
Residence-Based Taxation and FAPI: A World of Fictions

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ABSTRACT

This paper covers two aspects of Canadian tax law—corporate residence and foreign accrual property income (FAPI).

In the first part of the paper, the author reviews the development of the concept of corporate residence in tax law. She shows that the law is so loose that a corporation can establish residence in a country without actually having any operations there. Parent corporations can set up subsidiaries that are resident in low-tax jurisdictions or tax havens, and then transfer some of their taxable income from high-tax jurisdictions to those subsidiaries in order to avoid tax. To deal with this problem, Canada has enacted anti-avoidance legislation, notably, in the case of passive income, the FAPI rules.

In the second part of the paper, the author provides a broad description of the FAPI system. The topics covered include FAPI as an anti-deferral measure; the controlled foreign affiliate concept; attribution of “tainted” income of a controlled foreign affiliate; the distinction between business income and property income, and between an active and an inactive business; rules to deem income to be from a business other than an active business; and the calculation of FAPI.

In the third part of the paper, the author briefly considers whether it would be possible to amend the law of corporate residence to get rid of the legal fictions on which it relies and reduce the need for supplementary measures such as the FAPI rules.

KEYWORDS: INTERNATIONAL TAXATION ■ MULTINATIONAL CORPORATIONS ■ RESIDENCY ■ FAPI ■ TAX AVOIDANCE ■ TAX POLICY

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