and the rest of his income for the year in question is taxed at the graduated rates in the normal way.

Mr. IRWIN: That is right.

Senator HUGESSEN: In other words, he would be deemed to have received these amounts, and would be taxed on them at this special rate, but they would not be added to his ordinary income for tax purposes in the year in question.

Mr. IRWIN: If the taxpayer elects to be taxed in that way.

Senator KINLEY: Is there any industry or co-operative in Canada which is exempt from tax on their profit-sharing plans? Are there any co-operatives exempt from paying taxes on plans of that nature?

Mr. IRWIN: No; the law is not drawn up in terms of particular industries, it refers to profit-sharing plans.

Senator KINLEY: Are any co-operatives exempt, or any industry exempt in this regard, such as profit-sharing plans in the grain industry and others? Are they all taxed now?

Mr. IRWIN: I do not think what you have in mind would fall in line with employees profit-sharing plans.

Senator KINLEY: I thought that we were moving up to the point where we were going to tax them all? I thought we were closing it up by degrees. Is that happening?

Mr. HARMER: Well, co-operatives are treated specially in the act, but they are not under this profit-sharing arrangement. This has really nothing to do with them. They are treated, you may say, the same as any other corporation in that they can deduct, as any other corporation can, the patronage dividends they pay out to their members. A co-operative, as in the case of any other corporation, can deduct in computing its income the amount it pays out.

Senator KINLEY: And profit-sharing?

Mr. HARMER: No, we call it patronage dividends. They cannot, however, pay out dividends that would reduce their income below 3 per cent of their capital employed.

Senator KINLEY: But this gives a little better advantage to the average taxpayer in that he can take a three-year average instead of just taking the single year.

Mr. HARMER: That is the object of this.

The ACTING CHAIRMAN: Is everybody clear on that?

There is a subsection 2, Mr. Irwin, in connection with retirement. Do you want to say a word on that too?

Mr. IRWIN: This subsection 2 adds the underlined words "if made in the year of retirement or within one year after that year". These paragraphs are part of the section to which Senator Connolly has just referred, providing a lower rate of tax when a lump sum is received. This lower rate of tax applies in several circumstances including retirement or death benefits, and previously there was no requirement that these lump sum payments had to be received within a limited time in order to qualify for this tax abatement, which is, essentially, an abatement of lump sum payments. It is now provided these

lump sum payments must be received within a year of retirement or one year after if they are going to qualify for this tax abatement.

The ACTING CHAIRMAN: Shall section 8 carry?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 9—Associated corporations.

Senator ASELTINE: I take it this section means that a small company with a taxable income of less than \$20,000 gets no relief.

Mr. IRWIN: That is correct.

Senator ASELTINE: It just applies to companies which have an income of more than \$20,000; and their tax is reduced by 2 per cent?

Mr. IRWIN: Two percentage points.

Mr. HARMER: On an income over \$20,000. They also do not receive any benefit on the income up to \$20,000.

Senator KINLEY: They all receive benefit up to \$20,000?

Mr. IRWIN: They have previously received that, but not under this bill.

Senator KINLEY: What does this do?

Mr. IRWIN: This reduces the rate on an income over \$20,000 by two percentage points.

Senator KINLEY: But does it affect the rate up to \$20,000?

Mr. IRWIN: No, sir.

Senator KINLEY: Fifteen per cent up to \$20,000.

Mr. HARMER: 20 per cent now.

Senator KINLEY: And after that you go into the big bracket.

Mr. HARMER: Yes.

Senator CONNOLLY: When was the line drawn between corporations with income of less than \$20,000 and corporations with income of more than \$20,000?

Mr. IRWIN: 1949 was the first time this different rate was introduced. At that time the lower rate applied on the first \$10,000. I believe it was in 1953 that the first bracket was increased from ten to twenty thousand.

Senator CONNOLLY: And the rate for them is a straight 20 per cent now? Eighteen plus two?

Mr. IRWIN: Eighteen plus two.

Senator TURGEON: Is the \$20,000 deducted from the total amount taxable or included in the total amount taxable?

Mr. IRWIN: It is not deducted from the amount which is taxable.

Senator CONNOLLY: I think it might be helpful to the committee to explain that point.

The ACTING CHAIRMAN: The actual figures?

Senator CONNOLLY: Yes. Mr. Harmer could do it with an illustration, very simply.

Mr. HARMER: If a corporation has an income of, say, \$10,000, its total tax is 20 per cent, or \$2,000. If it has an income of \$100,000, it pays 20 per cent on the first \$20,000 of that \$100,000, and 45 per cent—or 47 per cent, including old age security tax—on the \$80,000 which is in excess of the \$20,000.

The ACTING CHAIRMAN: Shall section 9 carry?

Some Hon. SENATORS: Carried.

Senator CONNOLLY: There is a subsection about associated companies. I did not explain that part of the section.

The ACTING CHAIRMAN: What section is that?

Senator CONNOLLY: That is the second subsection of section 9. It is a very technical section.

Senator CAMPBELL: The principal purpose of that is to say that more than one company which is closely associated with the others can get the benefit of the reduction.

The ACTING CHAIRMAN: Would you just explain what it is, Mr. Harmer?

Mr. HARMER: As Mr. Irwin said, when this low rate of tax on the first ten or twenty thousand dollars of income, as it now is, was put into effect, it was feared that the bigger companies might split up their operations into several smaller ones in order to get the advantage of the low rate on more than one \$20,000 of income; so the provision was made then that where companies are associated, either parent or subsidiary, or owned by the same people, only one of the group could get the \$20,000 subject to tax at the low rate. Then that had to be widened, because there were groups of companies where the total profits of all the companies in the group did not exceed \$20,000, so we made a provision that they could elect how they wanted the \$20,000 to be split amongst the companies in the group, and each one was taxable then on the amount allocated to it, at the 20 per cent rate. The trouble with that provision was that the allocation they had to make had to be filed with the income tax return of the first company in the group to file its return, and unfortunately some people overlooked filing it then, and because they overlooked it the result was that nobody in the group got any benefit of this rate. This amendment is designed to cure that by saying that if they do not file their allocation on time, the Department will give them notice that "we require an allocation"; they have thirty days within which to file it, and if they do not file it after that time we can still allocate the \$20,000 amongst them so that they get the benefit out of it.

Senator HUGESSEN: It is a relieving section?

Mr. HARMER: Yes.

Senator WOODROW: The parent company can go up to \$20,000 apart from the subsidiaries?

Mr. HARMER: No, sir. Just one of the group.

Senator WOODROW: Including the parent company.

Senator McLEAN: How many shares does a corporation have to own to be related to another, or to be treated as persons not dealing with each other "at arm's length"?

Mr. HARMER: "Arm's length" comes into it. The definition says that any two companies will be deemed to be associated if one of them owns directly or indirectly 70 per cent of the common shares of the capital stock of the other, or if 70 per cent or more of all the common shares of the capital stock of each of them is owned directly or indirectly by one person, or by two or more persons jointly, or by persons not dealing with each other at arm's length.

Senator McLEAN: I notice that in the United States several of the larger companies have stock in associated companies and want to get the benefit of a change in the law which makes the tax less if they own 90 per cent. The Standard Oil Company got 90 per cent of stock of Humble Oil, and claim that, with that 90 per cent ownership, they are entitled to the lesser tax rate.

Mr. HARMER: Under Canadian law or United States law?

Senator McLEAN: United States law.

Mr. HARMER: I am sure I don't know.

Senator KINLEY: How is that term "associated companies" defined, and 70 per cent ownership?

Senator ISNOR: Dealing with associated companies at arm's length, 70 per cent held by a family group, we will say, has there been a change in the last two years with regard to the assessment of that stock, or the dividends, by assessing the individual direct for his holdings in two or three companies? Have I made my point clear?

Mr. HARMER: I am afraid I do not understand.

Senator ISNOR: A, B and C companies are controlled to the extent of 70 per cent by Senator Kinley; and in his return on these companies, instead of dealing directly with those companies, it is decided that "we will assess Senator Kinley direct, because his assessment will place him in a higher bracket". Has that practice been followed recently?

Mr. HARMER: No, sir.

Senator ISNOR: You are quite sure of that?

Mr. HARMER: Not to my knowledge, and I don't know how we would do it.

Senator CAMPBELL: What Senator Isnor probably has in mind is investment companies. It has nothing to do with this at all.

Mr. HARMER: Personal corporations?

Senator ISNOR: Well, companies.

Mr. HARMER: There are only certain companies that come within the definition. They have to derive their income from certain specific sources. This is not new. It has been in the law for many years. Where such companies are controlled by one person or members of his family we do not look upon the company as a separate entity. We treat all the income as income of the shareholders.

Senator ISNOR: Up until two years ago you dealt with those companies individually.

Senator KINLEY: If it is not at arm's length then I suppose the 70 per cent is affected. You have to deal at arm's length in associated companies.

Mr. HARMER: If the persons holding the shares deal with each other at arm's length, then the companies they are controlling are not associated.

Senator ASELTINE: I have read this bill through and I am wondering if any change whatsoever has been made with regard to personal corporations.

Mr. HARMER: There has been no amendment made with respect to personal corporations.

Senator ASELTINE: I am interested in several, and I was not sure from the debate that took place in the House of Commons, which I also read, as to whether or not they were affected.

The Acting CHAIRMAN: Shall Section 9 carry?

Some Hon. SENATORS: Carried.

The Acting CHAIRMAN: Section 10—Tax otherwise payable under this Part.

Senator CONNOLLY: This is a very technical section, as I understand it, Mr. Chairman, and I think it deals with the place where you can apply the foreign tax credit. It seems to me to be an accounting problem more than anything else, is it not?

Mr. IRWIN: Yes, this sets out the Canadian tax against which foreign taxes can be offset.

Senator McLEAN: For instance, the 15 per cent in the United States.

Senator CONNOLLY: Whatever the foreign rate is.

Senator McLEAN: Plus the exchange?

Mr. HARMER: The allowance of the foreign tax is the lesser of the amount of tax actually paid on income derived from that country or the portion of the Canadian tax that the income derived from the foreign country is of the total income derived from all sources. All this does is provide that in computing the second amount, the tax demand to be applicable to the foreign income, you do it after deducting credit for provincial taxes. Previously you made that computation before you deducted the credit for provincial taxes. Now you do it after.

The Acting CHAIRMAN: Shall Section 10 carry?

Some Hon. SENATORS: Carried.

The Acting CHAIRMAN: Section 11—Repeal of Section 54(6).

Mr. IRWIN: This section repeals the section in the act which was enacted in 1946 to provide a restriction on interest. At that time, following the war, there was a considerable delay in assessing returns, and it is felt as these circumstances no longer exist the section is no longer required.

Senator ASELTINE: What happens in a case of this kind? Suppose I overpay my income tax for 1954 by \$2,000. I pay instalments every three months. I have had trouble in cases of that kind in getting any interest at all. I was of the opinion I was entitled to 2 per cent interest on overpayments, but they refused to give me any consideration whatsoever in connection with it. I would like to have some explanation of that.

Mr. IRWIN: I can only point out that this section has no bearing on the payment of interest by the Government on overpayment of taxes.

Senator ASELTINE: I know, but we are talking about interest now and I should like if possible to get some explanation about this 2 per cent that I was supposed to get and which they would not pay me. They say my return is not assessed until April 30th and therefore even if I have overpaid in 1954 I have to pay my instalment for 1955 on the 31st day of March, and if I do not pay it I pay interest on it, and I do not get interest on the other. It does not seem fair to me.

The ACTING CHAIRMAN: What you have just said, Senator Aseltine, is that they ask you to pay interest on your instalment on the 31st of March but they won't give you any interest on the amount of your money in their hands at the year's end.

Senator ASELTINE: Yes.

Mr. HARMER: The law provides that the 2 per cent we have to pay you on overpayments is only in respect of a period commencing with the latest of three days: the day when you make the overpayment, the day on which your return should have been filed, or the day on which your return was actually filed. So for any period from the time you overpaid the money up until the time you filed your return, you do not get interest on it, but from then on you do.

Senator HUGESSEN: All Section 11 of the bill does is to take out the section in the act under which interest was not payable by a taxpayer for a certain period during which there was a delay in assessing. That is, if he was not properly assessed within a year, from that time on he did not pay interest until he was assessed. Is that not it? The reason for repealing that particular section is that there is now no great delay in properly assessing people.

Mr. HARMER: That is right.

Senator HUGESSEN: If we pass Section 11 it will get rid of the question which arose in the courts recently as to what was a proper assessment.

Mr. HARMER: That is right.

Senator ASELTINE: I understand perfectly that this section has nothing to do with the point that I raised.

The ACTING CHAIRMAN: Shall we pass section 11?

Some hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 12—what does it do, Mr. Irwin?

Mr. IRWIN: This is consequential upon the amendment to section 69. This particular subsection referred to a corporation exempt by section 69 as an investment company, and a further clause in the bill makes investment companies liable for a certain tax. So this particular subsection (n) of section 62 has no longer any application.

The ACTING CHAIRMAN: Does section 12 carry?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 13—Capital cost allowance?

Senator ASELTINE: Does section 13 effect any real change? I know that when we have filed returns from the States we have taken off the depreciation and only shown the net amount that accrued to the benefit of each beneficiary, and they paid a tax on that. Is there any real change in this section?

Mr. HARMER: Yes. Up to now a beneficiary who was not entitled to an interest in the corpus of the estate was not entitled to deduct anything for depreciation.

Senator HUGESSEN: Such as a widow who was only entitled to income?

Mr. HARMER: Yes. Now any beneficiary may get the benefit of it.

Senator ASELTINE: Whether such person has any interest in the corpus of the estate or not?

Mr. HARMER: Yes.

Senator CONNOLLY: There is an exception to section 13, though, in the case of a business. There the residuary heir would get the benefit of the depreciation.

Mr. HARMER: You mean under the present law, or as amended?

Senator CONNOLLY: As amended.

Mr. HARMER: Any beneficiary of any estate will get the allowance for depreciation.

Senator CONNOLLY: We used the example, in the house, of the John Ross Robertson estate. In that case, would the life tenant still be entitled to a deduction for the depreciation that was allowed?

Mr. HARMER: After this amendment is passed, yes. In fact, I think the courts told us that even without this amendment they were entitled to the deduction, because when a business was being carried on by the estate it was legal for executors to withhold the depreciation from the beneficiary. This, in effect, enlarges the application of that which was previously applicable only to estates carrying on business.

The ACTING CHAIRMAN: Does section 13 carry?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 14—Special tax rate?

Senator ASELTINE: This is the section I had in mind when I asked the question about personal property. I know there are investment corporations which are not personal corporations. This applies to that class which are not personal corporations, is that right?

Mr. IRWIN: That is right. At the present time companies who can qualify as investment companies are exempt from tax. They have to meet certain

qualifications in Section 69, but since these companies were not Canadian tax-paying corporations, the shareholders who received dividends from those corporations could not claim the 20 per cent dividend tax credit.

Senator HUGESSEN: Under the new system the corporation itself will pay this tax, but the shareholders will be entitled to the 20 per cent deduction with respect to their dividends?

Mr. IRWIN: That is correct.

Senator CONNOLLY: And the same rate in each case, 20 per cent?

Mr. IRWIN: That is right.

The ACTING CHAIRMAN: Does section 14 carry?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 15?

Mr. IRWIN: Clause 15 is an addition to the list of conditions with which a corporation must comply to qualify as a non-resident-owned investment corporation. It provides that a corporation cannot be a non-resident-owned investment corporation for purposes of the Income Tax Act if it receives more than 10 per cent of its gross revenue from rents.

Senator HUGESSEN: What is the principle behind that amendment?

Mr. IRWIN: If a non-resident owns property in Canada which produces rents he is subject to a 15 per cent tax on those gross rents, or he may elect to file a return and pay tax on his net revenue from that income at graduated rates, if he is an individual, or at corporate rates if it is a corporation. On the other hand, the non-resident might be the owner of a non-resident-owned corporation in Canada which owned rent-producing property. Now, as the law stood previously those rents would only be taxed at 15 per cent if received through the non-resident-owned corporation.

Senator CONNOLLY: Fifteen per cent of the net?

Mr. IRWIN: On the net. Now, this will prevent the non-resident-owned corporation being such a corporation if it has more than 10 per of its revenue from rents. It is to equalize the taxation of these rents.

Senator ASELTINE: But if the rental obtained on Canadian property is 10 per cent or less, what happens?

Mr. IRWIN: It would continue to qualify as a non-resident-owned corporation.

Senator ASELTINE: Fifteen per cent on that?

Mr. IRWIN: The net income of the non-resident-owned investment corporation is subject to tax of 15 per cent.

Senator ASELTINE: But if it is over 10 per cent, what happens?

Mr. IRWIN: They cannot qualify as a non-resident-owned investment corporation.

The ACTING CHAIRMAN: Does section 15 carry?

Some hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 16?

Mr. IRWIN: Clause 16 is an addition to the list of conditions with which a corporation must comply to qualify as a foreign business corporation. It provides that it cannot be a foreign business corporation if it derives more than 10 per cent of its gross revenue from the leasing or operation by it of a ship or aircraft.

Canada has treaties with a number of countries under which the income from operating ships or aircraft will be taxed in the countries in which that company is resident, and not where it may operate. Now, it could be that such a company would form a foreign business corporation in

Canada, which is an exempt corporation, and the income from operating ships and aircraft would completely escape taxation.

Senator HUGESSEN: Both in Canada, in which it was a foreign business corporation and in another country in which it operated?

Mr. IRWIN: That is right.

Senator HUGESSEN: Of course it would not operate an aircraft in Canada, because it would then no longer qualify as a foreign business corporation; it would have to carry on all its operations outside Canada.

Mr. IRWIN: That is right.

Senator CAMPBELL: This section really is intended to prevent a Canadian corporation, who owns a vessel and carries on business outside Canada, from escaping taxation, is it not?

Mr. HARMER: Yes.

Senator CAMPBELL: For example, a deep sea operation might be carried on outside Canada in such a manner so that the vessel would never come to a Canadian port; the company, if it was a Canadian corporation could derive substantial revenues from its operations and would previously have escaped taxation. Now irrespective of where its operations are carried on, if the business is that of engaging in leasing and operating ships or aircraft a tax is payable in Canada, is that right?

Senator KINLEY: But only if the ship is registered in Canada?

Senator CAMPBELL: No, irrespective of that.

Senator HUGESSEN: I am afraid I still do not understand the explanation. Nothing that we do here would prevent such a company from being subject to tax in the country in which it carried on its operations. I am not quite certain of the applicability of these agreements between Canada and the other countries to which you referred.

Mr. IRWIN: Because of these agreements other countries would not tax the income from operating a ship or aircraft by a Canadian company.

Senator HUGESSEN: If it is a Canadian company, and regardless of whether it carries on its operations entirely elsewhere.

Mr. IRWIN: Correct.

The ACTING CHAIRMAN: Shall Section 16 carry?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 17?

Mr. HARMER: This is a rather simple section. It is again to bring the law into line with practice. The section that it amends provides for the depreciation of capital expenditures made on scientific research over a three-year period. The technical wording of the law previous to this amendment could have been held to deny such a company any depreciation in the first year in which it made its capital expenditures. This is to insure that it gets them, not only in the second and third years, but also in the first year.

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Clause 18—Limitation?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Clause 19—Allocation Contingent or Absolute Taxable.

Senator ASELTINE: That needs some explanation.

Mr. IRWIN: This section refers to employees profit sharing plans. As I mentioned earlier, the scheme under the employee profit sharing plan is that the amount allocated by the employer shall be taxable in the hands of the

employee each year as allocated. Moreover, when an employee who was a member of the plan terminated his employment, the plan might provide that his share be reallocated to other employees and under the present law that reallocation is taxable in the year so reallocated. This amendment provides that these reallocations will not be taxed.

Senator CAMPBELL: May I ask a question which occurs to me? What is the practice in determining the amount allocated to employees in such a plan, if a substantial or some portion of the revenue is derived from capital appreciation, from investments which would ordinarily be non-taxable?

Mr. HARMER: My understanding is that everything that is allocated to an employee under the plan is taxable, regardless of its source.

Senator CAMPBELL: I am thinking of substantial moneys invested in Canadian securities as investments, not for speculative purposes. Now by reason of the very large increase in the value of these securities and the revenues that come from them, the appreciation in capital is sometimes much more than the income. Ordinarily they would not be taxable in the hands of employees, if derived as capital gains.

Mr. HARMER: If he made those gains himself.

Senator CAMPBELL: But the practice is to treat capital gains as income, is that so?

Mr. HARMER: I don't think we recognize them as capital gains. The point is, what the employee is getting is a benefit out of his employment, and the source from which the funds arose which are used to give him that benefit, which arises by virtue of his employment, we do not regard as too material.

Senator CAMPBELL: Has that question been raised recently?

Mr. HARMER: We have had it raised with individual taxpayers, yes.

Senator CAMPBELL: But there has been no consideration of a change in the law to grant relief in those circumstances?

Mr. HARMER: That is something I could not answer. I don't know whether the department of Finance has considered it.

Senator CONNOLLY: If capital appreciation went to an employee without the profit sharing plan, would Senator Campbell's question be answered in the same way?

Mr. HARMER: Anything the employee gets by virtue of his employment is considered to be income in his hands.

Senator WOODROW: What about the contributions?

Mr. HARMER: He would not be taxed on them when they are returned to him.

The ACTING CHAIRMAN: Shall the section carry?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 20—Taxable portion of deemed to be dividend.

Mr. HARMER: That merely adds a cross reference.

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Clause 21—Exemption for three years.

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 22?

Senator CONNOLLY: This section simply means that Crown companies if they have an income of not more than \$20,000 can get the benefit individually

without reference to associated companies, such as we had in section 1. Is that correct?

Mr. HARMER: That is right; and even if they make more than \$20,000, the first \$20,000 in each year is taxable at the lower rate.

The ACTING CHAIRMAN: Shall section 23 carry?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 24?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 25?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 26?

Senator CONNOLLY: Bottles are not included, Senator Roebuck.

Senator ROEBUCK: They are not. But they are good containers.

The ACTING CHAIRMAN: Shall section 26 carry?

Some Hon. SENATORS: Agreed. Carried.

The ACTING CHAIRMAN: Now we will take up section 27. Are there any questions on section 27?

Senator ASELTINE: I think we should have an explanation of this section—sale of inventory.

Mr. HARMER: Within the last couple of years, Senator Aseltine, we have taken to court—

Senator ASELTINE: Just a moment before you go on. If I have a business and I sell my inventory of goods at the wholesale cost to me, say, plus carrying charges, and make no profit on it, would I be taxable under this section?

Mr. HARMER: If you made no profit, no sir.

Senator ASELTINE: It is only if I sell at a profit.

Mr. HARMER: If you sell at a profit this would affect you.

Senator KINLEY: Yes, but what are these carrying charges?

Senator ASELTINE: In our province, where sales of businesses are concerned, I know that if a person buys a business the goods are usually turned over to him at what the actual cost was to the seller of the business.

Mr. HARMER: That is, I think, a fact, but in practice what happens is that, although they may be sold at cost, because of the fact that they have been in stock for a long time the original proprietor may have written them down by reducing his inventory values over a period of years so that when he comes to the end of the road he has a stock that cost him \$100,000 but which appears in his inventory at only \$80,000, so if he sells for cost he will get \$100,000, and in the past we have not been able to tax that \$20,000. This amendment enables us to do so.

Senator ASELTINE: Is it the custom to depreciate stock on hand at the end of the year?

Mr. HARMER: It is permissible to value your inventory at the end of the year at the lower of cost or market. If the market has gone down in the meantime, which includes recognition of some shopworn or obsolete goods, it can be that the inventory value is less than the original cost.

Senator ASELTINE: In the example that you gave, you will now be able to tax the \$20,000?

Mr. HARMER: Yes.

Senator HUGESSEN: That amount representing deductions which you had allowed him to make from his income during the years.

Mr. HARMER: Yes.

The ACTING CHAIRMAN: What is the difference between the amendment proposed in the bill and the present act?

Mr. HARMER: We always thought we had the right to tax such sums on the sale of inventory en bloc, but in the last couple of years we have taken two or three cases to court and we found we did not have any right to tax.

The ACTING CHAIRMAN: But thousands of taxpayers have paid the tax in the belief that you had that power?

Mr. HARMER: Yes, but two or three did not, though.

Senator ISNOR: This is along the lines of the same question that I asked Senator Connolly in regard to the sale of stock, and as I understand it there has been a markdown at the end of each year over a period of say five or six years, but when the sale of the inventory en bloc is made you will now be able to assess on the difference between the selling price and the original cost. Is that it?

Mr. HARMER: The sale price and the marked down price.

Senator ISNOR: The sale price?

Mr. HARMER: The difference between the sale price and the marked down price that he last used.

Senator ISNOR: Yes, the depreciated price.

Mr. HARMER: Yes.

Senator CONNOLLY: There was another question asked in connection with this, and that has to do with mortgage reserves. One of the senators on the floor of the house asked if that applied only to companies. My understanding is that it is to apply to any taxpayer.

Mr. HARMER: Yes, whose business is the lending of money.

Senator CONNOLLY: Yes.

The ACTING CHAIRMAN: Are there any other questions on section 27? Shall the section carry?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 28—tax. Any questions?

Some Hon. SENATORS: Carried.

The ACTING CHAIRMAN: Section 29—tax. Are there any questions on section 29?

Senator ASELTINE: I just do not understand 105B, tax in respect of dividends paid out of designated surplus.

Senator CAMPBELL: That is for a special purpose is it not?

The ACTING CHAIRMAN: Will you give us an explanation of the proposed section 105B?

Mr. HARMER: 105B; to understand it you have to go back to certain fundamentals the first of which is that dividends paid by one Canadian corporation to another Canadian corporation are not taxable in the receiving corporation's hands. Secondly, several years ago now, because by reason of that first provision the owners of businesses were able to sell their shares of a company which had accumulated a surplus to another company and that surplus then disappeared without tax being paid on it, provision was made in the law that a dividend paid by a corporation that had a surplus when its shares were acquired by another corporation would not pass tax-free between those two corporations.

Senator CAMPBELL: Out of surplus accumulated to that date.

Mr. HARMER: That is right. This amendment enlarges that to say that a dividend paid by a corporation that had a surplus on hand when its shares were

acquired by a non-resident corporation, by a person exempt from tax under section 62, which is mostly charitable organizations, or by a trader or dealer of securities, also is not tax-free when paid out of that surplus on hand when its shares were acquired. The object of this is to prevent the same abuse that the original provision was subject to, which was being accomplished by shareholders selling their shares to these kinds of people. For instance, if the shares of a corporation were acquired by a charitable organization it could then pay dividends to itself which were not taxable in its hands. So, in the case of a non-resident corporation the dividend could be paid at a very low rate of 5 per cent if it was a wholly-owned subsidiary or in the case of a trader or dealer in securities the dividend could be paid and while it was taxable there was an offset to that in the traders or dealers hands in that he could deduct from his income the loss on his investment in this corporation, so this section now says that there will be a special tax of 15 per cent if such dividends are paid to either a non-resident corporation or a charitable organization, or a 20 per cent tax is payable if dividends are paid to a dealer or trader in securities.

Senator CONNOLLY: Why the discrimination between the two?

Mr. HARMER: Mr. Irwin may know the answer to that. I don't.

Mr. IRWIN: It was thought that the heavier rate was necessary here because under certain circumstances a dealer might get an additional benefit from this transaction. If, for example, he is an individual, he will receive dividends; and, as Mr. Harmer has explained, he can offset this income by a loss; but having received dividends he is also eligible for a dividend tax credit on these dividends that he has received.

Senator CAMPBELL: Does not the section really go farther than to catch the surplus that has been accumulated from dividends received from Canadian corporations? Is it not also intended to prevent a company that has carried on an ordinary business operation over a number of years and accumulated a large surplus, leaving the company with substantial cash, including a large earned surplus, from selling the shares of that company to a foreign investment corporation or some other person who is not taxable in Canada, and then distributing the surplus, and thus avoiding the tax on the distribution of surplus on winding up proceedings?

Mr. HARMER: That is right.

Senator CAMPBELL: So it is really to close the door on some escapes that were found in the winding up of corporations?

Mr. HARMER: That is right.

The CHAIRMAN: Shall section 29 carry?

Some Hon. SENATORS: Agreed.

Section agreed to.

The ACTING CHAIRMAN: Section 30—Timber royalties.

Senator CONNOLLY: Sections 30 and 31 are pretty specialized, are they not? They relate to deals based on the timber royalty system.

Mr. HARMER: That is right, senator. There is a tax of 15 per cent on royalties paid by a person resident in Canada to a non-resident. However, some non-resident taxpayers entered into transactions with Canadians for the sale of timber on a stumpage basis where the payment that was to be made was not really a royalty, it was in fact part of the purchase price, but it was in the nature of a royalty. In those cases we were unable to tax that at 15 per cent; and this enables us to do so.

Senator CONNOLLY: It closes a gap, too.

Mr. HARMER: That is correct. And section 31 follows up on that, and gives the option to non-residents who are subject to this tax on timber

royalties of 15 per cent of the gross to file a return and pay a tax on the net, depending, as Mr. Irwin said previously, whether they were a corporation, at corporation rates, or an individual, at the graduated rates.

The ACTING CHAIRMAN: Shall section 30 carry?

Some Hon. SENATORS: Agreed.

Section 31 was agreed to.

The ACTING CHAIRMAN: Section 32—Loan to wholly-owned subsidiary.

Senator HUGESSEN: Is that just a change of draftmanship?

Mr. IRWIN: It substitutes the word "creditor" for the expression "original lender".

Senator ASELTINE: Why is that necessary?

Mr. IRWIN: It covers a situation where the original lender may have transferred the indebtedness to another person and the term "original lender" did not cover all the circumstances.

Senator WOODROW: Does that apply only to non-resident corporations?

Mr. HARMER: It only affects a non-resident taxpayer.

Section agreed to.

Sections 33 and 34 agreed to.

The ACTING CHAIRMAN: Shall the bill carry?

Hon. SENATORS: Carried.

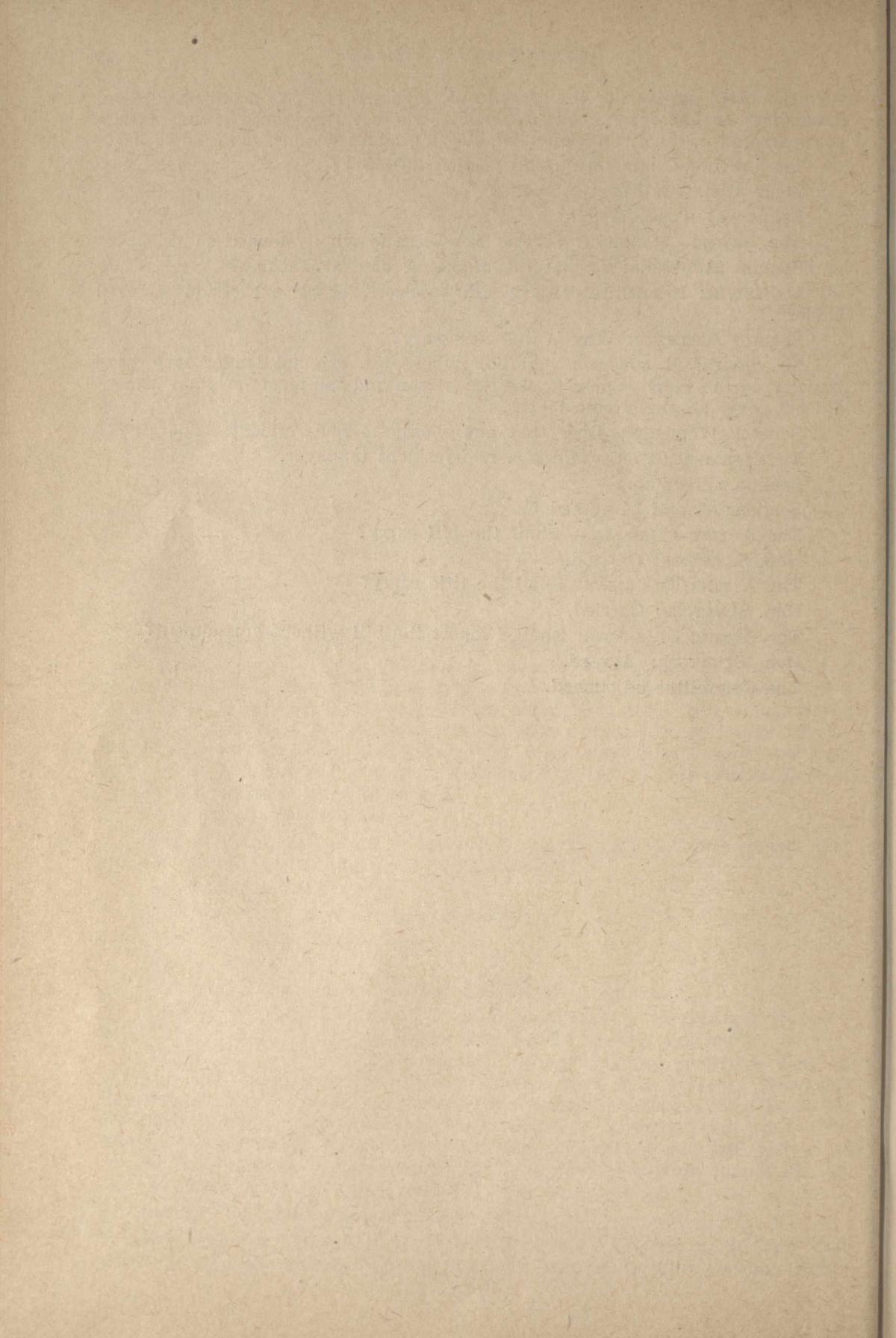
The ACTING CHAIRMAN: Shall the title carry?

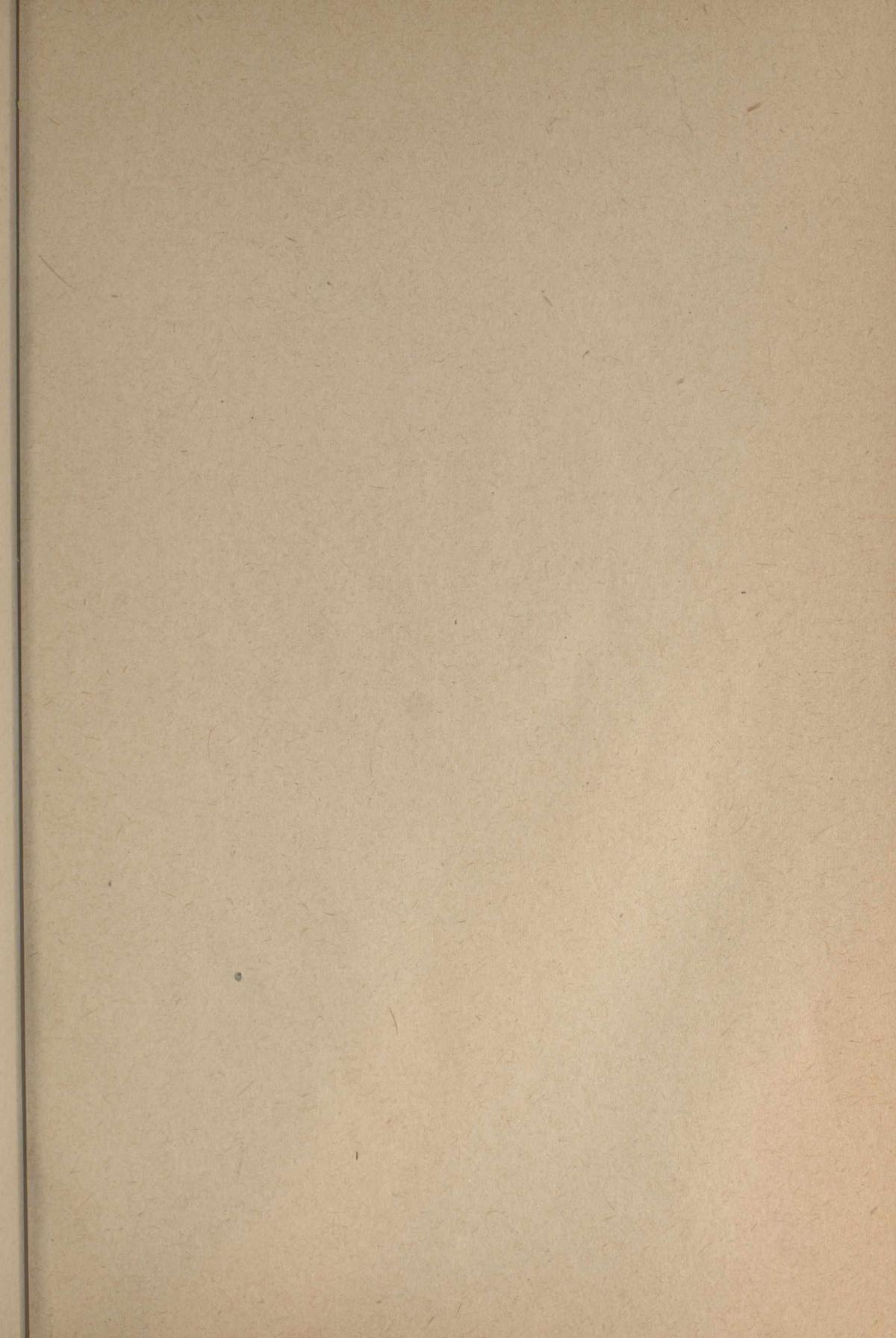
Hon. SENATORS: Carried.

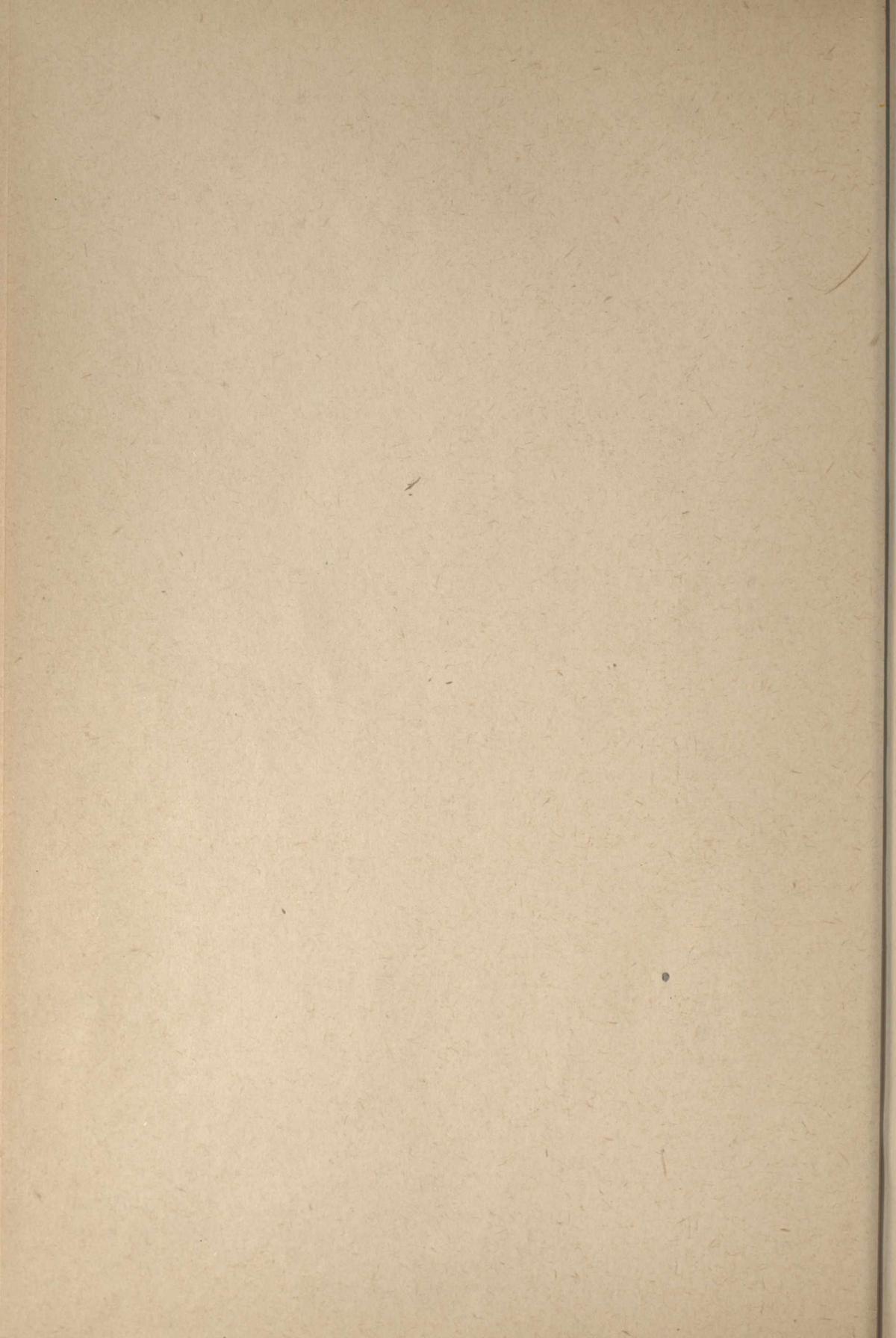
The ACTING CHAIRMAN: Shall I report the bill without amendment?

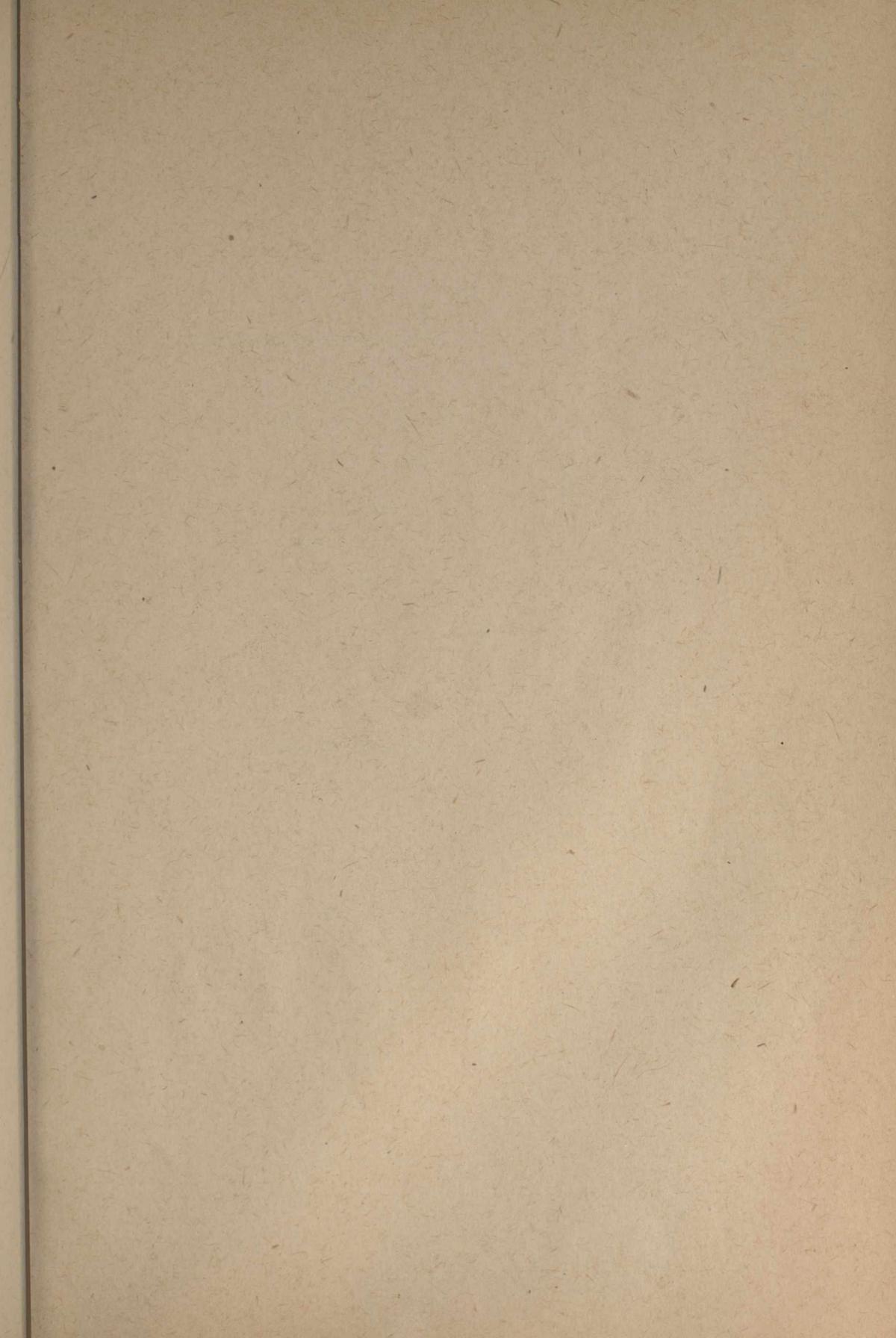
Hon. SENATORS: Agreed.

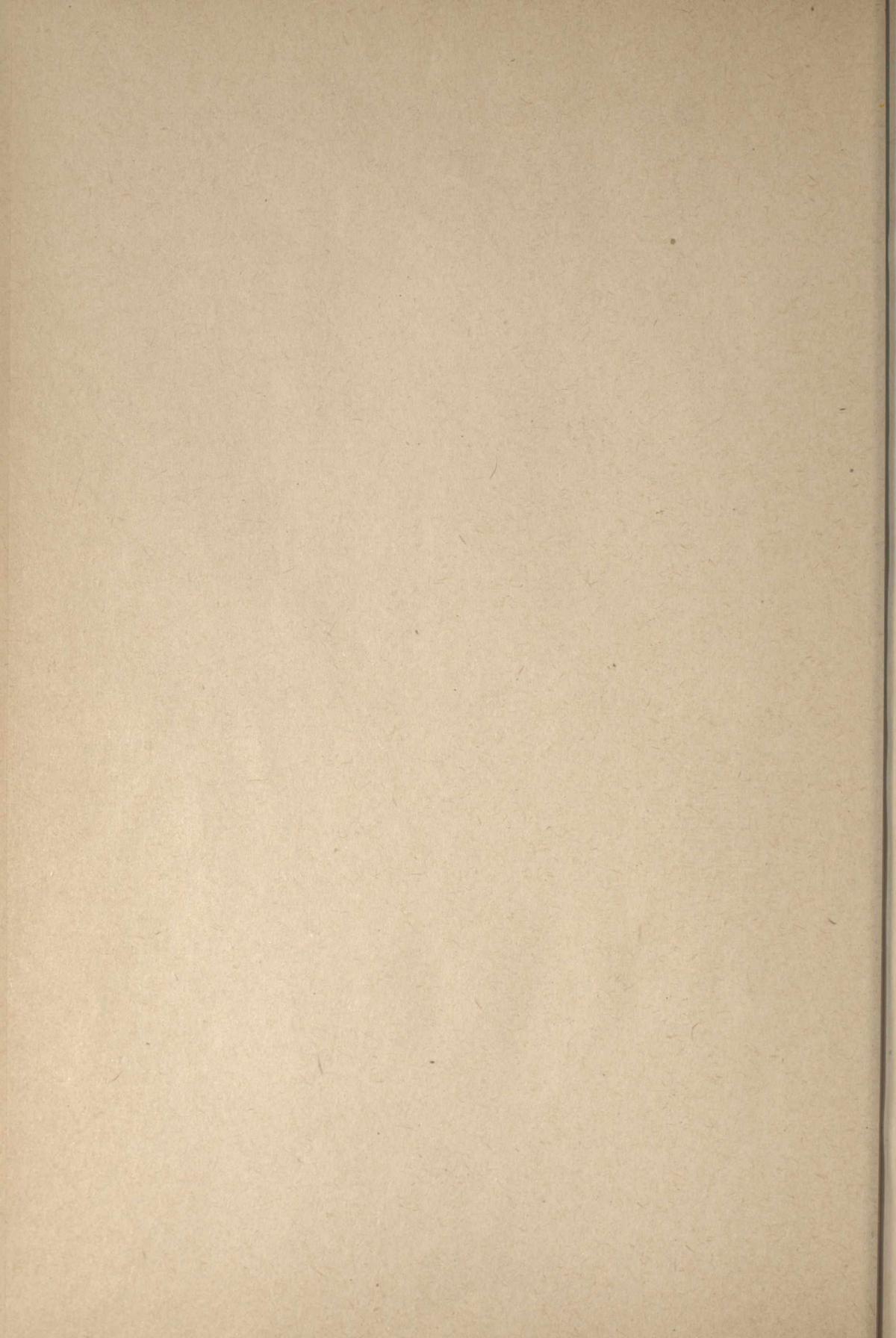
The Committee adjourned.

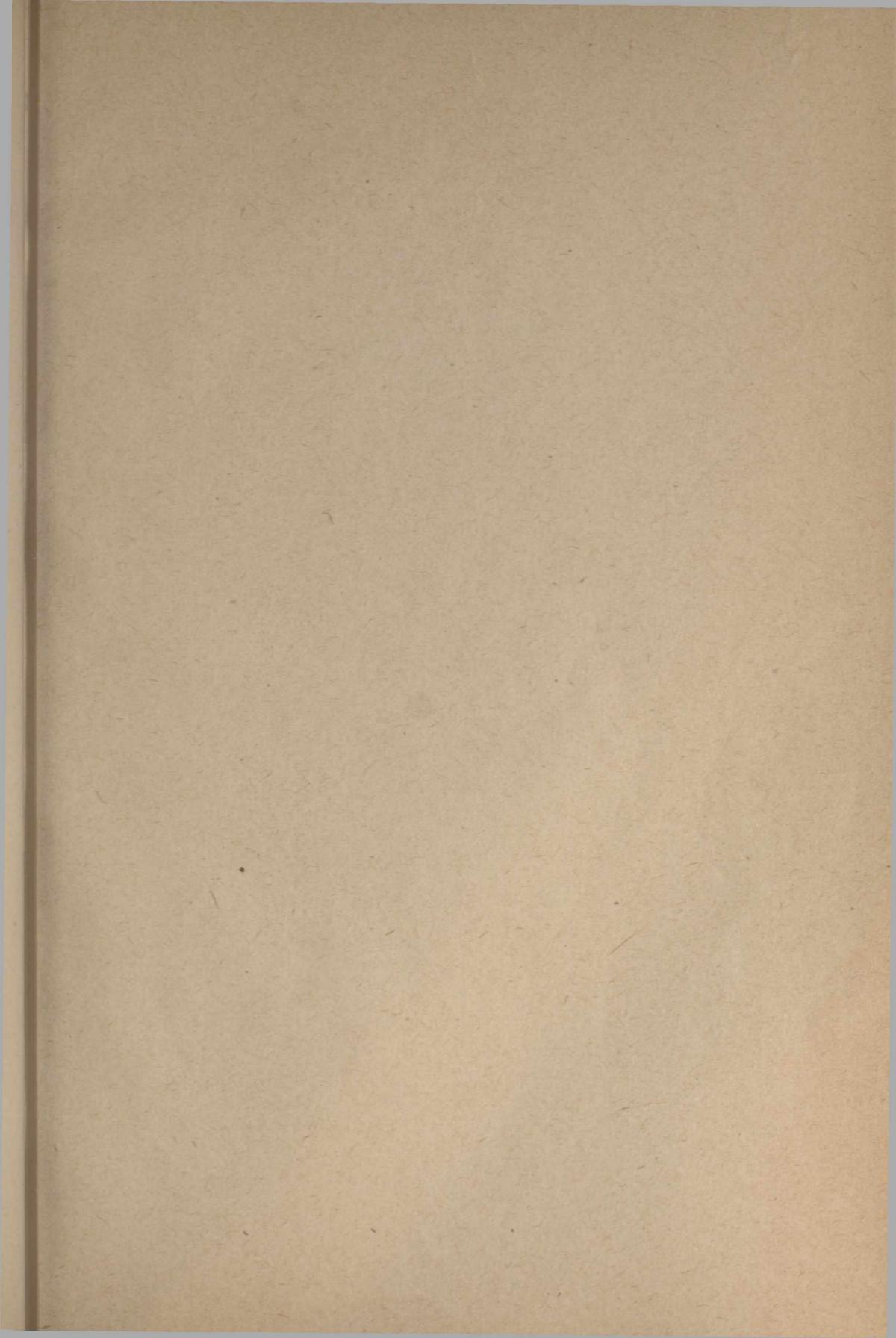


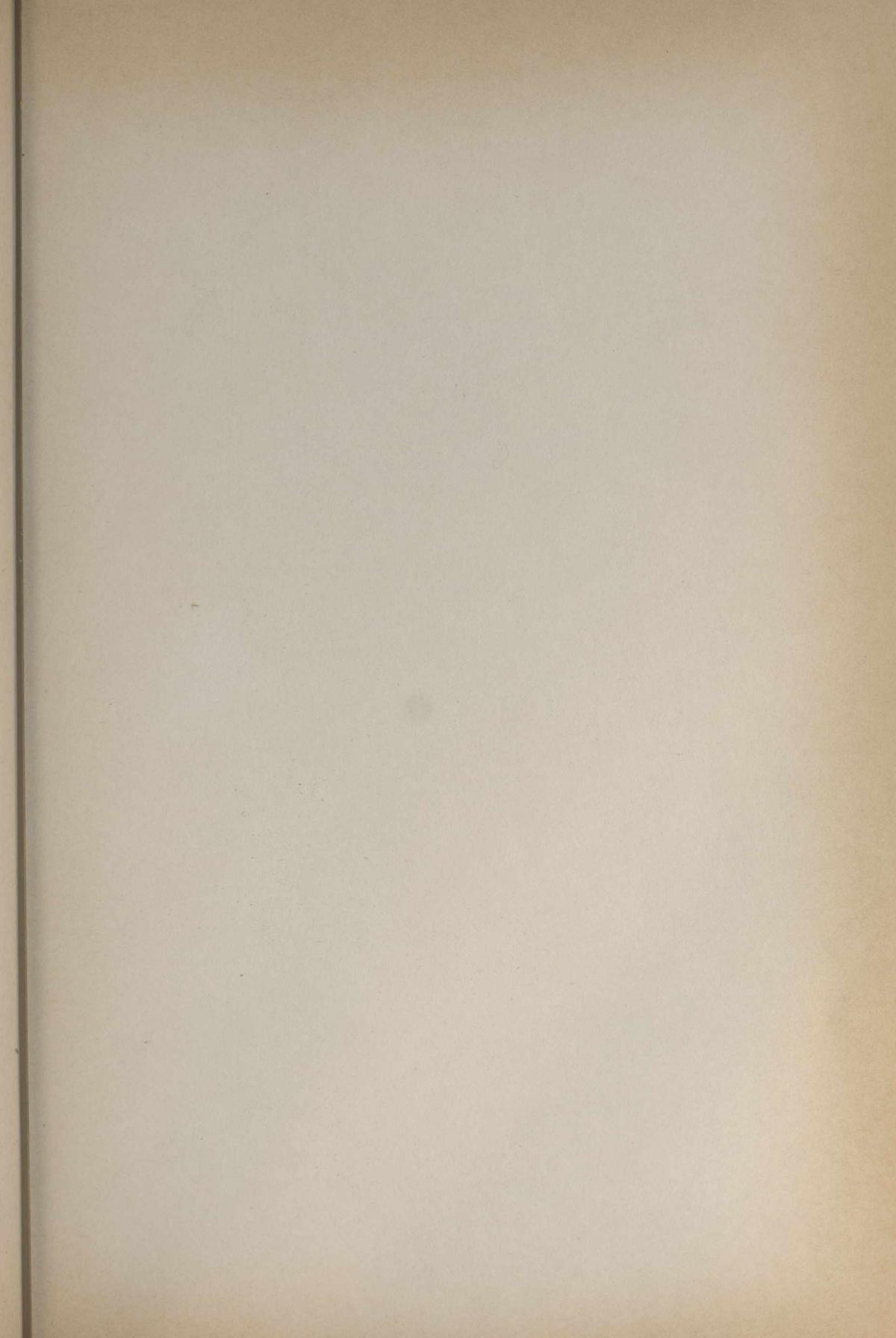












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