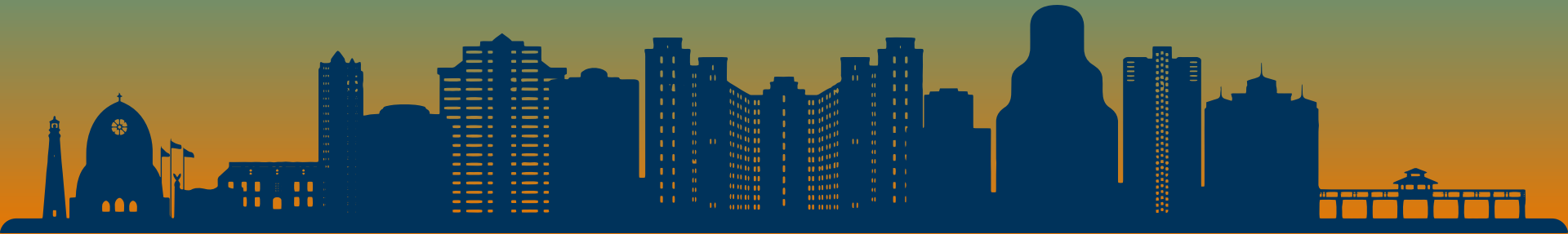


Fuller Landau LLP
June 10, 2024



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Overview of EIFEL Cross-border structures



Excessive Interest and Financing Expenses Limitation (EIFEL) Rules



Excessive Interest and Financing Expenses Limitation (EIFEL) Rules

- The purpose of the EIFEL regime is to address base erosion and profit shifting (“BEPS”) issues arising when taxpayers are deducting excessive interest and other financing costs for income tax purposes, principally in the context of multinational enterprises and cross-border investments.
- The rules adopt an "earnings stripping" approach, which restricts a taxpayer's deductions for interest expense and other financing costs to an amount that is proportionate to the taxable income generated by its activities in Canada.

Excessive Interest and Financing Expenses Limitation (EIFEL) Rules

- New limitation on the deductibility of net interest and other financing expenses based on a fixed ratio of “tax-adjusted” EBITDA (adjusted taxable income):
 - 40% fixed ratio applicable for taxation years commencing on or after October 1, 2023, but before January 1, 2024 (minority of taxpayers).
 - 30% fixed ratio for taxation years beginning on or after January 1, 2024 (most taxpayers).
- The thin capitalization rules apply prior to the EIFEL rules. Any amounts denied under thin capitalization rules are not subject to limitation under EIFEL.

Excessive Interest and Financing Expenses Limitation (EIFEL) Rules

Taxpayers that are “excluded entities” are not subject to the EIFEL rules. An excluded entity is a taxpayer that meets at least one of the following three conditions:

1. Canadian-controlled private corporation with taxable capital not in excess of \$50 million (alone or with associated group (not "eligible group" – an eligible group entity would generally be defined as a corporation or trust that is related to or affiliated with (with modification) a taxpayer)).
2. Canadian groups with net interest expense not in excess of \$1 million (corporations and trusts) (across the "eligible group").
3. Taxpayers who are sufficiently “Canadian” across the "eligible group", meaning for each taxpayer in the eligible group:
 - All or substantially all of business is carried on in Canada;
 - “Immaterial” investments in foreign affiliates;
 - No non-resident specified shareholders or specified beneficiaries (25% ownership/interest respectively);
 - No partnership in which more than 50% of the FMV of the interests are held by non-residents, and the property of the partnership includes more than 25% of the equity in the taxpayer;
 - Minimal interest paid to non-arm’s length tax-indifferent creditors.

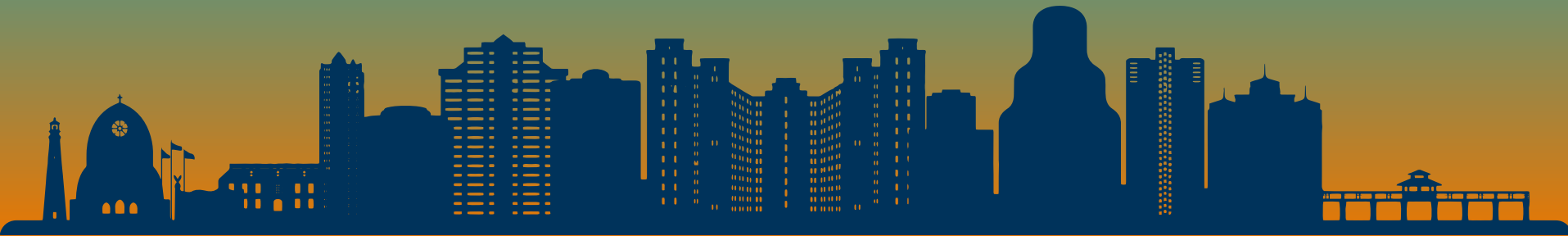
Excessive Interest and Financing Expenses Limitation (EIFEL) Rules

- **Group ratio:**
 - Aims to provide alternative potential relief for taxpayers that are highly leveraged by virtue of their industry or business, primarily in situations where Canada is part of a multinational group.
 - May be particularly beneficial if Canada is as leveraged, or under leveraged relative to the rest of the global group under accounting principles.
 - Group ratio is based on accounting income and not taxable income. If GR election is made, the GR as determined for the particular taxpayer replaces the 30% fixed ratio in the denial formula.
 - Not available if group adjusted net book income, i.e., EBITDA, of the consolidated group is nil or negative.

Excessive Interest and Financing Expenses Limitation (EIFEL) Rules

- **Group ratio:**
 - Allows deduction of interest and financing expense in excess of the fixed ratio where all of the following conditions are met:
 - Taxpayer is a member of a “consolidated group” for the relevant period under accounting principles.
 - All in-scope group members have elected into group ratio (and thus out of Fixed Ratio).
 - Represents the ratio of third-party interest expense to EBITDA (as determined for accounting standards purposes, subject to adjustments), plus a 10% bonus “uplift.
 - Elective on a year-by-year basis for all group members within a “consolidated group”
 - Group capacity is allocable as needed among group members on a discretionary basis.

Cross-border structures: U.S. to Canada and Canada to U.S.



U.S. to Canada structure: Scenario 1

Ontario corporation

- Canadian tax rate → 26.5%
- Disregarded entity for US purposes → No
- CFC → Yes
- Disclosure → 5471
- Income inclusion → GILTI*
- FTC available → Yes*
- Dividend* withholding tax → 5%
- Conversion to ULC
 - US → Taxable event
 - Canada → No taxable event

C Corp



ONT

C Corp



ULC

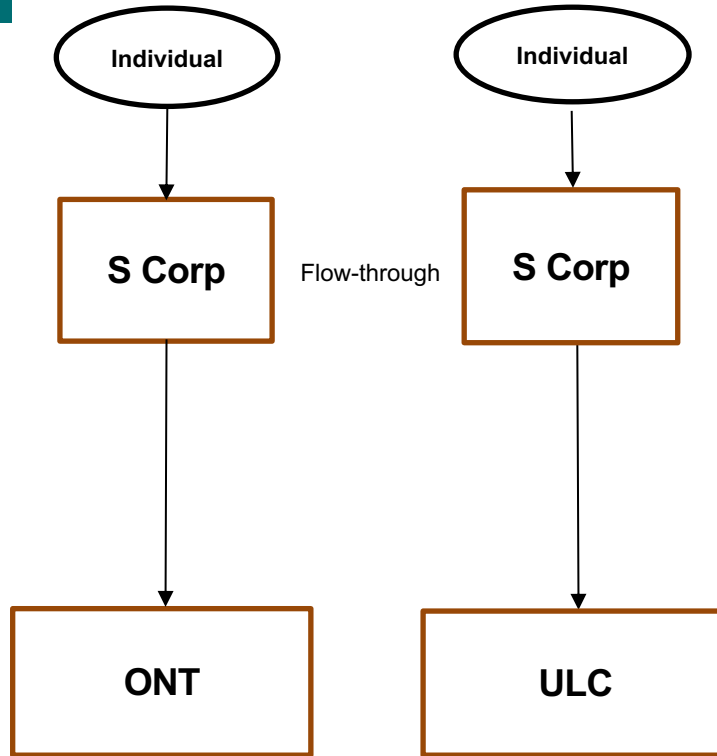
B.C. ULC

- Canadian tax rate → 27.0%
- Disregarded entity for US purposes → Yes
- CFC → No
- Disclosure → 8858
- Income inclusion → Flow through
- FTC available → Yes
- Dividend* withholding tax → 5%
- Conversion to Ontario corporation
 - US → No taxable event
 - Canada → No taxable event

U.S. to Canada structure: Scenario 2

Ontario corporation

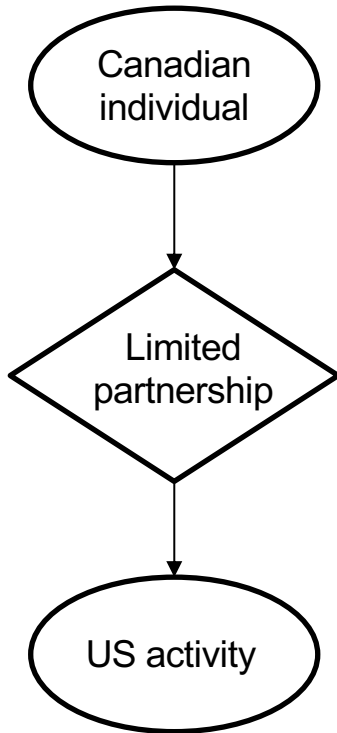
- Canadian tax rate is 26.5%
- Disregarded entity for US purposes → No
- CFC → Yes
- Disclosure → 5471
- Income inclusion → GILTI
- FTC available → Yes
- Could benefit from high-tax exclusion ("HTE")
- Dividend could be PTEP; NIIT only
- Dividend tax @ 20% + NIIT + state if HTE or non-PTEP (962 election)



B.C. ULC

- Fully flow-through structure
- Canadian tax rate is 27%
- Disregarded entity for US purposes → Yes (for ULC)
- CFC → No
- Disclosure → 8858
- Income inclusion → Flow through → 37% + state
- FTC available → Yes
- Dividend withholding tax → 5%
- If multi-member LLC instead of S Corp - 25% withholding tax rate on any dividends.
 - 2-step process for dividends doesn't work in this case.

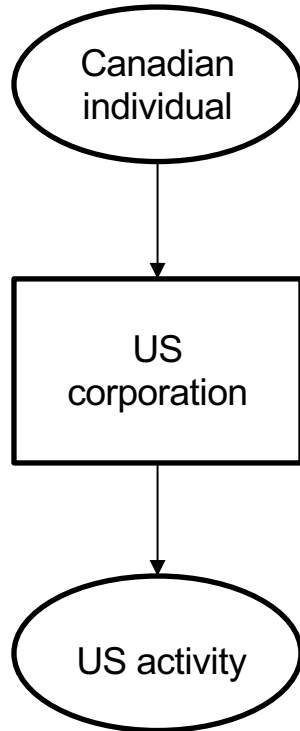
Canada to U.S. structure: Scenario 1



Calculation of Effective Tax Rate on US Active Business Income

A. Undistributed income	100.00
Deduction for qualified business income	(20.00)
	<u>80.00</u>
US tax	
Individual	(34.00)
Corporate	-
	<u>(34.00)</u>
Total US tax on undistributed income	<u>(34.00)</u>
B. Distribution to Canadian interest holder	<u>100.00</u>
C. US withholding/branch tax	<u>-</u>
Total US tax	(34.00)
D. Canadian federal and provincial tax	
Corporate tax	
US branch income	-
Dividend income	-
Dividends-received deduction	-
Taxable income	-
Canadian corporate tax before foreign tax credit	-
Foreign tax credit	-
Net Canadian corporate tax	-
Personal tax	
Income	100.00
Deduction for US taxes	-
Taxable income	<u>100.00</u>
Tax before foreign tax credit	(48.84)
Foreign tax credit	<u>34.00</u>
	(14.84)
Deduction of US taxes against other sources of income subject to Canadian tax [A]	-
Canadian tax savings [B]	-
Total Canadian tax [A] + [B]	-
Total tax on income distributed to Canadian interest holder	<u>(48.84)</u>

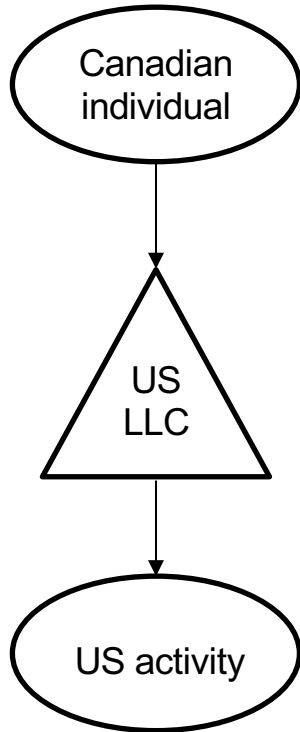
Canada to U.S. structure: Scenario 2



Calculation of Effective Tax Rate on US Active Business Income

A. Undistributed income	100.00
Deduction for qualified business income	-
	<u>100.00</u>
US tax	
Individual	-
Corporate	<u>(26.00)</u>
Total US tax on undistributed income	<u>(26.00)</u>
B. Distribution to Canadian interest holder	<u>74.00</u>
C. US withholding/branch tax	<u>(11.10)</u>
Total US tax	<u>(37.10)</u>
D. Canadian federal and provincial tax	
Corporate tax	
US branch income	-
Dividend income	-
Dividends-received deduction	<u>-</u>
Taxable income	-
Canadian corporate tax before foreign tax credit	-
Foreign tax credit	<u>-</u>
Net Canadian corporate tax	-
Personal tax	
Income	74.00
Deduction for US taxes	<u>-</u>
Taxable income	74.00
Tax before foreign tax credit	<u>(36.85)</u>
Foreign tax credit	<u>11.10</u>
	<u>(25.75)</u>
Deduction of US taxes against other sources of income subject to Canadian tax [A]	-
Canadian tax savings [B]	-
Total Canadian tax [A] + [B]	-
Total tax on income distributed to Canadian interest holder	<u>(62.85)</u>

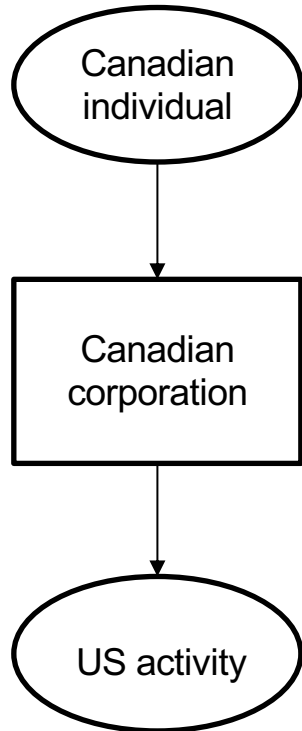
Canada to U.S. structure: Scenario 3



Calculation of Effective Tax Rate on US Active Business Income

	Current distribution	Deferred distribution	
		Year 1	Year 2
A. Undistributed income	100.00	100.00	-
Deduction for qualified business income	(20.00)	(20.00)	-
	80.00	80.00	-
US tax			
Individual	(34.00)	(34.00)	-
Corporate	-	-	-
Total US tax on undistributed income	(34.00)	(34.00)	-
B. Distribution to Canadian interest holder	100.00	-	100.00
C. US withholding/branch tax	-	-	-
Total US tax	(34.00)	(34.00)	-
D. Canadian federal and provincial tax			
Corporate tax			
US branch income	-	-	-
Dividend income	-	-	-
Dividends-received deduction	-	-	-
Taxable income	-	-	-
Canadian corporate tax before foreign tax credit	-	-	-
Foreign tax credit	-	-	-
Net Canadian corporate tax	-	-	-
Personal tax			
Income	100.00	-	100.00
Deduction for US taxes	(19.00)	-	-
Taxable income	81.00	-	100.00
Tax before foreign tax credit	(38.67)	-	(49.80)
Foreign tax credit	15.00	-	-
	(23.67)	-	(49.80)
Deduction of US taxes against other sources of income subject to Canadian tax [A]	-	(34.00)	-
Canadian tax savings [B]	-	16.93	-
Total Canadian tax [A] + [B]	-	16.93	(49.80)
Total tax on income distributed to Canadian interest holder	(57.67)	(17.07)	(49.80)
Cumulative tax for year 1 and year 2			(66.87)

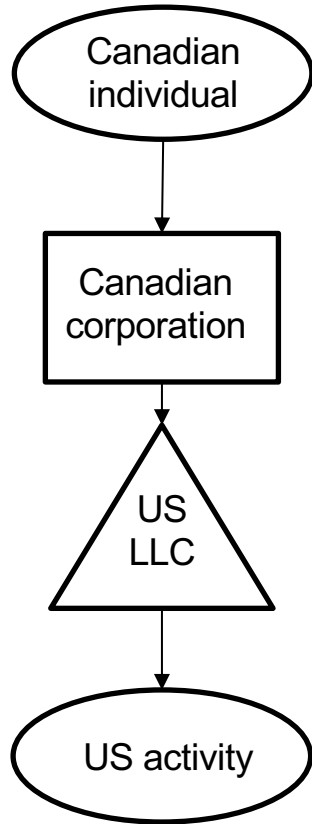
Canada to U.S. structure: Scenario 4



Calculation of Effective Tax Rate on US Active Business Income

A. Undistributed income	100.00
Deduction for qualified business income	<u>-</u>
	100.00
US tax	
Individual	-
Corporate	<u>(26.00)</u>
Total US tax on undistributed income	<u>(26.00)</u>
B. Distribution to Canadian interest holder	<u>74.00</u>
C. US withholding/branch tax	<u>(3.70)</u>
Total US tax	(29.70)
D. Canadian federal and provincial tax	
Corporate tax	
US branch income	100.00
Dividend income	-
Dividends-received deduction	<u>-</u>
Taxable income	100.00
Canadian corporate tax before foreign tax credit	(25.00)
Foreign tax credit	<u>25.00</u>
Net Canadian corporate tax	-
Personal tax	
Income	70.30
Deduction for US taxes	<u>-</u>
Taxable income	70.30
Tax before foreign tax credit	(24.04)
Foreign tax credit	<u>-</u>
	(24.04)
Deduction of US taxes against other sources of income subject to Canadian tax [A]	
Canadian tax savings [B]	
Total Canadian tax [A] + [B]	
Total tax on income distributed to Canadian interest holder	<u>(53.74)</u>

Canada to U.S. structure: Scenario 5

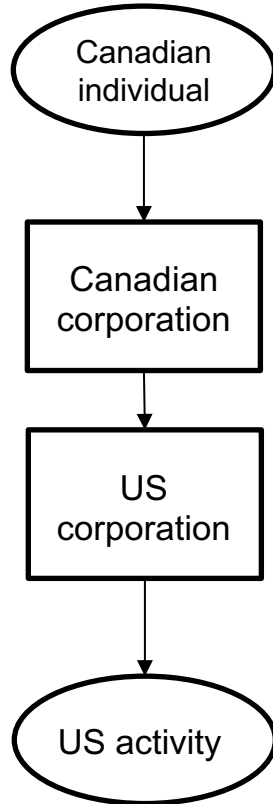


Calculation of Effective Tax Rate on US Active Business Income

A. Undistributed income	100.00
Deduction for qualified business income	<u>-</u>
	100.00
US tax	
Individual	
Corporate	<u>(26.00)</u>
Total US tax on undistributed income	<u>(26.00)</u>
B. Distribution to Canadian interest holder	<u>100.00</u>
C. US withholding/branch tax	<u>(22.20)</u>
Total US tax	(48.20)
D. Canadian federal and provincial tax	
Corporate tax	
US branch income	-
Dividend income	100.00
Dividends-received deduction	<u>(100.00)</u>
Taxable income	-
Canadian corporate tax before foreign tax credit	-
Foreign tax credit	<u>-</u>
Net Canadian corporate tax	-
Personal tax	
Income	51.80
Deduction for US taxes	<u>-</u>
Taxable income	51.80
Tax before foreign tax credit	(17.72)
Foreign tax credit	<u>-</u>
	(17.72)
Deduction of US taxes against other sources of income subject to Canadian tax [A]	
Canadian tax savings [B]	
Total Canadian tax [A] + [B]	
Total tax on income distributed to Canadian interest holder	<u>(65.92)</u>

Canada to U.S. structure:

Scenario 6

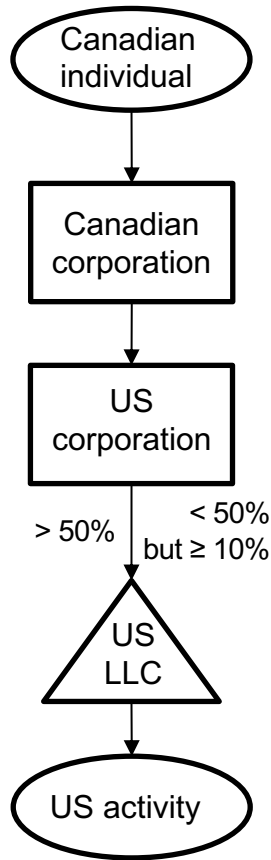


Calculation of Effective Tax Rate on US Active Business Income

A. Undistributed income	100.00
Deduction for qualified business income	<u>-</u>
	100.00
US tax	
Individual	
Corporate	<u>(26.00)</u>
Total US tax on undistributed income	<u>(26.00)</u>
B. Distribution to Canadian interest holder	<u>74.00</u>
C. US withholding/branch tax	<u>(3.70)</u>
Total US tax	(29.70)
D. Canadian federal and provincial tax	
Corporate tax	
US branch income	-
Dividend income	74.00
Dividends-received deduction	<u>(74.00)</u>
Taxable income	-
Canadian corporate tax before foreign tax credit	-
Foreign tax credit	<u>-</u>
Net Canadian corporate tax	-
Personal tax	
Income	70.30
Deduction for US taxes	<u>-</u>
Taxable income	70.30
Tax before foreign tax credit	(24.04)
Foreign tax credit	<u>-</u>
	(24.04)
Deduction of US taxes against other sources of income subject to Canadian tax [A]	
Canadian tax savings [B]	
Total Canadian tax [A] + [B]	
Total tax on income distributed to Canadian interest holder	<u>(53.74)</u>

Canada to U.S. structure:

Scenario 7



Calculation of Effective Tax Rate on US Active Business Income

A. Undistributed income	100.00
Deduction for qualified business income	<u>-</u>
	100.00
US tax	
Individual	
Corporate	<u>(26.00)</u>
Total US tax on undistributed income	<u>(26.00)</u>
B. Distribution to Canadian interest holder	<u>74.00</u>
C. US withholding/branch tax	<u>(3.70)</u>
Total US tax	(29.70)
D. Canadian federal and provincial tax	
Corporate tax	
US branch income	-
Dividend income	74.00
Dividends-received deduction	<u>(74.00)</u>
Taxable income	-
Canadian corporate tax before foreign tax credit	-
Foreign tax credit	<u>-</u>
Net Canadian corporate tax	-
Personal tax	
Income	70.30
Deduction for US taxes	<u>-</u>
Taxable income	70.30
Tax before foreign tax credit	(24.04)
Foreign tax credit	<u>-</u>
	(24.04)
Deduction of US taxes against other sources of income subject to Canadian tax [A]	
Canadian tax savings [B]	
Total Canadian tax [A] + [B]	
Total tax on income distributed to Canadian interest holder	<u>(53.74)</u>



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Questions?

