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Tax Notes

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New Case Stresses Family Business Corporate Governance

Estate and succession planning structures generally involve the introduction of family members as shareholders. Without this planning, the founder of a business would likely be inclined to simply hold on to the shares of the family business. In fact, even with these structures in place, the founder's impulse will be to carry on as if nothing happened. And we practitioners are eager to assist in achieving this objective by designing structures to put the founder in a position to continue to control the company with a minimum of interference from family members. Trouble is, these positions of control may often carry duties to the family member shareholders which may conflict with the inclinations of the founder. This is all well and good when the family is young and harmony prevails. But it's not so good when kids grow up and the founder wishes to favour some family members over others.

In these situations, what can/should be done to protect the interests of the founder – i.e., as estate and succession plans mature? A recent Ontario case, *Tanenbaum v. Tanjo Investments*[1] provides some insight into this issue.

For the purposes of discussion, we can think of the share structure of Tanjo as an estate freeze by the grandfather, the late (and very successful) Joe Tanenbaum. For many years, the growth shares of Tanjo had been held by three family trusts, one for each of Mr. Tanenbaum's children wherein Mr. Tanenbaum's grandchildren were beneficiaries. Prior to the distribution from the three trusts, Mr. Tanenbaum executed a "letter of wishes" to his trustees, which indicated that he wanted each of the grandchildren treated equally. While two of Mr. Tanenbaum's children each had three of their own kids, the third had only one, Katherine. Consequently, when the shares were distributed from that particular trust, Katherine's equity interest represented a third of the shares in question, whereas, if the grandchildren were to be treated equally, she would be entitled only to a one-seventh interest.

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Even though the shares of Tanjo had been distributed from the family trust, the directors and executives of Tanjo wanted to continue to provide for the wishes of Mr. Tanenbaum (who passed away in 1992). Of course, payment of dividends would have not achieved this objective. So instead, the distributions were made to one of the grandchildren in the form of a bonus. The particular grandchild paid tax on the bonus and gifted the after-tax proceeds to the other six grandchildren so that they shared the proceeds equally.

An Oppression Application

Unfortunately, Katherine passed away in 2005. The trustee for Katherine's estate brought an action for oppression, based on the bonus regime.[2] As the Court put it, the issue was whether the expectations of Katherine should be as a shareholder indirectly entitled to the benefits associated with the one-third shareholding in Tanjo, or "are those expectations to be limited to those of a young individual who was advised of her grandfather's wishes . . . ".[3]

Although the Court indicated that there was some evidence that Katherine was aware and concurred with the bonus regime, it observed that it "lacks the objectivity, transparency, and accountability that should accompany corporate acts."[4] The Court concluded that the reasonable expectation was that Katherine was entitled to expect that Tanjo would be operated in a lawful and proper corporate form with meetings, resolutions and minutes that would reflect proper corporate acts.[5] It was not reasonable to change to the bonus scheme, the effect of which was to effectively reduce or eliminate the value of her shares "without informed advice or consent reflected in appropriate corporate resolutions".[6]

The Court summarized a number of deficiencies in respect of the corporate records of Tanjo, including the fact that there were "no records of directors or shareholder meetings" nor formal record or other evidence to reflect the scheme for payments.[7]

Some Important Lessons

Tanjo teaches some important lessons for founders who have introduced family members as shareholders in succession and estate planning structures. The founder will typically be a director of the corporation in question (often the sole director) as well as a trustee of the family trust which typically holds growth or other shares of the corporation. As a director, the founder will have fiduciary duties to the corporation and its shareholders, as well as to the beneficiaries of the family trust as a trustee.

The case underscores the advisability of founders giving consideration to corporate and trust governance matters in estate and succession planning structures. Consideration should be given, for example, to having regular family shareholders' meetings, with minutes being prepared or at least notes of the discussion. Special consideration should be given to proper corporate governance and documentation where there are transactions that favour some shareholders over others.[8] Examples may include the payment of large bonuses[9] or dividends, especially if large enough to significantly erode the value of the corporation, as well as additional compensation given to children who are involved in the family business that cannot be justified by arm's length benchmarks.[10] Finally, as was the case with Mr. Tanenbaum, it is not uncommon for a founder to seek to treat his or her offspring equally or in some other manner which may not be consistent with the underlying share structure. *Tanjo* itself queries: "how easy would it have been to have the process proceed formally, including the appropriate resolutions . . .".[11]

In such situations, it is important both from a corporate and trust standpoint that there be records that seek to justify the particular course of action. For example, in the case of an asymmetrical distribution from a discretionary family trust, trustees' resolutions should document the considerations addressed by the trustees – and that these included relevant factors and excluded irrelevant factors, such as disapproval with a particular beneficiary's spouse or other personal circumstances.[12] Some other themes of *Tanjo* itself include the requirement for "informed knowledge sufficient to acquiesce" to the bonus regime[13] as well as lack of corporate documentation and corporate steps that would be required to support a conclusion that Katherine's reasonable expectations were only to receive what those in charge advanced her.[14]

TAX NOTES

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The early years of an estate or succession plan will typically be uneventful, what with young kids, the protection of a family trust and so on. But kids grow up and get married, and family trusts run their course. Transactions could be impugned, often years after they are done, if there is a dispute among family members. Old corporate records, financial statements and tax returns could be reviewed by counsel representing a disgruntled family member. The *Tanjo* case illustrates that, from a corporate governance standpoint, the safe thing to do is to run the family business on the assumption that, one day, someone might be looking over your shoulder – and it is possible that the assumption may turn out to be correct.

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Notes:

[1] *Tanenbaum v. Tanjo Investments Limited*, 2009 CanLII 48526 (Ont. Sup.Ct.).

[2] When I first saw the judgment, one thing that jumped out at me was the top-drawer "legal firepower" that was brought to bear by both the applicants and respondents.

[3] Paragraph 52.

[4] Paragraph 55. The Court also observed that two of Katherine's cousins were part of the decision makers who changed the distribution scheme from dividends to the bonus regime, assuming that they could be governed by the wishes of the late Mr. Tanenbaum – see paragraphs 53 and 54.

[5] Paragraph 64.

[6] Paragraph 65.

[7] Paragraph 60.

[8] This is particularly important where the transaction is somewhat unorthodox, as was the case with *Tanjo*.

[9] Including where the business has been following the practice of bonusing-down to the small business limit, which until recently at least, was commonplace.

[10] Of course, it may be advisable to document these benchmarks.

[11] Paragraph 71. Query whether this would have been as "easy" as the Court suggests.

[12] In fact, the importance of records of trustees' deliberations may have become more important due to the recent *Garron* case, 2009 DTC 1287 (TCC), a digest of which appears below.

[13] Paragraph 66

[14] Paragraph 69. Also important in the case is the "appearance" of other transactions undertaken by the corporation. See, for example, paragraph 70.

Recent Cases

Trusts were resident in Canada – Capital gains not exempt from tax

PMPL Holdings Inc. ("PMPL") was incorporated in 1992 to hold the shares of two operating companies. On April 2, 1998, in the course of a reorganization of PMPL's share structure (the "Reorganization"), two trusts with Canadian beneficiaries, the Summersby Settlement and the Fundy Settlement (the "Trusts"), were settled by an individual resident in the Caribbean. The sole trustee of each of the Trusts was St. Michael Trust Corporation ("St. Michael"), which was a corporation resident in Barbados. As part of the Reorganization, the Trusts subscribed for shares of newly incorporated Canadian corporations ("1287325 Ontario Inc." and "1287333 Ontario Inc."), and these new corporations, in turn, subscribed for new common shares of PMPL. Under the Reorganization, the previous common shareholders of PMPL acquired Class A Preference shares of PMPL and were no longer common shareholders of PMPL. As part of an arm's length sale of PMPL in 2000, the Trusts disposed of the majority of the shares they held in 1287325 Ontario Inc. and 1287333 Ontario Inc., realizing capital gains of over $450 million (the "Capital Gains"). These gains were not subject to tax in Barbados. Potential Canadian tax on the Capital Gains, however, had been remitted by the Trusts to the Minister under the withholding procedures of s. 116 of the Act. In filing their returns for 2000, the Trusts sought a return of the amounts remitted under s. 116, alleging that the Capital Gains were exempt from Canadian tax under Article XIV(4) of the *Canada–Barbados Income Tax Agreement* (the "Treaty"). (Article XIV(4) states that gains from the alienation of property can only be taxed by the Contracting State of which the alienator is a resident). In assessing the Trusts for 2002, the Minister denied them the Article XIV(4) exemption claimed. The Minister also assessed four Canadian residents (Dunin, M. Garron, B. Garron, and the Garron Family Trust (the "Other Appellants")) with respect to the Capital Gains, since they all had interests in PMPL either directly or through a holding company prior to the Reorganization. The Minister emphasized, however, that there was no intent to tax the Capital Gains more than once, and that the assessments of the Other Appellants were carried out solely as a protective measure, since the assessments of the Trusts took priority. The Trusts and the Other Appellants all appealed to the Tax Court of Canada. On the appeal, the Minister's position was that: (a) the exemption in Article XIV(4) of the Treaty was inapplicable because the Trusts were resident in Canada under general principles; (b) the Trusts were deemed under s. 94(1)(*c*) of the Act to be residents of Canada because they had received property from beneficiaries resident in Canada; (c) the Capital Gains were subject to tax in the Other Appellants' hands under the attribution rule in s. 75(2); (d) the General Anti-Avoidance Rule ("GAAR") applied to justify the taxation of the Capital Gains imposed in all of the assessments; and (e) the allocation of the sale proceeds from the arm's length sale of PMPL should be

partially reallocated from the Trusts to the Other Appellants.

The Trusts' appeals were dismissed and the Other Appellants' appeals were allowed. Although the Trusts and the Other Appellants alleged that the Trusts were resident in Barbados for the purpose of the Treaty, it was not necessary to decide the outcome of the appeal on this basis, because the Minister took no specific position on the issue of the Trusts' Barbados residence. To promote consistency and certainty, the judge-made test for residence established for corporations should also apply to trusts with any appropriate modifications. That test for residency is "where the central management and control lies". When the Trusts disposed of the shares of 1287325 Ontario Inc. and 1287333 Ontario Inc., the management and control of the Trusts was located in Canada with Dunin and M. Garron, and not with St. Michael in Barbados. St. Michael had neither expertise nor experience in managing trusts, and Dunin and M. Garron made the substantive decisions for the Summersby Settlement and the Fundy Settlement, respectively. The Trusts were therefore resident in Canada for purposes of the Treaty, and this finding was sufficient to dispose of all of the appeals. Further observations on some of the other issues raised, however, were appropriate. Since the Trusts did not acquire property from Dunin and M. Garron, they could not be deemed under s. 94(1)(*c*) of the Act to be residents of Canada, as the Minister had attempted to argue. For the same reason, the attribution rule in s. 75(2) was inapplicable to justify the Minister's assessments of the Other Appellants for tax on the Capital Gains. The Trusts and the Other Appellants did not dispute the fact that the Reorganization involved avoidance transactions and tax benefits for purposes of the GAAR. There was, however, no abuse of any of the provisions of the Treaty, so that the Minister's reliance on the GAAR in support of his assessments was unjustified. It was inappropriate to analyze whether there had been an abuse of s. 75(2) of the Act, since the Minister did not specifically raise this issue in a timely fashion. However, the Capital Gains reallocation issue under s. 68 should, under all of the circumstances, be left for consideration on another day. The Minister's assessments of the Trusts were affirmed accordingly. The Minister was ordered to reassess the Other Appellants on the basis that no part of the Capital Gains should be included in their incomes.

Garron Family Trust et al., 2009 DTC 1287

Trust was not validly created – GAAR also applied

The taxpayer, Antle, and Mukesh Kapila incorporated PM. Antle owned 2.39 million shares of PM. In 1998, in an arm's length transaction (the "SCC Acquisition Agreement"), PM acquired shares of SCC Environmental Group Inc. ("SCC") from Stratos Global Corporation ("Stratos") in return for preferred shares of PM, debt, and a right to 50 per cent of the profits from any future sale of the SCC shares by PM (the "50-50 Clause"). The share certificate for Antle's shares of PM was endorsed in blank by him, and was placed with Stratos to be held as security for PM's performance of its obligations under the SCC Acquisition Agreement. On October 1, 1999, Antle accepted an offer from MI Drilling Fluids Canada Inc. ("MI") to purchase his shares of PM, subject to the negotiation of a definitive agreement. Stratos was aware of this agreement between Antle and MI, and gave its approval in principle, subject to the proviso that Antle would ensure that, out of the proceeds of sale of the shares of PM, Stratos would be paid for its preferred shares and debt of PM, plus an amount under the 50-50 Clause as additional consideration, as contemplated in the SCC Acquisition Agreement. To accomplish the sale of his PM shares to MI without Canadian tax liability on the resulting capital gain, Antle decided to employ a capital property step-up strategy. Because of impending Canadian tax law amendments, there was a rush to complete all of the transactions and supporting documentation by the end of 1999. Antle, therefore, purported to transfer his shares of PM, by way of s. 73(1) rollover, to a Barbados spousal trust that he purported, allegedly on December 5, 1999, to settle with a Barbados resident solicitor, Mr. Truss, as trustee (the "Trust"). The Trust would not be subject to Barbados tax on any realized capital gains. The Trust then purported to sell its shares of PM at their fair market value to its sole beneficiary, Antle's wife, allegedly on December 8, 1999, although Antle never signed the Trust Deed until December 14, 1999. Mrs. Antle purported to sell the shares of PM to MI, again at their fair market value, and to use the proceeds of that sale to pay off the Trust. The Trust then distributed the proceeds to Mrs. Antle as its sole beneficiary, and dissolved shortly thereafter. The closing of the sale of PM shares to MI took place on December 14, 1999 in the office of Antle's lawyer, Chalter, and all transfers of funds among all of the parties were processed through Chalter's trust account. Stratos' claims were also paid out of the proceeds of sale of the shares of PM from Chalter's trust account. In reassessing Antle and The Trust for 1999, the Minister included in their income the taxable capital gain resulting from the sale of the shares of PM. On the taxpayers' appeals to the Tax Court of Canada, the Minister's principal arguments were that the Trust was a sham, and that, in the alternative, the reassessments were justified under the GAAR.

Antle's appeal was dismissed and the Trust's appeal was quashed. Antle did not truly intend to settle the PM shares in a discretionary trust with Mr. Truss as trustee. He simply signed documents on the advice of his professional advisers, expecting to avoid paying tax in Canada. Neither on December 14, 1999, nor on any earlier date, did he ever relinquish control of his PM shares to the Trust. He did not even sign the Trust Deed until December 14, 1999, and did not communicate with Mr. Truss until that date. If he transferred anything to the Trust, it was not his full interest in the PM shares, since Stratos did not release the share certificate for those shares until its claims were satisfied out of the proceeds of sale coming from MI on December 14, 1999, when the sale closed. Mr. Truss, as the trustee of the Trust,

accordingly never became the owner of the PM shares in his fiduciary capacity, nor was he given any discretion to act as a trustee. At best, he might have been Antle's agent to effect a gift from Antle of the PM shares to Mrs. Antle. The Trust, therefore, was not validly created, because it lacked the certainty of intention on Antle's part to create it, and the certainty of its subject matter, i.e., the complete ownership and control over the PM shares. The Trust, however, was not a sham, despite the Minister's allegations to the contrary. There was no intention on Antle's or Mr. Truss's part to engage in any form of deception, even though there was an element of artificiality in Antle's attempt to use the Trust as part of his capital property step-up strategy. With no valid Trust, Antle either sold his shares of PM to Mr. Antle, generating a capital gain in his hands, or he rolled them over to his wife, and the resulting gain in her hands was attributed back to him. This conclusion was sufficient to dispose of Antle's appeal. However, the GAAR also applied. There was clearly a tax benefit and an avoidance transaction through the purported use of the Trust whose sole purpose was to avoid tax. There was also an abuse of the object, spirit, and purpose of the provisions of the *Income Tax Act* (the "Act") that are intended to ensure taxation of Canadian residents on capital gains arising on dispositions of capital property outside the marital unit, including through the use of offshore trusts. By relying on s. 94(1)(*c*) of the Act to deem the Trust to be a Canadian resident, thus taking advantage of the s. 73(1) rollover, and then escaping Canadian tax by invoking s. 110(1)(*f*) of the Act, due to the strange tax treatment of trusts and the conflicting resident status treatment under the Act and the *Canada–Barbados Income Tax Agreement Act, 1980* (the "Treaty"), Antle blatantly frustrated the object, spirit, and purpose of the rollover/attribution regime. The outcome was one that s. 73(1), the attribution rules, and s. 94(1)(*c*) specifically sought to prevent. Also, under the very clear language in s. 4.1 of the *Income Tax Convention Interpretation Act*, the GAAR can apply to benefits under the Treaty. As a result of the foregoing findings, the Minister's reassessment of Antle was affirmed, and the Trust's appeal was quashed, since it had not been validly created.

Antle et al., 2009 DTC 1305

Taxpayer liable under transferor–transferee joint liability provision on spouse's transfer of shares to RRSP

At a time when he owed tax of $36,823.88, the taxpayer's husband, D, transferred 46,848 shares of Icecap Equity Inc. (the "Shares") into her self-directed RRSP. On the assumption that the Shares had a fair market value ("FMV") of $28,108.80 at the time of their transfer by D to the taxpayer's RRSP (the "Transfer"), the Minister assessed her vicariously under s. 160(1) of the Act for $28,108.80. The taxpayer appealed to the Tax Court of Canada.

The taxpayer's appeal was dismissed. Whether D's intention at the time of the Transfer was or was not to defraud the Minister of an asset available to pay tax owing, intention is not relevant to the application of s. 160(1) of the Act. The Transfer gave the taxpayer exclusive control over the Shares. There was, therefore, a valid "transfer" of the Shares to the taxpayer's RRSP, whether or not she was aware of such transfer, and whether or not she consented to it. Also, there was ample evidence that the FMV of the Shares at the time of the Transfer was $28,108.80, so that the taxpayer's allegation that the FMV of the Shares at this time was nil was simply untenable. In addition, the taxpayer gave D no consideration for the Transfer, and the fact that he received a tax deduction in respect of the Transfer did not constitute a payment by her of valuable consideration for the Transfer for purposes of s. 160 of the Act. In light of the foregoing findings, the Minister's assessment was affirmed.

Woodland, 2009 DTC 1291

Unreported income amount was reduced and gross negligence penalties cancelled

During 2000 and 2001, the taxpayer carried on business as a stuntman. On the assumption that the taxpayer was carrying on additional businesses, the Minister conducted an analysis of the taxpayer's bank deposits and added unreported amounts to his income for 2000 and 2001. The Minister also disallowed numerous business expense deductions claimed and imposed late-filing penalties and penalties for gross negligence. The taxpayer appealed to the Tax Court of Canada.

The taxpayer's appeal was allowed in part. The taxpayer's testimony was made up largely of vague and imprecise recollections, and was uncorroborated by any reliable supporting documentation. The taxpayer did, however, adequately explain his deposit of six cheques totalling $10,300 from a Mr. Lelek ("Lelek"), who also corroborated these explanations. These cheques constituted reimbursements for materials purchased by the taxpayer for Lelek, loans from Lelek to the taxpayer, and reimbursements for auto and boat parts purchased by the taxpayer for Lelek. The $26,820.90 added to the taxpayer's income for 2001 should therefore be reduced by $10,300. The Minister also conceded that the taxpayer was entitled to certain business expense deductions in addition to those originally allowed. These concessions were reasonable in light of the lack of supporting documentation (e.g., an additional $3,809.75 for motor vehicle expenses). Although the late-filing penalties were justified, the Minister failed to establish that the taxpayer knowingly provided false information in his tax returns for the years under appeal. The penalties for gross negligence, therefore, should be deleted. The Minister was ordered to reassess accordingly.

Szlavy, 2009 DTC 1293

Transfers of property from non-arm's length corporation – Penalties not justified

The corporate taxpayer's business involved constructing houses for resale. Its sole shareholders and directing minds were Agata and Bogus Nowak (the "Nowaks"). The Minister's income tax and goods and services tax ("GST") assessments for the taxpayer's 2002, 2003, and 2004 taxation years were predicated on the general assumptions that: (a) the taxpayer had transferred certain properties to the Nowaks for amounts that were less than their fair market value ("FMV"); (b) net GST was underreported and input tax credit claims were overstated as a result of the said property transfers; (c) the taxpayer was not entitled to certain new housing rebates ("NHRs") assigned to it by the Nowaks, and arising from the property transfers; and (d) penalties under the *Excise Tax Act* for gross negligence were appropriate. The four properties involved were 1169 Srathcona Drive ("1169"), 3139 Signal Hill Drive ("3139"), 3135 Signal Hill Drive ("3135"), and 160 Strathlea Place ("160"). The taxpayer appealed to the Tax Court of Canada.

The taxpayer's appeal was allowed in part. The Minister was ordered to reassess to reflect the following findings: (a) 160 was transferred to the Nowaks at its FMV, so that no additional amounts should be added to the taxpayer's income as a result of this transfer; (b) the taxpayer was only a conduit for the purchase of 3139 by the Nowaks and since the taxpayer never acquired 3139, could not have disposed of it, which rendered moot the FMV issue respecting 3139; (c) since 160 was transferred to the Nowaks at its FMV, the taxpayer was entitled to the resulting NHR that the Nowaks had assigned to it; (d) GST was therefore not underreported on the taxpayer's transfer of 160; (e) 3139 was purchased by the Nowaks as a "primary place of residence", which entitled the taxpayer to the NHR that the Nowaks had validly assigned to it (see s. 254(2)(*b*) of the *Excise Tax Act*); (f) the taxpayer was a "builder" with respect to 3135, since it had a definable interest in that property; (g) the taxpayer was thus entitled to the NHR related to 3135 that the Nowaks had assigned to it; (h) the taxpayer provided the Nowaks with a service in assisting them with the construction of 1169, and this service was a taxable supply on which GST was payable; (i) such GST should be calculated as if the taxpayer's usual arm's length fees had been charged to the Nowaks; and (j) since the taxpayer made inquiries respecting the FMV of the properties involved in this case, the penalties imposed under the *Excise Tax Act* were unjustified and should be deleted.

Stan Wire Application Ltd., 2009 DTC 1294

Shareholder debt was reduced to take into account certain credits

During 1998 and 1999, the taxpayer was a shareholder of Gravel Ridge Investments Inc. ("Gravel Ridge"). In reassessing the taxpayer for 1998 and 1999, the Minister: (a) refused to accept as valid certain credits the taxpayer applied to his shareholder's loan account with Gravel Ridge to reduce the overall amount of the outstanding loan he owed Gravel Ridge (the "Credits"); (b) included $1,104,827 in the taxpayer's income for 1998 under s. 15(2) of the Act, which was the amount of the loan he owed to Gravel Ridge, which had not been reduced by the Credits, and which had not been repaid within the time frame set out in s. 15(2.6) of the Act; and (c) included in his income for 1998 and 1999 standby charges and operating cost benefits under ss. 6(1)(*e*), 6(1)(*k*), and 6(2) of the Act. On the taxpayer's appeal to the Tax Court of Canada, the Minister's counsel conceded that the standby charges and operating cost benefits should not be included in the taxpayer's income for 1998 and 1999.

The taxpayer's appeal was allowed in part. After an exhaustive review of all of the Credits in dispute, the conclusion was that credits totalling $826,455 should be applied to the taxpayer's shareholder's loan account with Gravel Ridge to reduce the amount of the outstanding loan he owed Gravel Ridge for purposes of calculating the s. 15(2) income inclusion for 1998.

Rudolph, 2009 DTC 1295

Director never removed as person in charge of company's affairs – Liable for unremitted source deductions and GST

The taxpayer and his wife were directors of AquaNorth Farms Inc. ("Farms"), and the taxpayer was also Farms' president and CEO. In 1995, Farms received a significant capital investment from Environmental Research and Development Capital Corporation ("ERD"), of which D. Rolfe ("Rolfe") was the managing director. By 2001, Farms was experiencing financial difficulties, and the relationship between Rolfe and the taxpayer had become acrimonious. On December 21, 2001, Rolfe wrote a letter to the taxpayer ("Rolfe's Letter"), purporting to terminate the taxpayer's responsibilities as a director of Farms and ordering him not to attend further Board meetings as a director. The taxpayer ignored Rolfe's Letter, and Rolfe obtained an interim receivership order, issued on January 22, 2002, appointing Ernst & Young as Farms' receiver. Rolfe's objective was to remove the taxpayer as a director of Farms and gain control of it to enable ERD to realize on its investment in Farms. On March 4, 2002, the Royal Bank, another of Farms' creditors, obtained a further order appointing Deloitte & Touche as receivers of Farm. On March 4, 2004, the Minister assessed the taxpayer as a director of Farms for the latter's unremitted payroll source deductions and goods and serv-

ices tax ("GST"). The taxpayer appealed to the Tax Court of Canada.

The taxpayer's appeal was dismissed. The taxpayer ignored Rolfe's Letter and ERD did not execute the January 22, 2002 receivership order because of the taxpayer's ongoing interactions with the Royal Bank and Deloitte & Touche. Neither Rolfe's Letter nor the January 22, 2002 receivership order, therefore, effectively removed the taxpayer as the person in charge of running Farms' affairs during the relevant period covered by the Minister's assessments. The applicable standard for directors' due diligence routinely being applied by the Tax Court is the objective/subjective standard established by the Federal Court of Appeal in *Soper v. The Queen* (97 DTC 5407), rather than the objective one that some commentators alleged was established by the Supreme Court of Canada in *Peoples Department Stores v. Wise*. Applying the *Soper* standard to the taxpayer's situation in this case, the conclusion was that he simply failed to prove his assertions that he had taken proactive steps, such as installing accounting systems, to ensure that Farms' payroll source deductions and GST were being remitted, even though he knew of Farms' financial difficulties. He was therefore unable to establish either that he was not a director of Farms at the relevant times, or that he had exercised due diligence in managing Farms' business affairs. The Minister's assessments were affirmed accordingly.

Liddle, 2009 DTC 1296

Mandatory T2 Electronic Filing

On November 10, 2009, the CRA released a reminder that for taxation years ending after 2009, the T2 corporation tax returns for corporations with gross revenues exceeding $1 million must be filed electronically. Penalties will be applied for taxation years ending after 2010 for such corporations that do not comply. Although it is not mandatory that corporations with gross revenues of less than $1 million file their returns via the Internet, the CRA noted that there are benefits from doing so, including fewer delays, elimination of delivery expenses, reduction in printing costs, and immediate confirmation of filing. The requirement for electronic filing by "prescribed corporations" was added by Bill C-10 (Royal Assent March 12, 2009) in new subsection 150.1(2.1), with the penalties for failing to do so added in new subsection 162(7.2).

2010 Employment Insurance Premiums

The T4127-JAN (Draft) sets out the 2010 Employment Insurance premiums. The premium rate is 1.73%, unchanged from 2009, for a maximum annual premium of $747.36. The employer rate is 1.4 times the employee rate. The 2010 premium rate for Quebec is 1.36%, for a maximum annual premium of $587.52. The 2010 maximum insurable earnings is $43,200, up from $42,300 in 2009.

Canada Pension Plan Maximum Pensionable Earnings for 2010

On November 3, 2009, the CRA announced that for 2010, the maximum pensionable earnings on which Canada Pension Plan contributions are made will be $47,200, increased from $46,300 in 2009. The basic exemption remains at $3,500 for 2010. The employee and employer contribution rates for 2010 remain at 4.95%, and the self-employed contribution rate remains at 9.9%. In 2010, the maximum employer and employee CPP contributions will be $2,163.15 (up from $2,118.60 in 2009), and the maximum self-employed contribution will be $4,326.30 (up from $4,237.20 in 2009).

Some Statistics on Tax Litigation

On November 22, 2009, at the Canadian Tax Foundation's 2009 Annual Conference, Johanne D'Auray, Assistant Deputy Attorney General, Tax Law Services, Department of Justice, as part of the panel discussing current tax cases, presented some statistics. She stated that the Appeals Branch handles between 50,000 to 70,000 objections per year, of which 92% are resolved administratively. The remaining 8% of the objections are appealed to the Tax Court of Canada. Of those appeals, about one-third are settled, one-third are withdrawn, and one-third go to hearing. In 2008, there were 3,170 income tax and GST appeals to the Tax Court. This number is actually down slightly from the number of appeals in each of 2005, 2006 and 2007. She stated that 161 tax cases were appealed to the Federal Court of Appeal in 2008-2009; 26 of which were filed by the Crown. On average, the FCA generally follows the Tax Court, allowing only 15% of the 161 appeals. Between 2003 to date, 18 federal and provincial tax cases have been decided by the Supreme Court of Canada. The Crown's position was upheld in 13 of those appeals and the taxpayer's in five.

2010 Federal Indexing Factor

On November 16, 2009, the CRA posted a draft version of its guide T4127-JAN, Payroll Deductions Formulas for Computer Programs – 91st Edition – Effective January 1, 2010. The information contained in the guide is final but according to the note on the CRA Web site, the version posted is in draft form because the formatting such as margin sizing, fonts, and spacing are not finalized. The CRA has published the guide in draft to accommodate payroll professionals who need the information now. The guide contains the formulas needed to calculate federal, provincial (except Quebec) and territorial income taxes, CPP and EI deductions effective January 1, 2010. As a result it contains the indexing factor for 2010 tax brackets and personal amounts.

The federal indexing factor for 2010 is 0.6%, therefore, to calculate the indexed income thresholds and personal amounts for 2010, the 2009 amounts should be multiplied by 1.006. The guide states that this factor of 1.006 is also applied to Saskatchewan, Yukon, Northwest Territories, and Nunavut. The indexing factors for the other provinces are as follows: New Brunswick at 1.020, Newfoundland and Labrador at 1.007, Ontario at 1.007, Alberta at 1.003, and British Columbia at 1.004. There is no indexing applied to Nova Scotia, Prince Edward Island, and Manitoba.

It is expected that as usual, later this year the CRA will release a Fact Sheet that lists all of the indexed amounts for next year. In the meantime, the personal income tax thresholds and some of the personal amounts for 2010 that are noted in the T4127-JAN (Draft) are shown below.

	2010 ($)	2009 ($)
Tax Bracket Thresholds		
Taxable income above which the 22% bracket begins	40,970	40,726
Taxable income above which the 26% bracket begins	81,941	81,452
Taxable income above which the 29% bracket begins	127,021	126,264
Selected Personal Amounts		
Basic personal amount	10,382	10,320
Spouse or common-law partner amount (maximum)	10,382	10,320
Amount for an eligible dependant (maximum)	10,382	10,320
Age amount	6,446	6,408
Amount for children under age 18 (maximum per child)	2,101	2,089
Canada employment amount (maximum)	1,051	1,044
Infirm dependant amount (maximum per dependant)	4,223	4,198
Caregiver amount (maximum per dependant)	4,223	4,198
Disability amount	7,239	7,196

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