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REFDATE 131204

SUBJECT Transitional reserve - tiered partnership

SECTION 34.2

Please note that the following document, although believed to be correct at the time of issue, may not represent the current position of the CRA. Prenez note que ce document, bien qu'exact au moment émis, peut ne pas représenter la position actuelle de l'ARC.

PRINCIPAL ISSUES: Can a corporate partner of a top-tier partnership in a multi-tier partnership structure continue to claim a transitional reserve under subsection 34.2(11) in respect of the top-tier partnership after the top-tier partnership has been dissolved?

POSITION: **No.**

REASONS: No reserve due to subparagraphs 34.2(13)(a)(i) and 34.2(13)(c)(i). As the transitional reserve under subsection 34.2(11) is **claimed in respect of a particular partnership, it cannot be claimed after that partnership ceases to exist.**

XXXXXXXXXX

2013-049968

December 4, 2013

Dear XXXXXXXXXXXX:

Re: Transitional Reserve under Subsection 34.2(11)

This is in response to your letter of July 29, 2013 in which you enquire whether or not a corporate partner of a top-tier partnership in a multi-tier partnership structure can continue to claim a transitional reserve under subsection 34.2(11) of the Income Tax Act (the "Act") in respect of the **top-tier partnership** after the top-tier partnership has been dissolved.

You provide a hypothetical situation where a Canadian corporation (the "Corporate Partner"), with a December 31st taxation year end, is a member of the top-tier partnership in a multi-tier partnership structure and has a significant interest in that top-tier partnership. You state that there was a **deemed multi-tier alignment election pursuant to subsection 249.1(11)** of the Act and that the **first aligned fiscal period of the partnerships ended December 31, 2011**. In addition, you state that Corporate Partner has **"qualifying transitional income" (QTI) as defined in subsection 34.2(1) of the Act in respect of the top-tier partnership** and has **claimed a transitional reserve starting in its taxation year ending December 31, 2011**. Specifically, you wonder whether Corporate Partner would be able to continue to claim a transitional reserve if the top-tier partnership were to be dissolved.

This technical interpretation provides general comments about the provisions of the Act and related legislation (where referenced). It does not confirm the income tax treatment of a particular situation involving a specific taxpayer but is intended to assist you in making that determination. The income tax treatment of particular transactions proposed by a specific taxpayer will only be confirmed by this Directorate in the context of an advance income tax ruling request submitted in the manner set out in Information Circular IC 70-6R5, Advance Income Tax Rulings.

Our Comments

Budget 2011 introduced a measure to limit the deferral of corporate tax through the use of partnerships. The main rules implementing this measure are found in new sections 34.2 and 34.3, and amended section 249.1 of the Act. The rules under section 34.2 contain provisions that provide **transitional relief** if certain conditions are met. Whether a corporate partner is eligible for transitional relief depends initially on whether the corporation has QTI in respect of a partnership. A corporation's QTI in respect of a particular partnership may include **"eligible alignment income", as defined in subsection 34.2(1)**, which can arise from a deemed multi-tier alignment under subsection 249.1(11). With respect to the transitional relief available in multi-tier partnership structures, Budget 2011 contained the following statements:

A corporate partner will compute QTI for each partnership of which it is directly a member and which is part of a multi-tier structure....In order to qualify for this transitional relief, a corporate partner must have been a direct member of the partnership continuously since before March 22, 2011 until the end of the taxation year in which a reserve is being claimed. [Emphasis added]

Subsection 34.2(11) of the Act provides the amount that a corporation may claim as a transitional reserve in respect of the partnership; however, subsection 34.2(13) of the Act sets out the circumstances under which a corporation cannot claim a reserve under subsection 34.2(11). In particular, paragraph 34.2(13) (a) provides that the corporation cannot claim a transitional reserve unless the corporation has been a member of the partnership continuously since before March 22, 2011 to the end of the taxation year in which the corporation is claiming a reserve.

Subsection 34.2(14) of the Act provides a continuation rule for the purposes of paragraph 34.2(13) (a) in cases where a corporation has disposed of its partnership interest to another corporation related to, or affiliated with, the corporation at the time of the disposition and a corporation related to, or affiliated with, the corporation has the partnership interest at the end of the particular taxation year.

However, this continuation rule cannot apply in a situation where the partnership ceases to exist as the requirements of that provision would not be met. Thus, the transitional reserve under subsection 34.2(11) in respect of a particular partnership cannot be claimed after that partnership ceases to exist as the requirement that the corporation continue to be a member of that partnership to the end of the taxation year would not be met.

Additionally, subparagraph 34.2(13) (c) (i) provides that a corporation cannot claim an amount under subsection 34.2(11) in respect of a partnership for a taxation year if the taxation year ends immediately before another taxation year at the beginning of which the partnership no longer principally carries on the activities to which the reserve relates.

Accordingly, in the situation described above, it is our view that Corporate Partner would not be able to continue to claim a transitional

reserve in respect of the top-tier partnership if the top-tier partnership were dissolved.

We trust the above comments will be of assistance.

Yours truly,

Chrys Tzortzis, CPA, CA

for Director

International Division

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