Income Tax Folio S3-F2-C2, Taxable Dividends from Corporations Resident in Canada

Series 3: Property, Investments and Savings Plans

Folio 2: Dividends

Chapter 2: Taxable Dividends from Corporations Resident in Canada

Summary

This Chapter discusses the tax implications of receiving a taxable dividend from a corporation resident in Canada, focusing on dividends received by individuals and corporations who are also resident in Canada. In general, the tax treatment of such dividends will depend upon two factors. The first factor is the underlying corporate income tax rate that has been applied to the income from which the particular dividend is paid. The second factor is the corporate status of the payor corporation (for example, a **Canadian-controlled private corporation**, defined in subsection 125(7)). The rules underlying this tax treatment are collectively referred to as the **eligible dividend regime**. The treatment of dividends received by a trust (other than a registered charity) resident in Canada, and the treatment of dividends received by a partnership whose members are persons resident in Canada, are also briefly described.

This Chapter comments on the following topics:

- the meaning for tax purposes of the terms **dividend**, **taxable dividend**, **eligible dividend** and **non-eligible dividend**;
- **stock dividends** and **dividends-in-kind**, special types of dividends;
- the concept of integration, together with the related concept of a dividend **gross-up** and **dividend tax credit** mechanism which is generally applicable to dividends received by individuals; and
- the rules of the eligible dividend regime.

Finally, this Chapter briefly describes certain provisions which give special tax treatment for taxable dividends in specific situations including, for example, securities lending arrangements and dividend rental arrangements.

The Canada Revenue Agency (CRA) issues income tax folios to provide a summary of technical interpretations and positions regarding certain provisions contained in income tax law. Due to their technical nature, folios are used primarily by tax specialists and other individuals who have an interest in tax matters. While each paragraph in a chapter of a folio may relate to provisions of the law in force at the time it was written (see the Application section), the information provided is not a substitute for the law. The reader should, therefore, consider the Chapter's information in light of the relevant provisions of the law in force for the particular tax year being considered.

The CRA may have published additional guidance and detailed filing instructions on matters discussed in this Chapter. See the CRA's Forms and publications web page for this information and other topics that may be of interest.

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Discussion and interpretation

Overview of taxable dividends

2.1 This section gives an overview of the tax implications for individuals and corporations resident in Canada that receive taxable dividends from a corporation resident in Canada. It is not intended as a substitute for the more detailed content that follows. The comprehensive discussion will be primarily of interest to tax specialists and to persons who may be affected by the payment or receipt of a taxable dividend.

2.2 A person (an individual or a corporation) must generally include in income the total of all taxable dividends received in a tax year from corporations resident in Canada. An individual (including a trust that is not a registered charity) will also include a gross-up amount on the dividends received and claim a non-refundable dividend tax credit. Together, the dividend gross-up and dividend tax credit help to ensure that income earned by an individual through a corporation resident in Canada is subject to the same total amount of tax as if the income had been earned directly by that individual.

2.3 A corporation may offset its income inclusion by deducting the total of all taxable dividends it receives from taxable Canadian corporations, or from certain corporations that it controls. This is called the intercorporate dividend deduction. The result of the **intercorporate dividend deduction** is that taxable dividends are generally paid tax-free between Canadian corporations. This tax treatment is subject to several anti-avoidance provisions. For example, subsection 55(2) prohibits, among other things, arrangements which convert a capital gain on a disposition of shares into a tax-free dividend (called capital gains stripping). Also relevant are the anti-avoidance provisions and the corresponding interpretative rules in subsections 112(2.1) to (2.9).

2.4 A taxable dividend paid after 2005 by a corporation resident in Canada is characterized as either an eligible or non-eligible dividend. In general terms, an **eligible dividend** is a taxable dividend paid to a person resident in Canada. The corporation must also follow certain procedures to notify all dividend recipients that all or a portion of a dividend is designated as an eligible dividend. All other dividends, including those that have not been properly designated, are considered to be **non-eligible dividends**.

2.5 The designation of an eligible dividend for **Canadian-controlled private corporations** (CCPCs) and other private corporations (defined in subsection 89(1)) must be made each time a dividend is paid by notifying the recipient shareholders in writing. For public corporations (defined in subsection 89(1)), notification is considered to have been made if before or at the time the dividend is paid, the corporation makes a designation using an acceptable method. The designation must state that all dividends are eligible dividends unless indicated otherwise.

2.6 In certain limited circumstances for taxable dividends paid after March 28, 2012, a corporation may be permitted to make a late designation of an eligible dividend (late designation).

2.7 There are separate dividend gross-up factors and dividend tax credit rates for eligible and non-eligible dividends. Specifically, there is an enhanced dividend tax credit and gross-up for eligible dividends. As a result, eligible dividends are taxed at a lower personal income tax rate (combined federal and provincial or territorial) to recognize that eligible dividends are considered to be paid from corporate income taxed at full corporate income tax rates. By comparison, non-eligible dividends are taxed at a higher combined personal income tax rate as they are considered to be paid from corporate income that has benefitted from preferential tax treatment at the corporate level, such as the small business deduction.

2.8 A CCPC maintains an account called the **general rate income pool (GRIP)** to track amounts that can be designated as an eligible dividend. Eligible dividends received by a CCPC increase its GRIP, while eligible dividends **paid** by the CCPC reduce its GRIP. If the total amount of eligible dividends that a CCPC pays in a tax year exceeds the balance of its GRIP at the end of that year, the corporation will have made an **excessive eligible dividend designation (excessive designation)** equal to the amount of the excess. This amount is prorated among all of the eligible dividends paid by the corporation in the year.

2.9 Public and private corporations (**non-CCPCs**) must maintain an account called the **low rate income pool (LRIP)**. The LRIP tracks amounts that must be paid out by the corporation as non-eligible dividends before it is permitted to pay eligible dividends. Non-eligible dividends received by a non-CCPC increase its LRIP, while non-eligible dividends that are **payable** by the non-CCPC reduce its LRIP. If a non-CCPC pays an eligible dividend at a particular time when it has LRIP, the corporation will have made an excessive designation at that time equal to the lesser of its LRIP and the total of all eligible dividends it paid, prorated on an eligible dividend by eligible dividend basis at that time.

2.10 Eligible dividends may also flow through partnerships to their partners and through trusts to their beneficiaries.

2.11 A corporation making an excessive designation will be subject to an additional tax equal to 20% of the excessive designation plus interest until the date of payment. This additional tax is often called **Part III.1 tax**. Each person who received any portion of the dividend will be jointly and severally, or solidarily, liable with the corporation for the person's appropriate share of the Part III.1 tax and interest.

2.12 An election is available to avoid Part III.1 tax. If the election is properly made, the excess portion of the dividend will be treated as a non-eligible dividend in the hands of the recipient shareholders, who are then responsible for any resulting additional tax and interest. However, the election can generally only be made if all of the shareholders who were entitled to any portion of the original dividend agree to the election.

2.13 Anti-avoidance rules may apply if transactions are structured to artificially maintain or increase a corporation's GRIP, or to artificially maintain or decrease a corporation's LRIP. If these rules apply, the eligible dividend will usually be treated as an excessive designation that is subject to an additional Part III.1 tax of 30% of the entire amount of the eligible dividend, together with interest on that amount until the date of payment. In this circumstance, no election can be made to avoid the Part III.1 tax.

2.14 Corporations might be combined—by amalgamation, merger or a winding-up of a subsidiary corporation into its parent corporation. In such situations, an actual or notional amount for each predecessor corporation's GRIP or LRIP in the particular circumstance, may be carried over to the surviving corporation.

2.15 If a corporation becomes or ceases to be a CCPC, the corporation will calculate a notional amount representing an opening GRIP or LRIP, respectively, for the corporation.

Terms used in a discussion of dividends

Meaning of dividend

2.16 The term **dividend**, as it applies to a dividend paid by a corporation resident in Canada, is not specifically defined in the Act except to the extent that subsection 248(1) provides that a dividend includes a stock dividend.

2.17 Although it is not explicitly defined in the Act, the term dividend does have a generally accepted meaning recognized under corporate law and by the courts. Specifically, any pro rata distribution by a corporation resident in Canada among shareholders of a particular class or series of shares of the capital stock of the corporation, may be described as a dividend where the relevant corporate law requirements to pay a dividend are met. Such a distribution can also be considered to be a dividend if other factors are present that show the corporation intended to pay a dividend. However, the fact that a distribution is not called a dividend by the corporation does not affect the nature of the distribution. These principles, which form the generally accepted meaning, will be used for purposes of interpreting the word dividend in the Act in the context of a dividend paid by a corporation resident in Canada.

2.18 In the ordinary course of business, a corporation may generally pay a dividend:

- in cash;
- as a dividend-in-kind by a distribution of corporate property (if allowed under the relevant corporate law); or
- as a stock dividend.

Stock dividend

2.19 A **stock dividend** is defined in subsection 248(1) to include any dividend paid by a corporation to the extent that it is paid by the issuance of shares of any class of the capital stock of the payer corporation. A stock split is not a stock dividend and the distinguishing features of each term, as well as the tax treatment of stock dividends, are discussed in Interpretation Bulletin IT-88R2, Stock dividends. The tax implications of a stock split are discussed in Interpretation Bulletin IT-65, Stock splits and consolidations.

2.20 The amount of a stock dividend is generally the **amount** by which the paid-up capital of the corporation paying the dividend is increased because of the payment of the dividend. This is set out in the definition of amount in subsection 248(1). This amount also determines the cost of the share under subparagraph 52(3)(a)(i), where the stock dividend is received by a shareholder that is an individual.

2.21 For a shareholder that is not an individual, the cost of a stock dividend received after April 20, 2015 is the total of two amounts which are determined under clauses 52(3)(a)(ii)(A) and (B) respectively.

2.22 In general terms, clause 52(3)(a)(ii)(A) provides that the cost of a stock dividend received by a corporation is the safe income that could reasonably be considered to contribute to the unrealized capital gain on the share on which the stock dividend is paid. More specifically, the amount determined under clause (A) is the amount, if any, by which

- the lesser of the amount of the stock dividend and the fair market value of the stock dividend
  exceeds
- the amount of the dividend that the shareholder may deduct under subsection 112(1) in computing taxable income, except any portion of the dividend that does not exceed the safe income on the share.

2.23 Clause 52(3)(a)(ii)(B) generally provides for an amount to be included in the cost of a stock dividend where the anti-avoidance rule in subsection 55(2) applies to the dividend. This amount is determined by the formula **A + B** where:

A = the amount of the stock dividend deemed to be a capital gain by paragraph 55(2)(c). For this purpose, and unlike in clause (A), the amount of the stock dividend is determined under subsection 55(2.2). In general, this amount is the greater of the increase in the paid-up capital of the corporation that paid the dividend and the fair market value of the share received as a stock dividend.

B = the amount, if any, by which:

- the amount of the stock dividend that is deemed by paragraph 55(2.3)(b) to reduce the safe income of any corporation that could reasonably be considered to contribute to the capital gain on the share (which gain was reduced by the dividend)
  exceeds
- the amount determined for clause (A).

Dividend-in-kind

2.24 A **dividend-in-kind** will generally receive the same tax treatment as a cash dividend. As contemplated by the definition of **amount** in subsection 248(1), the amount of a dividend-in-kind—other than a stock dividend—is equal to the fair market value of the property at the time of the payment or transfer to the shareholder. Similarly, a shareholder that has received a property as a dividend-in-kind is deemed to have acquired the property at a cost equal to its fair market value at that time. This is set out in subsection 52(2). Subsection 52(2) also deems the corporation to have disposed of the property at that time for proceeds equal to that same amount.

2.25 It is the CRA's view that where a credit to a shareholder's account or a reduction of a shareholder's debt constitutes the payment of a dividend, the amount received by the shareholder as a dividend is equal to the amount so credited or the amount by which the debt is so reduced. Whether such action constitutes the payment of a dividend is discussed in Interpretation Bulletin IT-243R4, Dividend Refund to Private Corporations.

Deemed dividend

2.26 A **deemed dividend** will receive the same tax treatment under the Act as a pro rata distribution by a corporation to its shareholders. A dividend may be deemed to have been paid by a corporation and received by a shareholder in the circumstances specified in section 84. For example, a deemed dividend may result where a corporation:

- increases its paid-up capital (other than by a stock dividend) by an amount that exceeds any increase in the corporation's net assets or any reduction in its net liabilities;
- reduces its paid-up capital by an amount that is less than the amount paid by it on a reduction of the paid-up capital;
- makes a distribution on the winding-up, discontinuance or reorganization of its business; or
- redeems, acquires or cancels a share of its capital stock.

2.27 A dividend may also be deemed under section 84.1 to have been paid by a corporation (the purchaser corporation) and received by a taxpayer resident in Canada (other than a corporation) where:

- the taxpayer disposes of shares of a corporation resident in Canada (the subject corporation) to the purchaser corporation;
- the taxpayer does not deal at arm's length with the purchaser corporation; and
- immediately after the disposition, the two corporations are connected within the meaning assigned by subsection 186(4) (with appropriate reference changes).

The provisions of section 84.1 should be carefully reviewed to determine the specific tax treatment for any given situation. Additional information about section 84.1 is provided in Interpretation Bulletin IT-489R, Non-Arm's Length Sale of Shares to a Corporation.

Meaning of taxable dividend

2.28 The term **taxable dividend** is defined in subsections 248(1) and 89(1). It is generally defined to be a dividend other than one that the payor corporation has elected to treat as a capital dividend under subsection 83(2). Generally, a taxable dividend on a share of the capital stock of a corporation resident in Canada must be included in the recipient's income under paragraph 12(1)(j) and subsection 82(1) in the tax year it is received.

Eligible dividend

2.29 The term **eligible dividend** is defined in subsection 89(1). It is the portion of a taxable dividend that is paid by a corporation resident in Canada to a person resident in Canada and designated as an eligible dividend in the manner set out in subsection 89(14).

2.30 An eligible dividend also includes certain amounts that might be deemed to be a taxable dividend received by a person resident in Canada. Specifically, this includes:

- an amount allocated by a SIFT partnership (a specified investment flow-through partnership, defined in subsections 197(1) and 248(1)) that is deemed by subsection 96(1.11) to be a taxable dividend; or
- a distribution from a SIFT trust (a specified investment flow-through trust, defined in subsections 122.1(1) and 248(1)) that is deemed by subsection 104(16) to be a taxable dividend.

Additional commentary on the concept and rules relating to eligible dividends is provided under the heading Determination and designation of eligible dividends.

Non-eligible dividend

2.31 The phrase **other than an eligible dividend** is used in the Act to describe a taxable dividend that does not meet the definition and/or designation requirements of an eligible dividend. While the terms **non-eligible dividend** or **ineligible dividend** do not appear in the Act, they are commonly used to describe such taxable dividends.

A capital dividend is not a taxable dividend

2.32 Where at a particular time a dividend becomes payable by a private corporation, the corporation might make a capital dividend election under subsection 83(2) for the full amount of the dividend. In this case, the dividend will be deemed to be a **capital dividend** to the extent of the corporation's capital dividend account immediately before the particular time. Such a capital dividend is not included in computing the income of any shareholder of the corporation. However, notwithstanding that a subsection 83(2) election has been made, subsection 83(2.1) may apply to deem the dividend to be received by the shareholder as a taxable dividend to be included in income. The concept of capital dividends is discussed in Income Tax Folio S3-F2-C1, Capital Dividends.

Tax treatment of taxable dividends paid by a corporation resident in Canada

Concept of integration

2.33 The Canadian tax system is designed to achieve corporate and personal tax integration on business and property income that is earned through a corporation resident in Canada. This income is generally subject to two levels of tax:

- corporate taxation when the income is earned; and
- personal taxation when the remaining after-tax amount is distributed as a dividend, through a chain of corporations or directly, to a shareholder that is an individual.

2.34 The underlying principle of integration is that income earned by a corporation resident in Canada and paid as a dividend to an individual should be subject to the same total amount of tax as if the income had been earned directly by the individual. In broad terms, integration is achieved through the combined use of the intercorporate dividend deduction system and the dividend gross-up and dividend tax credit mechanism. Additional information about the intercorporate dividend deduction and the dividend gross-up and dividend tax credit mechanism is provided under the heading Taxable dividends received by a corporation resident in Canada.

2.35 Related to the concept of integration is the refundable tax system under Part I and Part IV. In general terms, this refundable tax system is meant to prevent individuals from deferring personal tax on investment income and portfolio dividend income earned and retained in a private corporation.

2.36 A special tax is imposed on such amounts that are retained by a private corporation. This tax is intended to approximate the tax that would be paid by an individual had they received the investment income or portfolio dividend income directly. The tax is later refunded to the corporation, in whole or in part, when it distributes the income to its shareholders in the form of dividends. Subsections 129(1) to (8) provide rules for determining the refundable portion of Part I tax and the dividend refund of a private corporation. Information on these rules is available on the web page Dividend refund rules. The rules for determining the refundable Part IV tax liability under section 186 are discussed in Interpretation Bulletin IT-269R4, Part IV Tax on Taxable Dividends Received by a Private Corporation or a Subject Corporation.

Taxable dividends received by a corporation resident in Canada

2.37 Under paragraphs 82(1)(a) and (a.1), a corporation resident in Canada generally must include in its income in a tax year the total of all amounts received as taxable dividends from other corporations resident in Canada. The terms **dividend** and **taxable dividend** will be used interchangeably for the remainder of the Chapter to describe a taxable dividend, unless otherwise indicated.

2.38 In computing its taxable income under Part I, a corporation may use subsection 112(1) to offset the income inclusion arising from a dividend. Specifically, subsection 112(1) allows a corporation to deduct an amount equal to the dividends it receives from taxable Canadian corporations, or from certain corporations resident in Canada that it controls. This results in tax-free intercorporate dividends. However, this intercorporate dividend deduction is denied where any of the anti-avoidance provisions and corresponding interpretative rules in subsections 112(2.1) to (2.9) apply. The deduction will also effectively be denied where a corporation receiving a tax-free intercorporate dividend is considered to have used the intercorporate dividend deduction in a manner that is contrary to the anti-avoidance provision in subsection 55(2).

2.39 As noted in ¶2.38, a private corporation will not be liable for Part I tax on an intercorporate dividend to the extent that it is deductible under section 112. However, the corporation may still be subject to a refundable tax on the dividend under subsection 186(1). This is often called **Part IV tax**. The concept of the refundable tax system is discussed in ¶2.35 and 2.36.

Taxable dividends received by an individual resident in Canada

2.40 Under paragraphs 82(1)(a) and (a.1), an individual resident in Canada generally must include in income in a tax year the total of all amounts received as dividends from corporations resident in Canada. The amount to be included is that part of the dividend that exceeds certain amounts that are considered to have been paid by the individual in the context of a **securities lending arrangement**, described in section 260.

2.41 In addition to the actual dividend received, the individual (other than a trust that is a registered charity) must calculate and include in income a dividend **gross-up** amount as described in paragraph 82(1)(b). This gross-up amount is intended to approximate the average combined federal and provincial or territorial corporate income taxes paid on the income that funded the payment of the dividend. The effect of the gross-up mechanism is that for purposes of calculating the Part I tax liability, an individual is treated as having earned directly the amount of the pre-tax corporate income that is presumed to have funded the payment of the dividend.

2.42 The gross-up amount is calculated by multiplying the actual dividend received by the applicable gross-up factor in paragraph 82(1)(b). The applicable gross-up factor is determined based on the tax year in which the dividend is included in income and the type of dividend that is received.

2.43 An individual is entitled to claim a non-refundable **dividend tax credit** under section 121. The credit is applied to reduce the individual's federal Part I tax liability. The dividend tax credit is intended to compensate the individual for corporate income tax (notionally determined by the gross-up amount) which is presumed to have been paid by the corporation on the income that funded the dividend.

2.44 The dividend tax credit is calculated by multiplying the gross-up amount by the applicable dividend tax credit rate set out in section 121. The applicable dividend tax credit rate is determined by the tax year in which the underlying dividend is included in income and the type of dividend that is received.

Provincial and territorial taxation

2.45 The dividend gross-up factors and the dividend tax credit rates are established based on the expected average combined federal and provincial or territorial corporate income tax rates. The actual combined corporate income tax rates tend to vary from this expected amount between jurisdictions. This can impact the operation of integration. However, in general terms, if the combined federal and provincial or territorial dividend tax credit for the jurisdiction where the recipient individual resides approximates the gross-up amount for that dividend, then the individual will be fully credited for the corporate income taxes that are presumed to have been paid. This means that integration will be achieved. Note that Quebec imposes and collects its own provincial income tax. Therefore, dividends received by a person resident in that province are taxable as required by Quebec law.

2.46 The dividend gross-up factors and the dividend tax credit rates are occasionally adjusted by federal and provincial or territorial governments to reflect changes to federal corporate income tax rates and ensure the appropriate tax treatment of dividend income.

Tax years prior to 2006 – taxable dividends

2.47 All taxable dividends received by an individual prior to 2006 were subject to the same dividend gross-up factor and the same dividend tax credit rate (the **ordinary** dividend gross-up and dividend tax credit). In general, the ordinary dividend gross-up and dividend tax credit mechanism was based on a combined federal and provincial or territorial corporate income tax rate. This provided integration for corporate income subject to preferential tax treatment namely:

- income from an active business that qualified for the small business deduction under subsection 125(1); and
- distributed investment income of a CCPC such as interest, dividends and capital gains.

Tax years after 2005 – eligible and non-eligible dividends

2.48 To improve integration and neutrality in the tax system, an enhanced dividend gross-up and enhanced dividend tax credit (the **enhanced** dividend gross-up and dividend tax credit) were introduced for qualifying dividends paid after 2005. This eligible dividend regime provides for two dividend gross-up factors and dividend tax credit rates to recognize the two different corporate income tax rates that generally apply to corporations.

2.49 In broad terms, the enhanced dividend gross-up and dividend tax credit apply to dividends distributed to an individual from corporate income taxed at the **general corporate income tax rate**, which is the rate applying to **full-rate taxable income** (defined in subsection 123.4(1)). These dividends are called eligible dividends.

2.50 The ordinary dividend gross-up and dividend tax credit continue to apply to dividends (non-eligible dividends) distributed to an individual from corporate income taxed at other than the general corporate income tax rate. This refers to income benefiting from preferential tax treatment as described in ¶2.47. For the remainder of the Chapter, the expression **preferential income tax rates** will be used in this regard.

Example 1

The following example illustrates the federal taxation of an eligible dividend and a non-eligible dividend received in 2021 by an individual who has a federal marginal tax rate of 33% (highest marginal rate).

Determining the dividend gross-up and dividend tax credit amounts

Description	Eligible dividend	Non-eligible dividend
Dividend received	$1,000.00	$1,000.00
Add: Gross-up	$380.00	$150.00
Taxable dividend	**$1,380.00**	**$1,150.00**
Federal income tax (33%)	$455.40	$379.50
Less: Dividend tax credit	($207.27)	($103.85)
Federal tax payable	**$248.13**	**$275.65**

Notes:

For the **eligible dividend**, the dividend gross-up (percentage of the dividend amount) is **38%** and the federal dividend tax credit (fraction of the gross-up amount) is **6/11**.

For the **non-eligible dividend**, the dividend gross-up (percentage of the dividend amount) is **15%** and the federal dividend tax credit (fraction of the gross-up amount) is **9/13**.

For purposes of the **dividend tax credit**, this example does not consider the tax implications associated with the application of the provincial or territorial portion of the dividend tax credit.

2.51 The dividend gross-up amount and the dividend tax credit are calculated based on the amount of the dividend received, before deducting any carrying charges. The T5 Statement of Investment Income information slip for a dividend recipient specifies, among other things, the taxable amount of dividends (including the gross-up amount) and the applicable dividend tax credit for eligible and non-eligible dividends.

Determination and designation of eligible dividends

General discussion of eligible dividends

2.52 A taxable dividend paid after 2005 by a corporation resident in Canada is characterized as either an eligible or non-eligible dividend.

2.53 In general terms, a taxable dividend is a non-eligible dividend unless the payor corporation designates it as an eligible dividend. A taxable dividend is an eligible dividend if it:

- meets the subsection 89(1) requirements to be an eligible dividend; and
- is properly designated as such in the manner required by subsection 89(14).

This is the case even if the corporation paying the dividend designates an amount in excess of the corporation's capacity to pay an eligible dividend. Such a designation is called an **excessive eligible dividend designation** and is defined in subsection 89(1). It should be noted that this comment does not take into account an election under subsection 185.1(2) to treat an excessive designation as a non-eligible dividend. The concept of an excessive eligible dividend designation and the corresponding rules are discussed in more detail under the heading Excessive eligible dividend designations. The expression **excessive designation** will be used interchangeably with the term **excessive eligible dividend designation** for the remainder of the Chapter.

2.54 An eligible dividend must be a taxable dividend. Therefore, capital dividends and capital gains dividends (within the meaning assigned by subsections 130.1(4) and 131(1)) cannot be designated as eligible dividends. Deemed dividends under section 84 or 84.1 are taxable dividends that can be eligible dividends, if they otherwise meet the requirements to be an eligible dividend and are properly designated.

2.55 In general terms, eligible dividends are paid by a corporation from income subject to tax at the general corporate income tax rate. A corporation's capacity to pay an eligible dividend depends largely on its corporate status as a CCPC, as a deposit insurance corporation as defined in subsection 89(15) (**DIC**), or as a corporation resident in Canada that is not a CCPC or a DIC (**non-CCPC**). In the remainder of this Chapter, a reference to a CCPC will include a reference to a DIC unless otherwise indicated and a reference to a non-CCPC means a corporation that is neither a CCPC nor a DIC.

2.56 A CCPC can pay eligible dividends in a given tax year without making an excessive designation, to the extent of its GRIP as calculated at the end of that year. This is the case because a CCPC will generally earn income benefiting from preferential income tax rates, which cannot be distributed as an eligible dividend. Accordingly, a CCPC must maintain a GRIP account to track income subject to the general corporate income tax rate, to distribute any such income as an eligible dividend. In addition to tracking income subject to the general corporate income tax rate, a CCPC's GRIP account generally includes eligible dividends received from other Canadian corporations and dividends received from foreign affiliates that have been deducted in computing taxable income. The computation of a corporation's GRIP is discussed in more detail under the heading Calculation of GRIP.

2.57 Conceptually, non-eligible dividends are paid by a corporation from income subject to preferential income tax rates. A non-CCPC can pay an eligible dividend at a particular time without making an excessive designation, to the extent that the corporation does not have a balance in its **LRIP** at the particular time that the dividend is paid. This includes a CCPC that files a subsection 89(11) election not to be treated as a CCPC. It is generally expected that a non-CCPC will earn income that has been subject to the general corporate income tax rate. This income can be distributed to its shareholders as an eligible dividend. This means that, unlike a CCPC, a non-CCPC must maintain an LRIP account to track its income that has benefited from preferential income tax rates. This ensures that this income is paid as a non-eligible dividend before the corporation can pay an eligible dividend. In broad terms, a corporation's LRIP includes corporate income that has been taxed at the small business rate (when it was a CCPC for example), plus any non-eligible dividends that the corporation has received. The calculation of a corporation's LRIP is discussed in more detail under the heading Calculation of LRIP.

Eligible dividend designation

2.58 Subsection 89(14) sets out the manner in which a corporation must designate a dividend or any portion of it to be an eligible dividend. At the time of payment, the corporation must provide written notice that a portion of the dividend is an eligible dividend. The notice must be provided to each person or partnership to whom the dividend is paid, including a non-resident.

2.59 For any dividend paid on or after March 29, 2012, a corporation may designate all or a portion of it to be an eligible dividend. Prior to that date, a designation to be an eligible dividend could only be made for the entire amount of a dividend.

2.60 The portion of a dividend that is designated as an eligible dividend payable by a CCPC to a non-resident shareholder will not be considered to be an eligible dividend for purposes of calculating the corporation's GRIP under subsection 89(1). Therefore, that portion of the dividend will not reduce the corporation's GRIP account. This is discussed further under the heading Impact on GRIP of an eligible dividend received by a non-resident shareholder.

2.61 Similarly, where a non-CCPC designates a taxable dividend as an eligible dividend, any portion that is payable to a non-resident shareholder will not be an eligible dividend for purposes of calculating the corporation's LRIP. As a result, that particular portion of the dividend will, under certain conditions, reduce the corporation's LRIP. This is discussed further under the heading Impact on LRIP of an eligible dividend received by a non-resident shareholder.

Notification of an eligible dividend designation

2.62 Generally, notification before or at the time a dividend is paid is appropriate notification of an eligible dividend designation under subsection 89(14). There is no ability to late file an eligible dividend designation for dividends paid before March 29, 2012. However, for dividends paid on or after March 29, 2012, subsection 89(14.1) permits a late-filed eligible dividend designation in specific circumstances. This is discussed further under the heading Late eligible dividend designations.

2.63 For public corporations, notification of the designation of an eligible dividend may be made in a statement by the corporation asserting that all dividends are eligible dividends unless indicated otherwise. This statement must be made before or at the time that the dividends are paid. It can be in a notice posted on the corporation's website, in its financial reports or in other shareholder publications. These notifications will be considered valid for a specific period of time depending upon the notification method used. For example, a notice posted on a corporation's website is valid for all dividends paid during that time until the notice is removed; a notice in an annual or quarterly report is valid for that year or quarter, respectively. Notification of a designation is also accepted where a corporation issues a press release announcing the declaration of a dividend and the designation of that dividend as an eligible dividend.

2.64 For all corporations other than public corporations (for example, CCPCs and other private corporations), notification of the designation of an eligible dividend must be made each time a dividend is paid. This notification may be made by identifying the eligible dividend in letters to shareholders, in dividend cheque stubs, or where all of the shareholders are also directors of the corporation, a notation in the corporate minutes. Except as specified in ¶2.66, the particular notice must identify the amount of the eligible dividend at the time the dividend is paid. It is not sufficient for the corporation to specify that the eligible dividend will not exceed the lesser of the balance of the shareholder's loan account or the corporation's GRIP. Similarly, it is not sufficient to state that the eligible dividends will not exceed the corporation's GRIP at the time of their payment.

2.65 In certain circumstances, notification of an eligible dividend designation may be made by sending email correspondence to the shareholders, with the required written notice included in the email or as an attached document such as a Portable Document Format file (PDF). Such notification is acceptable provided that the email is sent with an acknowledgment of receipt.

2.66 Under subsection 248(1), a **subsidiary wholly-owned corporation** is defined as a corporation whose shares are all owned by a parent corporation. In certain circumstances, such a corporation may notify its parent corporation of the designation of an eligible dividend in a directors' resolution of the subsidiary corporation. The notification will be valid where:

- the parent corporation is a public corporation or a corporation controlled by a public corporation; and
- it is delivered to the parent corporation on a timely basis.

The notification of a designation in a directors' resolution of the subsidiary corporation may also be valid where the members of the board of directors of the subsidiary and the parent corporations are the same. If this is the case, the parent corporation will generally be considered to be notified of the designation at the time that the resolution is signed by the board of directors.

2.67 Under subsection 84(3), a dividend is deemed to be paid on a redemption of the shares of a corporation's capital stock. Where a CCPC designates such a dividend to be an eligible dividend, the CRA will not require the corporation to provide a fixed amount for the dividend in certain circumstances. This can occur where the amount of the deemed dividend is incorrectly stated in the designation resulting, for example, from a miscalculation of the paid-up capital attributable to the shares redeemed. In this circumstance, the designation will be valid if:

- the other notification conditions in subsection 89(14) are satisfied;
- the designation specifies both the number and class of shares being redeemed; and
- the designation specifies that it is for a deemed dividend resulting from a share redemption under subsection 84(3).

Furthermore, the correct amount of the deemed dividend designated as an eligible dividend must not exceed the corporation's GRIP determined for the tax year in which the deemed dividend is paid. If it does, an excessive designation can result. In some cases, the designation might not refer to the number and class of shares being redeemed. In this situation, the designation may still be considered valid for the total amount of the deemed dividend provided that the designation can only be considered to relate to the deemed dividend resulting from the redemption.

2.68 An individual resident in Canada might be deemed by paragraph 84.1(1)(b) to have received a dividend from a corporation. Such a dividend may be designated as an eligible dividend under subsection 89(14). This will be the case even if the individual does not hold any shares of the capital stock of the corporation. In other words, for purposes of the definition of eligible dividend in subsection 89(1) and the designation requirements in subsection 89(14), an individual does not have to hold shares of any class of the capital stock of the corporation. Similarly, the deemed dividend paid and received under paragraph 84.1(1)(b) does not have to be paid by the corporation on shares of its capital stock.

Eligible dividends received by a corporation resident in Canada

2.69 An eligible dividend received by a CCPC is added to its GRIP under variable E of the definition of GRIP in subsection 89(1). This increases the amount of GRIP available to be designated as an eligible dividend payable to the corporation's shareholders. Notionally, an eligible dividend can retain its character through a chain of corporations, to eventually be distributed as an eligible dividend.

2.70 Under variable B of the definition of LRIP in subsection 89(1), a non-CCPC is only required to include non-eligible dividends in its LRIP. Such non-eligible dividends are typically received from a CCPC. The balance of a corporation's LRIP account must be paid out by the corporation as non-eligible dividends before the corporation is permitted to pay eligible dividends.

Eligible dividends received by a partnership

2.71 Each partner of a partnership is generally considered to receive a pro rata share of any dividends received by the partnership, based on the terms of the partnership agreement and the applicable law. Each partner's share of an eligible dividend received by a partnership is considered to be an eligible dividend received by the partner, provided the conditions in the definition of eligible dividend in subsection 89(1) are met. This includes the requirement that the partner be a person resident in Canada, which is discussed further in ¶2.73.

2.72 A corporation that pays a dividend to a partnership may designate a portion of that dividend to be an eligible dividend by providing written notice of the designation to the partnership (rather than each partner) at that time.

2.73 If a corporation determines that a portion of a dividend it paid to a partnership has been allocated by the partnership to, and received by, a partner who is a non-resident of Canada, that portion of the dividend will not be an eligible dividend. In other words, only the portion of the dividend allocated to and received by partners who are persons resident in Canada, will reduce the GRIP of the particular corporation at the appropriate time. This situation may occur where, for example, the corporation paying the dividend obtains evidence that Part XIII tax has been withheld from the dividend paid to the non-resident partner. The computation of GRIP is discussed in more detail under the heading Calculation of GRIP.

Eligible dividends received by a trust

2.74 The enhanced dividend gross-up and dividend tax credit are available to a trust in respect of a dividend received from a corporation resident in Canada if:

- the trust is resident in Canada, including a trust deemed to be resident in Canada for the purposes described in subparagraphs 94(3)(a)(ii) and (viii);
- the trust is not a registered charity; and
- the corporation designates the dividend as an eligible dividend under subsection 89(14).

2.75 In certain circumstances, subsection 104(19) permits a trust to designate a portion of a taxable dividend to have been received by a beneficiary of the trust from the corporation paying the dividend. The trust will be considered not to have received any portion of the dividend that is deemed to be received by the beneficiary. If the taxable dividend meets the requirements to qualify as an eligible dividend, then that dividend will maintain its character as an eligible dividend in the hands of a Canadian-resident beneficiary. Where the beneficiary is an individual, the amount of the deemed dividend and the applicable gross-up amount must be included in the individual's income. The individual is entitled to claim the dividend tax credit. The gross-up and dividend tax credit are described under the heading Taxable dividends received by an individual resident in Canada. Where the beneficiary is a corporation, it will normally be eligible for the intercorporate dividend deduction under subsection 112(1) as described in ¶2.38. The corporation may be subject to Part IV tax as described in ¶2.39. Interpretation Bulletin IT-524, Trusts – Flow-through of taxable dividends to a beneficiary – After 1987, comments on the subsection 104(19) designation.

Late eligible dividend designations

2.76 If a corporation failed to designate a taxable dividend paid prior to March 29, 2012 as an eligible dividend, there is no provision in the Act that allows the corporation to make a late eligible dividend designation. This is so even if the corporation had sufficient GRIP to support the designation. Furthermore, the subsection 89(14) designation is not one of the prescribed provisions listed in Regulation 600 for which the Minister of National Revenue (Minister) may allow an extension of time under subsection 220(3.2).

2.77 For taxable dividends paid **after** March 28, 2012, subsection 89(14.1) describes certain conditions under which a late designation of an eligible dividend (**late designation**) may be permitted. First, the corporation must make the late designation within the three-year period following the day on which the designation was required to be made under subsection 89(14). Second, the Minister must be of the opinion that it would be just and equitable in the circumstances to permit the designation to be made. In forming this opinion, the Minister will take into account the interests of affected shareholders and the extent to which the corporation had income taxed at the general corporate income tax rate when the dividend was paid.

2.78 A late designation under subsection 89(14.1) may be permitted where, for example:

- the taxpayer is faced with unintended tax consequences and there is evidence that the taxpayer took reasonable steps to comply with the law;
- the taxpayer's request arises from circumstances beyond the taxpayer's control; or
- the taxpayer was unaware of the designation (and can demonstrate as much) but the taxpayer took reasonable care to comply with the law and took action to remedy the situation as quickly as possible.

Example 2

After March 28, 2012, a public corporation receives a dividend from its subsidiary corporation. The dividend otherwise qualifies as an eligible dividend. The subsidiary corporation fails to properly designate the dividend as an eligible dividend as required by subsection 89(14).

The receipt of the dividend creates an LRIP balance for the public corporation, even though the dividend was paid from income of the subsidiary corporation that was taxed at the general corporate income tax rate.

In this situation, the public corporation is able to demonstrate that the creation of the LRIP balance is an unintended tax consequence that resulted from circumstances beyond its control. Accordingly, the Minister may approve a late designation.

2.79 To avoid the tax otherwise imposed under subsection 184(2), a corporation can make an election under subsection 184(3) to deem the excess portion of a capital dividend to be a separate taxable dividend. This separate taxable dividend will be deemed to have been payable at the time the original dividend was payable. If the corporation wishes to designate the taxable dividend to be an eligible dividend, the designation will be made after the time required under subsection 89(14). In these circumstances, it will generally be considered just and equitable to permit the late designation of the dividend, provided the requirements of subsection 89(14.1) and certain additional conditions have been met. These additional conditions are:

- the corporation had sufficient GRIP at the time the dividend was paid, such that no portion of the designated amount would be an excessive designation under subsection 89(1);

- the corporation took reasonable steps to compute the capital dividend account and comply with the requirements of subsection 83(2) at the time the dividend was paid;
- the late designation request under subsection 89(14.1) was not specifically intended by the corporation at the time the dividend was paid;
- the late designation request does not form part of a series of requests made on a regular basis; and
- the late designation request does not involve abusive tax planning.

2.80 If the CRA considers a corporation's business to be a personal services business as defined in subsection 125(7), the corporation will be denied a claim for the small business deduction. The corporation's income will then be subject to higher corporate income tax rates. This can result in an increase in the corporation's GRIP for the year reassessed. If this is the case, the corporation might wish to make a late eligible dividend designation. The late designation provision will generally apply in this situation, provided the requirements of subsection 89(14.1) and the following additional conditions are met:

- the corporation has sufficient GRIP at the time that the dividend is paid, such that no portion of the designated amount will be an excessive designation under subsection 89(1);
- the corporation carefully reviewed the rules governing the small business deduction and the definition of personal services business before completing the return of income and the corporation had a strong basis to conclude that it was entitled to the small business deduction;
- the corporation or its representatives have not shown carelessness in the application of the rules of the small business deduction under the circumstances; and
- the late designation request does not involve abusive tax planning.

2.81 In general terms, subsection 89(14.1) is not intended to apply to situations involving either retroactive or abusive tax planning. The late designation is also not permitted in the circumstance where a corporation makes an application for a late designation deliberately or on a regular basis. The CRA has not prepared detailed guidelines or a list of the specific circumstances where a request for a late designation will not be accepted. However, Example 3 illustrates a situation where a late designation would not be covered by subsection 89(14.1).

Example 3

A corporation pays dividends annually to a shareholder in cash, or by way of a decrease in the amount due to the corporation by the particular shareholder. The corporation does not make an eligible dividend designation under subsection 89(14) at the time of payment of the dividend because the corporation is not able to determine the amount of its GRIP account at that time.

In this case, the corporation would request a late designation on an annual basis. Accepting a late designation request in such a situation would, in effect, override the written and contemporaneous designation requirements of subsection 89(14).

2.81.1 A corporation may also make a late designation for a taxable dividend it has paid, but not previously designated as an eligible dividend, subject to the conditions described in subsection 89(14.2). These conditions are:

- the designation must be made as a consequence of the application of subparagraph (a)(iii) of the **eligible refundable dividend tax on hand (ERDTOH)** definition in subsection 129(4), which applies in respect of certain eligible dividends received during the transition to the ERDTOH regime;
- the corporation must make the late designation within the six-year period immediately following the day on which the designation was first required to be made; and
- the Minister must be of the opinion that accepting the late designation would be just and equitable in the circumstances.

2.82 Late designation requests must be submitted to the appropriate tax services office or tax centre. The determination of whether it would be just and equitable to permit such a designation in light of the facts and circumstances will be decided on a case-by-case basis by the person authorized to exercise the authority of the Minister. Requests must include the reasons why it would be just and equitable to permit the late designation. The dividend payment that is the subject of a late designation will be treated as a non-eligible dividend until such time as it is approved. If the Minister accepts a late designation request, the designation will be deemed to have been made at the time it was required to be made under subsection 89(14). There is no penalty tax applied to a late designation that is accepted by the Minister under subsections 89(14.1) or (14.2).

Excessive eligible dividend designations

2.83 The method of determining whether a corporation has made an excessive designation for an eligible dividend it paid at any time in a tax year depends in part on the status of the corporation.

Excessive designation by a CCPC

2.84 For a corporation that is a CCPC in the tax year, the amount, if any, of an excessive designation made by the corporation is determined by a two-part formula, **(A - B) × C/A**. The formula is in paragraph (a) of the definition of excessive eligible dividend designation in subsection 89(1). This formula applies unless paragraph (c) of the definition applies to the dividend. The first part of the formula, **(A - B)**, identifies the amount, if any, by which the total of all eligible dividends paid by the corporation in the tax year, exceeds the corporation's GRIP **at the end of that tax year**. For this purpose a negative GRIP balance is treated as nil. The second part of the formula, **C/A**, prorates the amount of any excessive designation among all of the eligible dividends paid by the corporation in the year, on an eligible dividend by eligible dividend basis.

2.85 As previously described, the determination of an excessive designation for a CCPC is based on its GRIP at the end of the tax year in which the dividend is paid. As a result, a CCPC may declare a taxable dividend and designate the dividend as an eligible dividend at any particular time in a tax year without incurring an excessive designation. This will be the case even if the corporation has no balance in its GRIP at that time, provided it has a sufficient GRIP at the end of that tax year.

Excessive designation by a non-CCPC

2.86 For a corporation that is not a CCPC in the tax year (a non-CCPC), the two-part formula, **A × B/C**, in paragraph (b) of the definition of excessive eligible dividend designation in subsection 89(1) is used to determine any excessive designation. This formula does not apply if paragraph (c) of the definition applies to the dividend. The first part of the formula, **A**, is the lesser of two amounts:

1. the aggregate of all eligible dividends paid by the corporation **at that time**; and
2. the corporation's LRIP **at that time**.

The second part of the formula, **B/C**, prorates the amount of any excess determined by **A** among all of the eligible dividends paid by the corporation at that time, on an eligible dividend by eligible dividend basis.

2.87 An excessive designation for a non-CCPC is determined based on the corporation's LRIP balance at the time that it pays a taxable dividend. This effectively introduces an ordering rule for non-CCPC corporations. To avoid the additional tax on an excessive designation, a non-CCPC must first pay a non-eligible dividend to the limit of its LRIP at the time it pays the dividend. This will bring LRIP to zero. If a non-CCPC does not have LRIP at any particular time in its tax year it may pay eligible dividends without restriction, subject to the application of the anti-avoidance rule in paragraph (c) of the definition of excessive eligible dividend designation (described in ¶2.88).

Excessive designation anti-avoidance rule

2.88 Paragraph (c) of the definition of excessive eligible dividend designation in subsection 89(1) is an anti-avoidance rule. Under this rule, the amount of the excessive designation will be equal to the entire amount of the eligible dividend. This anti-avoidance rule applies if it is reasonable to consider that an eligible dividend was paid in a transaction, or as part of a series of transactions, and one of the main purposes was:

- to artificially maintain or increase a corporation's GRIP; or
- to artificially maintain or decrease a corporation's LRIP.

This rule can apply regardless of whether paragraph (a) or (b) (described in ¶2.84 and ¶2.86 respectively) would otherwise apply.

2.89 What might indicate that a CCPC has artificially maintained or increased its GRIP? Generally, an increase in the GRIP of a CCPC will be considered artificial if the transaction or series of transactions produces a GRIP that does not reflect the corporation's retained income after the payment of Part I tax at a rate that is **not less than** the general corporate income tax rate. In other words, an increase in the GRIP of a CCPC will generally be considered artificial if the underlying earnings upon which the dividend is based were not subject to Part I tax at this rate. These comments apply regardless of whether the tax is paid by the corporation or another corporation.

2.90 Similar factors will indicate that a non-CCPC has artificially maintained or decreased its LRIP. Specifically, the anti-avoidance rule will apply if the transaction or series of transactions produces an LRIP that does not reflect the corporation's retained income after payment of Part I tax at a rate that **is less than** the general corporate income tax rate (preferential income tax rates). These comments apply whether the tax is paid by the corporation or another corporation.

2.91 Examples 4 and 5 demonstrate situations in which the application of the anti-avoidance rule in paragraph (c) of the definition of excessive designation would be considered.

Example 4

A public corporation introduces a shareholder into its capital structure. The shareholder is indifferent to receiving eligible dividends. Any non-eligible dividend paid to this shareholder by the corporation would reduce the corporation's LRIP. In turn, this would allow the corporation to pay eligible dividends to its other shareholders. This would effectively stream the corporation's LRIP.

Although the eligible dividend rules contemplate that a corporation can choose which of its shareholders will receive eligible dividends, the corporation may be considered to have artificially reduced its LRIP depending upon the circumstances surrounding the payment of a particular dividend. Such circumstances might include the shareholder's identity, the conditions for redemption or cancellation of the shares, and financing issues.

Example 5

Subco is a subsidiary wholly-owned corporation of a public corporation, Pubco. Subco has an LRIP derived from income that has been taxed at preferential income tax rates. Through a transaction or series of transactions, this LRIP is isolated or parked in Parkco, a corporation designated for this purpose. This could be accomplished in part by Subco paying non-eligible dividends to Parkco to the extent of its LRIP. This allows Subco to pay eligible dividends to Pubco. Pubco then pays eligible dividends to its shareholders.

In this situation, Subco’s LRIP, and in turn Pubco’s LRIP, could be considered to have been artificially reduced in such a manner that it does not properly reflect the income in Subco that has been taxed at preferential income tax rates. Arguably, one of the main purposes of the series of transactions could be to allow Pubco to pay its shareholders eligible dividends. In the absence of the transactions, Pubco would have been required to first pay its shareholders non-eligible dividends to the extent of the LRIP that would have been created had Pubco received non-eligible dividends from Subco.

Application of GAAR

2.92 As is described in Example 5, an LRIP balance might be postponed indefinitely or permanently isolated in a corporation with no assets (effectively a shell corporation). In such circumstances, the underlying tax policy of the eligible dividend regime may be considered to be circumvented in a manner that is contrary to the object and spirit of the rules of this regime and the principle of integration. If it is determined that the excessive designation provisions would not apply in such a situation, the application of the **general anti-avoidance rule (GAAR)** in subsection 245(2) may also be considered. GAAR can apply to transactions undertaken to avoid the application of a specific anti-avoidance rule, such as paragraph (c) of the definition of excessive eligible dividend designation.

Tax on excessive designations

2.93 Excessive designations are subject to tax under paragraph 185.1(1)(a) of Part III.1. Specifically, a corporation that has made an excessive designation for an eligible dividend it paid at any time in a tax year must pay tax equal to 20% of the excessive designation. The tax is due on or before the corporation’s balance-due date for the tax year. This additional tax is intended to eliminate the tax benefit associated with the payment of eligible dividends. However, the dividend recipient can continue to treat the dividend as an eligible dividend.

2.94 Where the anti-avoidance provision in paragraph (c) of the definition of excessive eligible dividend designation applies to a dividend paid by a corporation, the corporation must pay an increased penalty tax under paragraph 185.1(1)(b). In this case, the total amount of tax payable is equal to 30% of the entire amount of the eligible dividend. As described in ¶2.93, the dividend recipient can continue to treat the dividend as an eligible dividend.

2.95 A corporation resident in Canada that pays a taxable dividend (other than a capital gains dividend) in a tax year must file a return for the year under Part III.1, as set out in subsection 185.2(1). The return must be in prescribed form, which is T2SCH55, Part III.1 Tax on Excessive Eligible Dividend Designations (2006 and later years). It must include an estimate of the corporation's Part III.1 tax payable for the year The return must be filed no later than the corporation's filing-due date for the year.

2.96 Subsection 185.2(3) applies when a CCPC makes an excessive designation for an eligible dividend paid to a non-arm's length shareholder. In this situation, the shareholder is jointly and severally, or solidarily, liable with the corporation for a proportionate share of the corporation's Part III.1 tax. The shareholder's proportion of the corporation's tax for this purpose is equal to the proportion of the eligible dividend that the shareholder received.

2.97 The treatment of a payment on account of a liability described in subsection 185.2(3) in respect of a particular excessive designation is determined under subsection 185.2(5). If a shareholder makes the payment, the payment will discharge the liability to the extent of the payment. If the corporation makes the payment, the payment discharges a proportionate amount of the liability of each shareholder who received the eligible dividend in question.

Election to treat excessive designation as a non-eligible dividend

2.98 Where a corporation has made an excessive designation for an eligible dividend (the **original dividend**), there is an alternative to paying tax under subsection 185.1(1). The corporation may elect under subsection 185.1(2) for a portion of the original dividend, up to the full amount of the excessive designation, to be treated as a separate taxable dividend that is a non-eligible dividend. The election allows a corporation that would otherwise be subject to Part III.1 tax on an excessive designation, to instead have all or part of the excessive designation subject to tax under Part I as a non-eligible dividend. ¶2.102 to 2.104 describe the tax treatment resulting from such an election.

2.99 An election under subsection 185.1(2) is only valid if:

- the increased penalty tax in paragraph 185.1(1)(b) does not apply to the excessive designation;
- the corporation and every shareholder who received or was entitled to receive all or any portion of the original dividend and whose address was known to the corporation (except as specified in ¶2.100 or 2.101), consent to the election; and
- the corporation makes the election in prescribed manner, on or before the day that is 90 days after the day the notice of assessment for Part III.1 tax was sent for the particular dividend.

2.100 Subparagraph 185.1(3)(b)(ii) applies where a subsection 185.1(2) election is made more than 30 months after the original dividend was paid. This provision requires that all of the shareholders who received or were entitled to receive the original dividend consent to the election. This is the case regardless of whether the corporation knew their addresses. In this situation, subsections 152(4) to (5) will not prevent any assessment of tax, interest and penalties payable by those shareholders for any tax year that may be necessary based on the corporation's election.

2.101 Subsection 185.1(4) provides that shareholder consent to a subsection 185.1(2) election is not required where all of the shareholders who are treated as having received a dividend at a particular time because of the election, are exempt from tax under Part I at that time. This will only be the case if the election is made on or before the day that is 30 months after the day the original dividend was paid.

2.102 The general effect of an election under subsection 185.1(2) is that the corporation is treated as having paid, immediately before the original dividend, a non-eligible dividend equal to the amount specified in the election. The balance of the original dividend (the original dividend less the amount specified in the election) is treated as an eligible dividend.

2.103 With the consent of its shareholders, the corporation making the election can decide how much of the original dividend will still be treated as an eligible dividend. If the corporation decides not to have the entire amount of the excessive designation treated as a non-eligible dividend, the remaining portion will continue to be treated as an excessive designation subject to the 20% tax payable by the corporation.

2.104 The shareholders who held shares on which the corporation paid the original dividend are treated as having received their pro rata portion of the non-eligible dividend and any eligible dividend that the corporation is considered to have paid.

2.105 An election under subsection 185.1(2) must be made in the manner prescribed by the Minister. In general terms, the corporation must send a signed letter to its tax centre stating that the corporation elects under subsection 185.1(2) for the particular dividend. The letter must be accompanied by certain documents to support the election. For more details, see the CRA web page Election to treat excessive eligible dividend designations as ordinary dividends.

2.106 An election cannot be filed outside the time period set out in subsection 185.1(2), regardless of the status of any appeal to the notice of assessment for Part III.1 tax. This is the case because the subsection 185.1(2) election is not one of the prescribed elections listed in Regulation 600 for which a late-filed election may be accepted by the Minister under subsection 220(3.2).

Determination of income pools – GRIP and LRIP

Calculation of GRIP

2.107 GRIP is relevant for determining the extent to which a corporation can pay eligible dividends in a tax year without making an excessive designation. It is defined in subsection 89(1) and the calculation applies to tax years that end after 2005. In general terms, GRIP is a cumulative balance calculated based on the corporation's income subject to tax at the general corporate tax rate. More specifically, a corporation that is a CCPC (as described in ¶2.55, a reference to a CCPC includes a reference to a DIC unless otherwise indicated) in a particular tax year calculates its GRIP at the end of that tax year. It is the positive or negative amount determined by the following formula:

A – B

2.108 In broad terms, the formula represents the corporation's GRIP at the end of the tax year (variable A) less an amount representing specified future tax consequences (variable B), which are defined in subsection 248(1).

Variable A

2.109 Variable A can be a positive or negative amount and is determined by its own formula:

C + D + E + F – G where:

C = the positive or negative balance of the corporation's GRIP at the end of the preceding tax year. A corporation may have an opening balance for its 2006 tax year, representing its income for tax years ending after 2000 and before 2006. This opening balance, which is calculated under subsection 89(7), is described under the heading GRIP addition for 2006

D = the product, if any, of the general rate factor for the particular tax year multiplied by the corporation's adjusted taxable income. The **general rate factor**, defined in subsection 89(1), is used to calculate an amount equal to the after-tax earnings of the corporation. It is based on a notional combined federal and provincial or territorial general corporate income tax rate. The **adjusted taxable income** for a CCPC (not including a DIC) is defined in subsection 89(1). It is generally equal to the corporation's taxable income for the tax year less income benefiting from the small business deduction for the tax year. The taxable income is also reduced by that portion of the corporation's aggregate investment income, defined in subsection 129(4), that does not exceed its taxable income for the year. Where the corporation is a DIC, the adjusted taxable income will be nil

E = the sum of eligible dividends received by the corporation in the particular tax year and amounts deductible by the corporation under section 113 for dividends received from a foreign affiliate in the particular tax year

F = certain amounts resulting from corporate changes, such as amalgamations and windings-up, as determined under subsections 89(4) to (6). This is discussed further under the headings Becoming a CCPC and GRIP additions: post-amalgamation or post-winding-up

G = the total amount of eligible dividends paid in the preceding tax year, in excess of any excessive designations that the corporation made on those eligible dividends. However, the amount for G is nil where the corporation becomes a CCPC in a tax year in such a way that subsection 89(4) applies. The application of subsection 89(4) is discussed further under the heading Becoming a CCPC.

Proposed legislative change

On August 9, 2022, the Department of Finance released proposed legislative amendments to the Income Tax Act relating to the 2022 Federal Budget announcement to align the taxation of investment income earned by CCPCs. The legislative proposals include amendments to eliminate the tax-deferral advantage available to CCPCs and their shareholders earning investment income through controlled foreign affiliates.

Paragraph (b) of variable E is amended to add subparagraph (i), applicable to CCPCs, and subparagraph (ii), applicable to deposit insurance corporations. More specifically, the amendments exclude the following amounts from GRIP:

- for a CCPC, amounts deductible under paragraphs 113(1)(a.1), (b) and (c); and
- for a deposit insurance corporation, the amount of foreign withholding tax paid with respect to a dividend deductible under section 113.

This measure will apply to tax years that begin after April 6, 2022.

Variable E is further amended to exclude from subparagraphs (b)(i) and (ii) amounts deductible under paragraph 113(1)(d) or subsection 113(2).

This measure will apply to tax years that begin after August 8, 2022.

Variable B - Impact on GRIP of specified future tax consequences

2.110 The preceding GRIP amount (variable A of the definition of GRIP) is reduced at the end of the tax year by variable B. Variable B represents the amount of any **specified future tax consequence** that, in any of the corporation's three preceding tax years, reduced its taxable income that was subject to the general corporate income tax rate. Specified future tax consequence is defined in subsection 248(1) and includes certain losses, tax credits and other similar amounts incurred or realized in the current tax year.

2.111 More specifically, variable B is determined by the formula:

H × (I - J) where:

H = the general rate factor for the particular tax year

I = the total of the corporation's full-rate taxable income (defined in subsection 123.4(1)) for its three preceding tax years, before considering the impact in those years of any specified future tax consequences that relate to the particular tax year

J = the total of the corporation's full rate taxable income for those three preceding tax years, after considering the impact of any specified future tax consequences for those years.

For the purposes of this calculation, the full rate taxable income amount is not reduced by any of the amounts specified in subparagraphs 123.4(1)(a)(i) to (iii).

2.112 An example of a specified future income tax consequence is a non-capital loss carryback—an amount referred to in paragraph 161(7)(a). Paragraph 111(1)(a) allows a corporation to carry back a non-capital loss incurred in a particular tax year to a preceding tax year to reduce its income in that year. In this situation, the corporation will reduce its GRIP in the particular tax year in which the loss is incurred or sustained. The amount of the reduction to its GRIP will generally be equal to the after-tax amount of the applied loss carryback in accordance with variable B of the definition of GRIP. The loss carryback will not affect the corporation's GRIP for the tax year to which the loss is applied. However, the application of the non-capital loss which reduces the corporation's GRIP for a particular tax year can result in a negative GRIP for the corporation for that year.

2.113 On the other hand, a corporation may carry forward a non-capital loss to a particular tax year under subsection 111(1). The loss is deducted in calculating the corporation's taxable income in that particular year. The non-capital loss therefore impacts the adjusted taxable income and GRIP of a corporation in the particular year that the loss is applied and not in the year that it was incurred.

Impact on GRIP of an eligible dividend received by a non-resident shareholder

2.114 There is no reduction of a CCPC's GRIP for the portion of a dividend that is designated as an eligible dividend and that is received by a non-resident shareholder. This is the case because GRIP is reduced by the total amount of all eligible dividends paid by a corporation (under subparagraph (a)(i) of variable G). Any portion paid to a non-resident shareholder is not received by a person resident in Canada and, therefore, is not an eligible dividend under subsection 89(1).

GRIP addition for 2006

2.115 A CCPC whose first tax year includes January 1, 2006 may include in its GRIP for that first tax year an amount for its GRIP at the end of its immediately preceding tax year. This is the case provided the corporation was a CCPC throughout this first tax year. The GRIP addition for 2006 is also available to a corporation that would have been a CCPC if it had not made a subsection 89(11) election. It is not available to a DIC. In effect, this GRIP addition represents the corporation's opening GRIP, based on its taxable income for the tax years ending after 2000 and before 2006. These tax years are described collectively as **the transition period** in this discussion.

2.116 The GRIP addition is determined by the formula **A – B** in subsection 89(7). Because the result of the formula cannot be less than nil, the GRIP addition will not reduce the corporation's GRIP for its first tax year. In broad terms, paragraphs (a) and (b) of variable A approximate the after-tax amount of the corporation's full-rate taxable income for the transition period. This calculation is made:

- using a notional combined federal and provincial or territorial corporate rate of tax of 37%;
- allowing for certain modifications depending on the tax year in question; and
- without taking into consideration the specified future income tax consequences for those tax years.

2.117 Dividends received by the corporation in the transition period are generally not included in the GRIP addition calculation. Under paragraph (c) of variable A, an exception is available where:

- the corporation receives a dividend that is deductible under subsection 112(1) and is from a connected corporation (within the meaning assigned by subsection 186(4)); and
- the dividend may reasonably be considered to be attributable to the payor corporation's after-tax full-rate taxable income that was earned during the transition period (described in ¶2.116).

2.118 In the GRIP addition calculation, variable A is reduced by variable B. Variable B represents the total of all taxable dividends paid by the corporation during the transition period, even if such dividends are not attributable to full-rate taxable income of the corporation in those tax years.

2.119 The GRIP addition for a CCPC's first tax year was intended to provide the corporation with an opening GRIP balance from which it could pay eligible dividends as of January 1, 2006. However, the GRIP addition of a CCPC is calculated for a tax year for which the reassessment period under section 152 has generally passed (referred to as statute-barred). Even so, the calculation of this amount might be relevant to such a CCPC. Specifically, the GRIP addition might be carried forward in a CCPC's GRIP balance to subsequent tax years. Accordingly, this GRIP addition may impact the determination of whether the CCPC has made an excessive designation in a tax year that is not statute-barred.

Calculation of LRIP

2.120 LRIP is relevant for determining the extent to which a corporation can pay eligible dividends in a tax year without making an excessive designation. In general terms, LRIP is a running balance that is calculated based on the corporation's income that is subject to preferential income tax rates. It cannot be a negative amount. LRIP is calculated at any particular time in a tax year for a corporation that is resident in Canada and is a non-CCPC in the particular year. As described in ¶2.55, the term non-CCPC is used in this Chapter to describe a corporation that is neither a CCPC nor a DIC.

2.121 More specifically, under the definition of LRIP in subsection 89(1), the LRIP of a non-CCPC in a particular tax year is the amount determined by the formula:

(A + B + C + D + E + F) – (G + H) where:

A = the balance of the corporation's LRIP at the end of the preceding tax year. This amount is already adjusted for non-eligible dividends paid, and excessive designations made, by the non-CCPC in the preceding tax year

B = the total of all amounts deductible under section 112 in computing the non-CCPC's taxable income for the year in respect of a non-eligible dividend that became payable, in the particular tax year but before the particular time, to the non-CCPC by a corporation resident in Canada. This amount will typically include dividends paid to the non-CCPC by a CCPC

C = the total of all amounts determined under subsections 89(8) to (10). These subsections describe certain LRIP additions resulting from corporate changes such as amalgamations and windings-up. This is discussed further under the headings Ceasing to be a CCPC and LRIP additions: post-amalgamation or post-winding-up

D = 80% of the non-CCPC's aggregate investment income for its preceding tax year, where the non-CCPC was a substantive CCPC (defined in subsection 248(1)) at any time in its preceding tax year or would have been a CCPC in that year, if it had not made an election under subsection 89(11) to cease to be a CCPC. The subsection 89(11) election to cease being treated as a CCPC is discussed under the heading Election not to be treated as a CCPC

E = 80% of any of the non-CCPC's taxable income that was reduced in its preceding tax year by the small business deduction, where the non-CCPC was not a CCPC in that preceding tax year. Variable E is relevant only to a non-CCPC that was a credit union in a preceding tax year and that claimed the small business deduction. Under subsection 137(7) a credit union is considered to be a private corporation for limited purposes including the small business deduction. Variable E also applies to any claim by the credit union for an additional deduction under subsection 137(3). Subsection 137(3) allows a credit union a deduction for amounts in excess of the small business deduction, for any days in its tax year that occur before 2017. Such amounts are considered deductible under the small business deduction rules by the application of subsection 137(4). However, the deduction under subsection 137(3) is being phased out and will no longer be relevant for tax years that are after 2016

F = four times any amount deducted by the non-CCPC under subsection 130(1) for its preceding taxation year, where the non-CCPC was an investment corporation in that preceding tax year. Variable F is generally equal to 80% of the non-CCPC's taxable income in excess of its taxed capital gains in that year

G = the total of all non-eligible dividends that became payable by the non-CCPC

(a) in the particular year but before the particular time or

(b) in the preceding tax year, but only to the extent of the lesser of (i) the amount included under variable D in the particular tax year, and (ii) the portion of the taxable dividend that did not reduce the non-CCPC's LRIP in the preceding tax year. The following amounts are not included under variable G:

- any capital gains dividends within the meaning of subsection 130.1(4) or 131(1)—applicable to a mortgage investment corporation and a mutual fund corporation, respectively; or
- any taxable dividends deductible by the non-CCPC under subsection 130.1(1) in computing its income for the particular tax year or its preceding tax year—applicable to a mortgage investment corporation

H = the total of any excessive designations made by the non-CCPC in the particular tax year but before the particular time.

Variables G and H reduce a non-CCPC's LRIP.

2.122 The calculation of LRIP applies for tax years that end after 2005. Unlike the GRIP addition, there is no requirement for a non-CCPC to calculate an opening LRIP for its first tax year that includes any part of January 1, 2006. However, in general terms, an opening LRIP must be calculated under subsection 89(8) where a corporation either ceases to be a CCPC, or makes an election not to be treated as a CCPC under subsection 89(11).

Impact on LRIP of an eligible dividend received by a non-resident shareholder

2.123 Where a non-CCPC designates a taxable dividend to be an eligible dividend and a portion of the dividend is paid to and received by a non-resident shareholder, that portion of the dividend will be a taxable dividend that is not an eligible dividend. If, as a matter of law, the taxable dividend becomes payable in the particular tax year but before it is paid, that portion will be an amount described in variable G of the definition of LRIP in subsection 89(1). This amount will be deductible in computing the non-CCPC’s LRIP at any particular time in the tax year, after the dividend become payable. If transactions are undertaken to artificially manipulate a corporation’s LRIP, paragraph (c) of the definition of excessive eligible dividend designation in subsection 89(1) or the GAAR in subsection 245(2) may apply.

Corporate changes – adjustment to GRIP and LRIP

Changes in corporate status

Becoming a CCPC

2.124 When calculating the GRIP of a CCPC, variable F of the formula includes certain amounts resulting from corporate changes. So, where a corporation is a CCPC in a particular tax year but was a non-CCPC in its preceding tax year, an amount determined under subsection 89(4) may be included in computing its GRIP at the end of the particular tax year.

2.125 The amount included under subsection 89(4) is determined by the formula:

A + B + C – D – E – F – G – H where:

A = the cost amount to the corporation of all of its property immediately before the end of its preceding tax year

B = any money on hand in the corporation immediately before the end of its preceding tax year

C = the amount, if any, of the corporation’s unused and unexpired losses deductible under subsection 111(1) at the end of its preceding tax year

D = the total of all amounts each of which is the amount of any debt owing by the corporation, or of any other obligation of the corporation to pay any amount, that was outstanding immediately before the end of its preceding tax year

E = the paid-up capital, immediately before the end of its preceding tax year, of all the issued and outstanding shares of the capital stock of the corporation

F = the total of all reserves deducted by the corporation in its preceding tax year

G = the capital dividend account of the corporation, if any, immediately before the end of its preceding tax year

H = the LRIP of the corporation immediately before the end of its preceding tax year.

As can be seen, variables A, B and C of the formula increase the amount that will be included in the corporation's GRIP. Variables D to H of the formula reduce the amount that will be included in the corporation's GRIP.

2.126 The formula in subsection 89(4) is based on a tax-balance-sheet approach. In broad terms, it is intended to calculate an amount representing a corporation's after-tax income that was subject to the general corporate income tax rate. This calculation is necessary in order to determine what the corporation's GRIP would have been at the end of its preceding tax year, had it been a CCPC in that tax year. Subsection 89(4) applies to tax years that end after 2005. However, a corporation is not required to calculate a GRIP balance on becoming a CCPC, though it can be advantageous to do so.

2.127 For tax years ending after 2005, subsection 249(3.1) provides that a corporation that becomes a CCPC is deemed to have a tax year-end immediately before the time that it became a CCPC. Further, a new tax year of the corporation is deemed to begin at that time. This subsection does not apply to:

- a corporation that becomes a CCPC because of an acquisition of control to which subsection 249(4) applies; or
- a DIC.

Similarly, where a corporation becomes a CCPC because of an acquisition of control under subsection 249(4), it will be deemed to have a tax year-end of the corporation immediately before the time that control is acquired.

Ceasing to be a CCPC

2.128 When calculating the LRIP of a non-CCPC, variable C of the formula includes certain amounts resulting from corporate changes. So, where a corporation is not a CCPC in a particular tax year but was a CCPC in its preceding tax year, any amount determined under subsection 89(8) must be included in computing its LRIP at any time in the particular tax year.

2.129 The amount included under subsection 89(8) for a corporation that ceases to be a CCPC in a particular tax year is determined by the formula:

A + B + C – D – E – F – G – H where:

A = the cost amount to the corporation of all of its property immediately before the end of its preceding tax year

B = any money on hand in the corporation immediately before the end of its preceding tax year

C = the amount, if any, of the corporation's unused and unexpired losses deductible under subsection 111(1) at the end of its preceding tax year

D = the total of all debt owing by the corporation, or of any other obligation of the corporation to pay any amount, that was outstanding immediately before the end of its preceding tax year

E = the paid-up capital of all the issued and outstanding shares of the capital stock of the corporation immediately before the end of its preceding tax year

F = the total of all reserves deducted by the corporation in its preceding tax year

G = the capital dividend account, if any, of the corporation immediately before the end of its preceding tax year, unless the corporation is a private corporation in the particular tax year, in which case the amount for G is nil

H = the positive or negative amount determined by the formula **I – J**, where **I** is the corporation's GRIP at the end of its preceding tax year and **J** is the total amount, if any, of all eligible dividends paid by the corporation in that year minus all excessive designations made by the corporation in that year.

As can be seen, variables A, B, and C of the formula increase the amount that will be included in the corporation's LRIP. Variables D to H of the formula reduce the amount that will be included in of the corporation's LRIP.

2.130 Similar to the determination of the GRIP addition under subsection 89(4), the formula in subsection 89(8) is based on a tax-balance-sheet approach. It calculates an amount representing a corporation’s after-tax income that benefitted from preferential tax rates. The purpose of the formula is to determine what the corporation's LRIP would have been at the end of its preceding tax year, had it not been a CCPC in that tax year. A corporation that ceases to be a CCPC is required to calculate an opening LRIP balance under subsection 89(8) for tax years that end after 2005.

2.131 For tax years ending after 2005, subsection 249(3.1) provides that a corporation that ceases to be a CCPC is deemed to have a tax year-end immediately before the time that it became a non-CCPC. Further, a new tax year of the corporation is deemed to begin at that time. This subsection does not apply to:

- a corporation that becomes a non-CCPC because of an acquisition of control to which subsection 249(4) applies; or
- a DIC.

Similarly, where a corporation ceases to be a CCPC because of an acquisition of control under subsection 249(4), it will be deemed to have a tax year-end of the corporation immediately before the time that control is acquired.

Election not to be treated as a CCPC

2.132 A corporation that is a CCPC (but not a DIC) may file an election under subsection 89(11) to be deemed not to be a CCPC. The election applies only for the purposes described in paragraph (d) of the definition of CCPC in subsection 125(7). If the election is filed with the Minister in prescribed form on or before the corporation’s filing-due date for a particular tax year that ends after 2005, the corporation will be deemed not to be a CCPC at any time in or after the particular tax year. In other words, the corporation will cease to be a CCPC at the beginning of the particular tax year and after.

2.133 A corporation that makes the election not to be treated as a CCPC will generally be considered to be a non-CCPC for purposes of the eligible dividend regime. More specifically, from the time that the corporation ceases to be treated as a CCPC the corporation’s capacity to pay eligible dividends will be determined by the calculation of LRIP rather than GRIP. Provided the corporation ceases to be a CCPC as described in subsection 89(8), the corporation will also be required to determine an amount for its LRIP as at the beginning of the tax year in which the election is effective. As a result of making the election the corporation will no longer be eligible to claim the small business deduction under subsection 125(1). However, the corporation will continue to be eligible for certain other CCPC benefits, such as the capital dividend account and refundable tax on investment income.

2.134 A corporation’s subsection 89(11) election must be considered in order to determine if a corporation becomes or ceases to be a CCPC for purposes of subsection 249(3.1). The tax implications of subsection 249(3.1) where a corporation becomes or ceases to be a CCPC are discussed in ¶2.127 and ¶2.131, respectively.

Example 6

Two public corporations, Pubco 1 and Pubco 2, become the owners of more than 50% of the voting common shares of the capital stock of Corporation X. Corporation X previously made an election under subsection 89(11).

Subsection 249(3.1) will not apply to deem Corporation X to become or cease to be a CCPC. This is the case because by virtue of its previous subsection 89(11) election, the corporation would already be deemed not to be a CCPC for the purposes of subsection 249(3.1).

Consequently, subsection 249(3.1) would not apply to trigger a deemed year-end. However, the loss-restriction provisions in, among others, subsections 111(4) to 111(5.5), 249(4) and 251.2(2) could apply in this circumstance.

2.135 On the other hand, subsection 249(3.1) will not be considered to apply at the time a corporation files an election under subsection 89(11). When it makes such an election, the corporation becomes a non-CCPC as of the beginning of the tax year in which the election is made. This means that it will not be considered to cease being a CCPC at a particular time for the purposes of subsection 249(3.1). Consequently, the fact that the corporation files a subsection 89(11) election will not, in and of itself, trigger a deemed year-end under subsection 249(3.1).

2.136 An election made under subsection 89(11) may be revoked under subsection 89(12). To do so, the corporation must file a notice in prescribed form revoking the election. The notice must be filed with the Minister on or before the corporation's filing-due date for a particular tax year. If the election is revoked, it will cease to apply to the corporation at the end of the particular tax year. This means that a corporation that revokes its subsection 89(11) election will no longer be deemed **not** to be a CCPC as of the beginning of the tax year following the particular tax year. However, the revocation of the subsection 89(11) election will not cause the corporation to be regarded as having become a CCPC at a particular time for the purposes of subsection 249(3.1). It will not, in and of itself, trigger a deemed year-end under subsection 249(3.1).

2.137 Subsection 89(13) provides that if a corporation has revoked an election under subsection 89(12), any subsequent election under subsection 89(11) or revocation under subsection 89(12) requires the Minister's consent in writing. The corporation will also be required to comply with any conditions imposed by the Minister.

2.138 Subsections 89(11) and (12) are not included in the list of prescribed provisions in Regulation 600. This means that the Minister cannot extend the time to make or revoke a subsection 89(11) election under the authority of subsection 220(3.2).

Amalgamations and windings-up

GRIP additions: post-amalgamation or post-winding-up

Amalgamation – corporation formed is a CCPC

2.139 An amalgamation under subsection 87(1) might result in the creation of a corporation that is a CCPC (the **amalgamated corporation**). In such a case, the amalgamated corporation's GRIP at the end of its first tax year will include the total of all amounts determined under subsection 89(5) for its predecessor corporations. This amount is included under variable F of the definition of GRIP in subsection 89(1). The calculation of the post-amalgamation GRIP addition in subsection 89(5) applies to tax years that end after 2005.

2.140 Paragraph 89(5)(a) specifies the amount to be included in an amalgamated corporation's GRIP with respect to a predecessor corporation that was a CCPC in the tax year that ended immediately before the amalgamation (the **last tax year**). Specifically, the amount flowed through to the amalgamated corporation's GRIP is the positive or negative amount determined by the formula:

A – B where:

A = the predecessor corporation’s GRIP determined at the end of its last tax year

B = the amount, if any, of all eligible dividends paid in excess of all excessive designations made by the predecessor corporation in that last tax year.

2.141 If the predecessor corporation was a non-CCPC in its last tax year, then paragraph 89(5)(b) specifies that the amount to be included in the amalgamated corporation's GRIP is determined by the formula:

A + B + C – D – E – F – G – H

This formula is based on a tax-balance-sheet approach. It is intended to determine what the predecessor corporation's GRIP would have been at the end of its last tax year had it been a CCPC in that year. This amount cannot be negative, unlike the amount determined for a CCPC predecessor under paragraph 89(5)(a).

2.142 The calculation of GRIP in paragraph 89(5)(b) is similar to the subsection 89(4) GRIP calculation for a corporation that becomes a CCPC. For a detailed description of the operation of this formula, see Becoming a CCPC, but to apply paragraph 89(5)(b), read the terms **corporation** and **preceding tax year** as **predecessor corporation** and **last tax year**, respectively.

Winding-up – parent corporation is a CCPC

2.143 A CCPC (the **parent corporation**) might wind-up a subsidiary corporation under subsection 88(1). In this situation, an amount determined under subsection 89(6) for the subsidiary corporation must be included in the parent corporation’s GRIP. This occurs at the end of the parent corporation’s tax year that immediately follows the tax year during which it receives the assets of the subsidiary corporation on the winding-up. This amount is included under variable F of the definition of GRIP. The calculation of the post-winding-up GRIP addition in subsection 89(6) applies to tax years that end after 2005.

2.144 Paragraph 89(6)(a) specifies the amount to be included in the parent corporation’s GRIP if the subsidiary corporation was a CCPC in the tax year its assets were distributed to the parent corporation on the winding-up (the subsidiary corporation’s **last tax year**). Specifically, the amount flowed through to the parent corporation’s GRIP is the positive or negative amount determined by the formula **A - B** where:

A = the subsidiary corporation’s GRIP at the end of its last tax year

B = the amount, if any, of all eligible dividends paid in excess of all excessive designations made by the subsidiary corporation in that last tax year.

2.145 If the subsidiary corporation was a non-CCPC in its last tax year, then paragraph 89(6)(b) specifies that the amount to be included in the parent corporation's GRIP is determined by the formula:

A + B + C – D – E – F – G – H

This formula is based on a tax-balance-sheet approach. It is intended to determine what the subsidiary corporation's GRIP would have been at the end of its last tax year had it been a CCPC in that year. This amount cannot be negative, unlike the amount determined for a CCPC under paragraph 89(6)(a).

2.146 The calculation of GRIP in paragraph 89(6)(b) is similar to the subsection 89(4) GRIP calculation for a corporation that becomes a CCPC. For a detailed description of the operation of this formula, see Becoming a CCPC but to apply paragraph 89(6)(b), read the terms **corporation** and **preceding tax year** as **subsidiary corporation** and **last tax year**, respectively.

LRIP additions: post-amalgamation or post-winding-up

Amalgamation – corporation formed is not a CCPC

2.147 An amalgamation or merger of two or more predecessor corporations, one or more of which is a taxable Canadian corporation, might result in the creation of a corporation that is a non-CCPC (the **amalgamated corporation**). In such a case, the amalgamated corporation's LRIP at any time in its first tax year will include the total of all amounts determined under subsection 89(9) for its predecessor corporations. This amount is included under variable C of the definition of LRIP in subsection 89(1). The calculation of the post-amalgamation LRIP addition in subsection 89(9) applies to tax years that end after 2005.

2.148 Paragraph 89(9)(a) specifies the amount to be included in the amalgamated corporation's LRIP if a predecessor corporation was a non-CCPC in its tax year that ended immediately before the amalgamation (the **last tax year**). The amount included in the amalgamated corporation's LRIP is equal to the predecessor corporation's LRIP at the end of that last tax year.

2.149 If the predecessor corporation was a CCPC in its last tax year, then paragraph 89(9)(b) specifies that the amount included in the amalgamated corporation's LRIP is determined by the formula:

A + B + C – D – E – F – G – H

This formula is based on a tax-balance-sheet approach. It is intended to determine what the predecessor corporation's LRIP would have been at the end of its last tax year had it been a non-CCPC in that year.

2.150 The calculation of the LRIP under paragraph 89(9)(b) is similar to the subsection 89(8) LRIP calculation for a corporation that ceases to be a CCPC. For a detailed description of the operation of this formula, see Ceasing to be a CCPC, but to apply paragraph 89(9)(b) read the terms **corporation** and **preceding tax year** as **predecessor corporation** and **last tax year**, respectively.

Winding-up – parent corporation is not a CCPC

2.151 On a dissolution or winding-up, all or substantially all of the assets of a subsidiary corporation might be distributed to its non-CCPC parent (the **parent corporation**). In this situation, an amount determined under subsection 89(10) for the subsidiary corporation must be included in computing the parent corporation's LRIP. This occurs at any time in a tax year that is at or after the end of subsidiary corporation's tax year during which its assets were distributed to the parent corporation (the subsidiary corporation's **last tax year**). This amount is included pursuant to variable C of the definition of LRIP. This post-winding-up LRIP addition applies to tax years that end after 2005.

2.152 Paragraph 89(10)(a) specifies the amount to be included in the parent corporation's LRIP if the subsidiary corporation was a non-CCPC in its last tax year. The amount included in the parent corporation's LRIP is equal to the subsidiary corporation's LRIP immediately before the end of that last tax year.

2.153 If the subsidiary corporation was a CCPC in its last tax year, the amount included in the parent corporation's LRIP under paragraph 89(10)(b) is determined by the formula:

A + B + C – D – E – F – G – H

This formula is based on a tax-balance-sheet approach. It is intended to determine what the subsidiary corporation's LRIP would have been at the end of its last tax year had it been a non-CCPC in that year.

2.154 The calculation of the LRIP under paragraph 89(10)(b) is similar to the subsection 89(8) LRIP calculation for a corporation that ceases to be a CCPC. For a detailed description of the operation of this formula, see Ceasing to be a CCPC, but to apply paragraph 89(10)(b), read the terms **corporation** and **preceding tax year** as **subsidiary** and **last tax year**, respectively.

Special situations

2.155 The relevant provisions of the Act should be carefully reviewed to determine the specific tax treatment for special situations involving:

- a taxable dividend paid on a **qualified security** under a **securities lending arrangement**, each of which is defined in subsection 260(1);
- a taxable dividend paid as part of a **dividend rental arrangement**, including a **synthetic equity arrangement**, each of which is defined in subsection 248(1);
- a taxable dividend paid to a specified individual and subject to the tax on split income rules in section 120.4;
- an amount paid as interest or a dividend on an income bond or income debenture under subsection 15(3) (where the corporation that paid the amount is not entitled to deduct it in computing its income);
- a capital gains dividend paid by an investment corporation, a mortgage investment corporation and a mutual fund corporation respectively under sections 130, 130.1 and 131;
- a patronage dividend under section 135 (see Interpretation Bulletin IT-362R, Patronage Dividends);
- a patronage dividend on a tax-deferred cooperative share of an agricultural cooperative corporation under section 135.1;
- certain dividends paid by life insurance corporations under section 148 (see Interpretation Bulletin IT-87R2, Policyholders' Income from Life Insurance Policies); and
- unclaimed dividends under subsection 153(4) (see Information Circular 71-9R, Unclaimed Dividends).

Income attribution rules

2.156 For purposes of the Act, subsection 82(2) deems a dividend to have been received by a taxpayer where the dividend was received by some other person but is included in the taxpayer's income under:

- subsection 56(4);
- subsection 56(4.1); or
- sections 74.1 to 75.

This provision is discussed in Interpretation Bulletin IT-440R2, Transfer of Rights to Income, Interpretation Bulletin IT-510, Transfers and loans of property made after May 22, 1985 to a related minor, and Interpretation Bulletin IT-511R, Interspousal and Certain Other Transfers and Loans of Property.

Spousal or common-law partner transfer election

2.157 In certain situations, a taxpayer may make an election under subsection 82(3). The effect of the election is that a dividend received by the taxpayer's spouse or common-law partner is deemed to have been received by the taxpayer.

This election is discussed in Interpretation Bulletin IT-295R4, Taxable Dividends Received After 1987 by a Spouse, Income Tax Folio S1-F4-C1, Basic Personal and Dependant Tax Credits (for 2016 and prior tax years) and Income Tax Folio S1-F4-C2, Basic Personal and Dependant Tax Credits (for 2017 and subsequent tax years).

Application

This updated Chapter, which may be referenced as S3-F2-C2, is effective October 7, 2024.

When it was first published on February 8, 2024, this Chapter replaced and cancelled Interpretation Bulletin IT-67R3, Taxable Dividends from Corporations Resident in Canada.

The history of updates to this Chapter as well as any technical updates from the related interpretation bulletin can be viewed in the Chapter History page.

Except as otherwise noted, all statutory references herein are references to the provisions of the *Income Tax Act,* R.S.C. 1985 (5th Supp.) c.1, as amended and all references to a Regulation are to the *Income Tax Regulations*, C.R.C. 1978, c. 945, as amended.

Links to jurisprudence are provided through CanLII.

Reference

Sections 74.1 to 75, 82, 83, 84, 84.1, 113, 121, 130, 133, 135, 135.1 and 260; subsections 15(3), 52(2), 52(3), 56(4) and (4.1), 89(1), 89(4) to (15), 104(19), 112(1), 112(2.1) to (2.9), 123(1), 123.4(1), 125(1), 125(7), 152(4), 153(4), 184(3), 185.1(1) to (4), 185.2(1) to (5), 186(1), 220(3.2), 249(3.1), 249(4) and 260(1), (5.1) and (6); paragraphs 12(1)(j), 111(1)(a), 161(7)(a); and the definitions of **amount**, **dividend**, **dividend rental arrangement**, **stock dividend**, **subsidiary wholly-owned corporation**, **synthetic equity arrangement** and **taxable dividend** in subsection 248(1) and **qualified security** and **securities lending arrangement** in subsection 260(1).

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