



SOMERSET LIMITED V. THE KING:
INTERPRETING THE DEFINITION OF
“CANADIAN CORPORATION”
IN SUBSECTION 89(1)

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The TCC's recent decision in *Somerset Limited v. The King* ([2026 TCC 123](#)) addressed transactions largely similar to the ones undertaken in *Canada v. DAC Investment Holdings Inc.* ([2026 FCA 35](#)), which the FCA held were subject to GAAR. (The substantive CCPC rules have since put an end to this type of planning.) However, *Somerset* raised a novel technical issue that was not present in *DAC* and will be of interest to tax practitioners because of the TCC's analysis of the meaning of “Canadian corporation,” as defined in subsection 89(1) of the ITA.

Somerset Limited (“Somerset”) was incorporated under the Companies Act (BC) on May 26, 1943, and has been resident in Canada since its incorporation. At the outset of the transactions at issue, all of Somerset's shareholders were individual taxpayers who were resident in Canada and members of the same extended family. Accordingly, before the planning was undertaken, Somerset was a CCPC within the meaning of subsections 248(1) and 125(7).

Somerset owned two apartment buildings in Vancouver and entered into an agreement to sell them for approximately \$34 million. On December 10, 2018, prior to the sale, Somerset was continued into the British Virgin Islands (BVI), with the aim, as in *DAC*, of exiting CCPC status and thereby avoiding the application of the additional tax on investment income under section 123.3 and accessing the general rate reduction under section 123.4.

After the continuance, on December 17, 2018, Somerset sold the apartment buildings.

The sale of the buildings resulted in a significant capital gain and created a balance in Somerset's capital dividend account. Capital dividends were paid to Somerset's individual shareholders on December 17, 2018 and on January 30, 2019. Each of the individual shareholders then transferred their Somerset shares to their respective newly incorporated holding corporations (“Holdcos”) on a tax-deferred basis. On February 25, 2019, Somerset paid the Holdcos taxable dividends (which were in part non-eligible dividends and in part eligible dividends) and paid additional eligible dividends in 2020.

Somerset originally had a December 31 year-end. Post-continuance, it filed tax returns on the basis that Somerset, having ceased to be a CCPC on December 10, 2018, had taxation years from January 1 to December 9, 2018 and from December 10 to December 15, 2018, and thereafter year-ends on December 15 of each subsequent year. In June 2022, the CRA approved Somerset's request to change its year-end from December 31 to December 15,

effective from 2018 onward. In its 2019, 2020, and 2021 tax returns, Somerset filed on the basis that the anti-deferral rules described above, applicable to investment income earned by a CCPC, did not apply to it.

On October 7, 2022, the minister of national revenue reassessed Somerset for its 2019, 2020, and 2021 taxation years on the basis that it remained a CCPC notwithstanding its continuance to the BVI. This tax treatment resulted in Somerset having made excessive eligible dividend designations. The minister allowed Somerset to elect under subsection 185.1(2) to treat the eligible dividends in respect of which the excessive eligible dividend designations had been made as ordinary taxable dividends.

Two issues were in dispute. The first was whether Somerset ceased to be a CCPC as a result of its continuance to the BVI because it ceased to be a “Canadian corporation,” as defined in subsection 89(1). The second issue was whether, in the alternative, GAAR applied to the transactions. In respect of the CCPC issue, the minister contended that Somerset remained a Canadian corporation after its continuance.

The relevant portion of the definition of “Canadian corporation” in subsection 89(1) provides as follows:

Canadian corporation at any time means a corporation that is resident in Canada at that time and was

- (a) incorporated in Canada, or
- (b) resident in Canada throughout the period that began on June 18, 1971 and that ends at that time.

The minister contended that the meaning of this provision was clear and unambiguous and that, on a plain reading of paragraph (b), Somerset was a Canadian corporation before the continuance and remained a Canadian corporation after the continuance. The minister reached this conclusion because Somerset was incorporated before 1971 and had remained resident in Canada ever since.

The taxpayer argued that, because of the continuance, Somerset had ceased to satisfy paragraph (a) of the definition of “Canadian corporation” by virtue of subsection 250(5.1), which, in simplified terms, deems a continued corporation to have been incorporated in the jurisdiction to which it was continued. In other words, the taxpayer argued that, after the continuance, it did not satisfy paragraph (a) of the definition of “Canadian corporation” because it was not incorporated in Canada. The taxpayer also argued that, after the continuance, it did not satisfy paragraph (b) of the definition of “Canadian corporation” because that paragraph applies only to corporations that were factually incorporated outside Canada (which Somerset was not).

The TCC agreed in part with the taxpayer’s arguments but ultimately upheld the reassessments on the basis that Somerset remained a Canadian corporation—and thus a CCPC—after the continuance. The court reached this conclusion after examining the text of the definition of “Canadian corporation” in subsection 89(1) and concluding that the word “or” between paragraphs (a) and (b) of the definition was “disjunctive.” The term “disjunctive” means that “or” demarcates two mutually exclusive conditions. Applying that reading, the TCC held that paragraph (b) applied only to corporations that were not incorporated in Canada (because paragraph (a) applied only to corporations incorporated in Canada). Accordingly, the court accepted Somerset’s argument that, before its

continuance into the BVI, it was a Canadian corporation by virtue only of paragraph (a) of the definition of “Canadian corporation.”

However, the TCC also held that the effect of the deeming rule in subsection 250(5.1) was to cause Somerset to be deemed to have been incorporated in the BVI on May 26, 1943. Therefore, the TCC held that Somerset satisfied the conditions of paragraph (b) of the definition of “Canadian corporation.” The court rejected the taxpayer’s argument that paragraph (b) applied only to corporations factually incorporated outside Canada. The TCC held that the deeming rule in paragraph 250(5.1)(a) applies for the purposes of the ITA (other than subsection 250(4)) and thus applied for the purposes of paragraph (b) of the definition of “Canadian corporation” in subsection 89(1).

The TCC’s ruling that Somerset remained a Canadian corporation and, therefore, a CCPC after its continuance into the BVI was sufficient to dispose of the appeal. However, in the event that the court was found to be in error with respect to that issue on appeal, the court also ruled that GAAR applied to the transactions.

The taxpayer argued that the transactions were not abusive, as the transactions in *DAC* had been found to be, because Somerset “through a different transaction, could have achieved the same commercial result and an equal or better tax result.” The taxpayer had proposed, as an alternative transaction, that Somerset could have been a BVI corporation all along. The TCC held that this alternative transaction was too remote to be feasible and that its tax consequences would not have been approximately as favourable as those of the series at issue. The tax consequences would not have been as favourable because had Somerset been originally incorporated in the BVI in 1943, it would still have been a CCPC because it would have satisfied the definition of “Canadian corporation” on the basis of its continued residence in Canada since 1971.

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