[Income Tax Folio S1-F5-C1, Related Persons and Dealing at Arm's Length](https://www.canada.ca/en/revenue-agency/services/tax/technical-information/income-tax/income-tax-folios-index/series-1-individuals/series-1-individuals/income-tax-folio-s1-f5-c1-related-persons-dealing-arms-length.html)

**Related Persons**

Related persons are deemed not to deal with each other at arm’s length

1. For individuals
	1. Can be a blood relationship
		1. a parent and a child (or other descendant, such as a grandchild or a great-grandchild), or
		2. a brother and a sister
	2. Can be through marriage, common-law partnership or through adoption
2. For corporations
	1. A person is related to a corporation in the following situations:
		1. That person controls the corporation
		2. That person is a member of a related group that controls the corporation
		3. That person is a person who is related to a person described in 1) and 2)
	2. Two corporations are related if
		1. Two corporations are controlled by the same person or group of persons
		2. Each of the corporations is controlled by one person and the person who controls one corporation is related to the person who controls the other corporation
		3. One of the corporations is controlled by one person and that person is related to any member of a related group that controls the other corporation;
		4. One of the corporations is controlled by one person and that person is related to each member of an unrelated group that controls the other corporation
		5. Any member of a related group that controls one of the corporations is related to each member of an unrelated group that controls the other corporation
		6. Each member of an unrelated group that controls one of the corporations is related to at least one member of an unrelated group that controls the other corporation
	3. In determining whether two corporations are related, paragraph 251(5)(c) provides that a person who owns shares of both corporations shall be deemed, as a shareholder of one of the corporations, to be related to himself, herself, or itself as a shareholder of the other corporation.

Control – [De jure control](https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/it64r4-consolid/archived-corporations-association-control.html#P127_13603) (control in law) “was established to be whether the shareholder enjoys “effective control” over the affairs and fortunes of the corporation, as manifested in the ownership of such a number of shares as carries with it the right to a majority of the votes in the election of the board of directors.”

**Unrelated persons**

It is a question of fact whether unrelated persons (other than a taxpayer and a specified personal trust) are dealing with each other at arm's length at a particular time. Sometimes unrelated persons may deal with each other at arm's length and sometimes they may not, depending on the circumstances. General criteria can be provided to determine whether there is an arm's-length relationship between unrelated persons for a given transaction. However, it must be recognized that all-encompassing guidelines to cover every situation cannot be provided. Each particular transaction or series of transactions must be examined on its own merits.

1. The following criteria have generally been used by the courts in determining whether parties to a transaction are not dealing at arm's length :
2. whether there is a common mind which directs the bargaining for both parties to a transaction; [1.39 of folio](https://www.canada.ca/en/revenue-agency/services/tax/technical-information/income-tax/income-tax-folios-index/series-1-individuals/series-1-individuals/income-tax-folio-s1-f5-c1-related-persons-dealing-arms-length.html)
3. whether the parties to a transaction act in concert without separate interests; and [1.39 of folio](https://www.canada.ca/en/revenue-agency/services/tax/technical-information/income-tax/income-tax-folios-index/series-1-individuals/series-1-individuals/income-tax-folio-s1-f5-c1-related-persons-dealing-arms-length.html)
4. whether there is de facto control. [1.40 of folio](https://www.canada.ca/en/revenue-agency/services/tax/technical-information/income-tax/income-tax-folios-index/series-1-individuals/series-1-individuals/income-tax-folio-s1-f5-c1-related-persons-dealing-arms-length.html)
5. Partnerships
	1. Where a partnership owns a majority of the issued voting shares of a corporation, the partnership will not be considered to deal at arm's length with the corporation.
	2. Where one partner is in a position to control a partnership (through ownership of controlling interest or through a mandate vested in that partner by the other partners), that partner is not considered to be dealing at arm's length with the partnership.
	3. Where a related group of partners owns a controlling interest in a partnership, each member of that related group will not be considered to deal at arm's length with the partnership.

Review starts here.

In order to use the examples below to determine whether a tenant and a property owner are not dealing with each other at arms length, you need the following information regarding each.

The name of any individuals that own or are renting the property and the nature of the relationship between them. The holders of the voting shares of any corporations that own or are renting the property and the percentage of voting shares held by each.

**Note**: Only amounts paid (or payable provided certain conditions are met) by an eligible entity to an arm’s-length party, in respect of a week in a claim period, are included for purposes of computing the Canada Emergency Rent Subsidy (CERS.) Therefore, rent, and amounts required to be paid under a net lease, that are paid to a non-arm’s-length party are not an eligible expense for the CERS.

However, if the owner of a property uses the property primarily to earn rental income, directly or indirectly from a non-arm’s length party, the owner may be able to claim eligible expenses such as property and similar taxes, property insurance and interest on a commercial mortgage. For these expenses to qualify, the property can not be a property used by the non-arm’s-length party primarily to earn rental income.

For example, Holdco and Retailco are related corporations and therefore do not deal at arm’s length with each other. Holdco owns a building which it leases to Retailco. Retailco pays rent to Holdco for use of the building to operate its retail store. Retailco uses the building for its business operations and does not use the building primarily to earn rental income. The rent paid from Retailco to Holdco would not be an eligible expense for purposes of the CERS because it is paid to a non-arm’s-length party. However, Holdco may be able to claim eligible expenses paid for the building it rents to Retailco, such as property and similar taxes, property insurance and interest on a commercial mortgage for purposes of the CERS.

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| **Example** | **Structure** | **Conclusion** |
| Mr. A owns 100% of the shares of Op Co. Op Co rents a building that is owned by Mr. A (or vice versa). | Op Co. | Mr. A and Op Co are related persons since Mr. A controls Op Co. As such, Mr. A and Op Co do **not deal at arm’s length with each other.** |
| Mr. A has a controlling interest in Partnership A. Partnership A rents a building that is owned by Mr. A (or vice versa). | Partnership A. | **Mr. A is not dealing at arm’s length with Partnership A** since Mr. A has a controlling interest in Partnership A. Refer to paragraph 1.43 of Folio S1-F5-C1: Related persons and dealing at arm's length. |
| Mr. A and Mrs. A (spouses) each own 50% of the shares of Hold Co. Hold Co owns 100% of the shares of Op Co. Hold Co owns a building and Op Co pays rent to Hold Co.  | 100% votesOp Co.Hold Co. | Mr. A and Mrs. A are related by virtue of marriage. Mr. A and Mrs. A are a related group that controls Hold Co. Since Hold Co owns all of the shares of Op Co, Hold Co controls Op Co. **Therefore, Hold Co and Op Co do not deal at arm’s length.** |
| Mr. A, Mr. B and Mr. C are not **related**. They each own 1/3 of the voting shares of Op Co. Op Co pays rent to Mr. C. | Op Co. | Mr. C and Op Co are not related. **It is a question of fact whether Mr. C and Op Co are dealing at arm’s length. Additional factors in paragraphs 1.37 to 1.40 of** Folio S1-F5-C1: Related persons and dealing at arm's length **will need to be considered.** If, for example, Mr. C and Op Co are acting in concert without separate interest in respect of the rental transaction **they may not be dealing at arm’s length.** |
| Mr. A, Mr. B and Mr. C are **related**. They each own 1/3 of the voting shares of Op Co. Op Co pays rent to Mr. C. | Op Co. | Mr. C and Op Co are related since Mr. C is part of a related group that controls Op Co. **Mr. C and Op Co are not dealing at arm’s length.** |
| Mr. A owns 100% of the shares of Op Co. Mrs. A (Mr. A’s spouse) owns 100% of the shares of Hold Co. Op Co pays rent to Hold Co (or vice versa). | Op Co.Hold Co. | Op Co and Hold Co are related since the individual that controls Op Co (Mr. A) is related to the individual that controls Hold Co (Mrs. A) by virtue of marriage. **Therefore, Op Co and Hold Co do not deal at arm’s length.** |
| Mr. A owns 100% of the shares of Op Co and 100% of the shares of Hold Co. Op Co pays rent to Hold Co (or vice versa). | 100% votes100% votesHold Co.Op Co. | Op Co and Hold Co are related, as both corporations are controlled by the same person (Mr. A). **Therefore, Op Co and Hold Co do not deal at arm’s length.** |
| Mr. A and Mr. B are **not related**. Mr. A and Mr. B each own 50% of the shares of Op Co and Hold Co. Mr. A and Mr. B act in concert to control Op Co and Hold Co. Op Co pays rent to Hold Co (or vice versa). | Hold Co.Op Co. | Op Co and Hold Co are related since each corporation is controlled by the same unrelated group **Therefore, Op Co and Hold Co do not deal at arm’s length.** |
| Mr. A and Mr. B are **related** (could be father son, brothers etc.). Mr. A and Mr. B each own 50% of the shares of Op Co and Hold Co. Op Co pays rent to Hold Co (or vice versa). | Hold Co.Op Co. | Op Co and Hold Co are related since both are controlled by the same related group. **Therefore, Op Co and Hold Co do not deal at arm’s length.** |
| Mr. A owns 100% of the shares of Op Co Mrs. A (spouse of Mr. A) and Child A (daughter of Mr. A and Mrs. A) each own 50% of the shares of Hold Co. Op Co pays rent to Hold Co (or vice versa). | Op Co.Hold Co. | Op Co and Hold Co are related: Mr. A controls Op Co and Hold Co is controlled by a related group (Mrs. A and Child A). Mr. A is related to any member of the related group that controls Hold Co (Mr. A is related to Mrs. A and Child A). **Therefore, Op Co and Hold Co do not deal at arm’s length.** |
| Mr. A owns 100% of the shares of Op Co. Mr. X and Mr. Y (both grandchildren of Mr. A) each own 50% of the shares of Hold Co. Mr. X and Mr. Y are cousins who act in concert to control Hold Co. Op Co pays rent to Hold Co (or vice versa). | Op Co.Hold Co. | Op Co and Hold Co are related: Mr. A controls Op Co and Hold Co is controlled by an unrelated group (i.e., Mr. X and Mr. Y - cousins are not related for tax purposes). However, Mr. A is related to each member of the unrelated group that controls Hold Co since they are his grandchildren. **Therefore, Op Co and Hold Co do not deal at arm’s length.** |
| Mr. A and Mr. B (Mr. A’s Child) each own 50% of the shares of Op Co. Mr. X (Mr. B’s Child and Mr. A’s grandchild) and Mr. Y (another grandchild of Mr. A) each own 50% of the shares of Hold Co. Mr. X and Mr. Y are cousins who act in concert to control Hold Co. Op Co pays rent to Hold Co. (or vice versa). | Op Co.Hold Co. | Op Co and Hold Co are related: Op Co. is controlled by a related group (Mr. A and Mr. B). Hold Co is controlled by an unrelated group (i.e., Mr. X and Mr. Y - cousins are not related for tax purposes). However, Mr. A is related to each member of the unrelated group that controls Hold Co since they are his grandchildren. **Therefore, Op Co and Hold Co do not deal at arm’s length.** |
| Mr. A and Mr. B are **not related** and each own 50% of the shares of Op Co. Mr. A and Mr. B act in concert to control Op Co. Mrs. A and Mrs. B (spouses of Mr. A and Mr. B, respectively), each own 50% of the shares of Hold Co. Mrs. A and Mrs. B act in concert to control Hold Co. Op Co. pays rent to Hold Co (or vice versa). | Op Co.Hold Co. | Op Co and Hold Co are related since each member of the unrelated group that controls Op Co is related to at least one member of the unrelated group that controls Hold Co (i.e. Mr. A is related to Mrs. A and Mr. B is related to Mrs. B by virtue of marriage). **Therefore, Op Co and Hold Co do not deal at arm’s length.** |