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# **Explanatory Notes Relating to the Income Tax Act**

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Published by  
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Minister of Finance

May 2017

## **Preface**

These explanatory notes describe proposed amendments to the *Income Tax Act*. These explanatory notes describe these proposed amendments for the assistance of Members of Parliament, taxpayers and their professional advisors.

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These notes are intended for information purposes only and should not be construed as an official interpretation of the provisions they describe.

## **Specified cooperative income**

ITA  
125(7)

Subsection 125(7) of the *Income Tax Act* contains definitions that are relevant to the small business deduction.

### **“specified cooperative income”**

In general terms, income from an active business carried on in Canada by a Canadian-controlled private corporation is eligible for the small business deduction under subsection 125(1) of the *Income Tax Act*, subject to limitations for certain types of income including “specified corporate income”, as defined in subsection 125(7). The new definition “specified cooperative income” is introduced so that certain income arising in connection with sales to farming or fishing cooperatives is excluded from “specified corporate income” with the consequence that such income remains eligible for the small business deduction.

To qualify as “specified cooperative income” of a corporation (referred to as the “selling corporation”), the income must be from the sale of the farming products or fishing catches of the corporation’s farming or fishing business. These sales must also be to a qualifying “purchasing corporation”.

A purchasing corporation will qualify under subparagraph (b)(i) if it is a cooperative corporation (as defined in subsection 136(2), but extended to include fishing businesses) with which the selling corporation deals at arm’s length. A purchasing corporation can also qualify under subparagraph (b)(ii) where such a cooperative corporation holds a direct or indirect interest in it.

To qualify under subparagraph (b)(ii), the selling corporation – or one of its shareholders or a person who does not deal at arm’s length with the selling corporation or one of its shareholders – must hold a direct or indirect interest in a cooperative corporation (as defined in subsection 136(2), but extended to include fishing businesses). That cooperative corporation must then hold a direct or indirect interest in the purchasing corporation. The last condition is that the selling corporation’s income from the sale of farming products or fishing catches would not otherwise be specified corporate income but for the fact that the selling corporation – or one of its shareholders or a person who does not deal at arm’s length with the selling corporation or one of its shareholders – holds a direct or indirect interest in the cooperative corporation.

Amounts included in a corporation’s income under subsection 135(7) (i.e., patronage dividends paid by a cooperative out its profits to its members) would not be income from the sale of the farming products or fishing catches of the corporation and would therefore not qualify as specified cooperative income. This is in keeping with the principle that a single business, including a cooperative business, is entitled to one business limit only.

For more information on what constitutes farming products or fishing catches, see the definitions of “farming” and “fishing” in subsection 248(1).

This amendment applies to taxation years that begin after March 21, 2016.

## **“specified corporate income”**

The definition “specified corporate income” is relevant in determining the portion of a Canadian-controlled private corporation’s income from an active business carried on in Canada that is eligible for the small business deduction under subsection 125(1) of the *Income Tax Act*.

In general terms, the portion of a Canadian-controlled private corporation’s income from an active business from the provision of services or property to a private corporation is not eligible for the small business deduction if the corporation or one of its shareholders (or a person who does not deal at arm’s length with the corporation or one of its shareholders) holds a direct or indirect interest in the corporation, unless the private corporation assigns any portion of its own business limit to the corporation.

The definition “specified corporate income” is amended to provide that income of a corporation that is “specified cooperative income” is not included in the corporation’s specified corporate income. For more information, see the comments under the new definition “specified cooperative income”.

This amendment applies to taxation years that begin after March 21, 2016.