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Is a Family Trust Vulnerable to the CRA? More Warning Signs: Subsections 75(2)–107(4.1)

In this month's article, I continue my discussion that began in last month's edition of TAX NOTES about warning signs that a family trust structure may be vulnerable to a CRA attack.

This month, I will focus on transactions that could trigger one of the most dangerous tax traps in the estate planning field. This is the application of subsection 107(4.1) which, in turn, is dependent on the application of the "reversionary trust rules" in subsection 75(2).[1] This provision is intended to preclude a rollout of the trust's assets – that is, on a tax deferred basis – to anyone other than the person from whom the property was received or his or her spouse[2] if subsection 75(2) was applicable at any time in respect of any property of the trust, and the contributor of such "tainted property" is alive ("in existence") at the time the property is distributed.[3]

Of course, one of the most important times at which the rollout is desired is just before the trust's 21st anniversary, in order to duck the tax in the trust that otherwise occurs on this anniversary by virtue of the deemed sale rules. The application of subsection 107(4.1) means that, rather than a rollout, there will be a deemed sale at fair market value when the property is distributed from the trust.[4] Note that the rectification of a situation such that subsection 75(2) no longer applies will not pre-empt the application of subsection 107(4.1) to property distributed by a trust.[5]

The reversionary trust rules themselves – in subsection 75(2) – apply if property contributed to the trust (or substituted property) is held on condition that it:

- may revert to the person from whom the property was directly or indirectly received;[6]

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- may pass to persons determined by the contributor after the creation of the trust;[7] or
- may not be disposed of during the contributor's life/existence without the consent or in accordance with the contributor's direction,[8] i.e., the contributor has a veto power over the disposition of the transferred property.

Because subsection 107(4.1) came into effect in the late '80s and did not receive much attention at first, trusts which are now reaching their 21st anniversary may often overlook the impact of this provision.[9]

Sign Sign Everywhere a Sign

The following are some common situations where subsection 75(2) – and potentially subsection 107(4.1) – may apply:

- The contributor is a beneficiary of the trust.[10] This may be the case if the contributor is a contingent beneficiary, e.g., if other beneficiaries pass away. (However, there is a distinction where the trust property reverts to the contributor by operation of law because of a failure of the trust, e.g., if the trust fails because there are no beneficiaries left to whom the property can be distributed.)
- The trust trips over a subsection 75(2) "technicality". The CRA interprets the reversionary trust rules quite strictly. An example of a situation where a trust may trip over subsection 75(2), and therefore subsection 107(4.1), is if there is a default distribution mechanism (e.g., if the trustees fail to exercise their discretion to distribute) which is dependent upon the provisions of the contributor's will, i.e., because the property may pass to a person determined by the contributor.[11]
- A beneficiary buys or sells property to the trust, even if at fair market value.[12] Although there is an exception for a *bona fide* loan to a trust, there is not an exception for other transfers, even if at fair market value. For example, suppose that an adult child is a beneficiary of a family trust (or an estate, for that matter), and the trust holds, say, a vacation property. If the child decides to buy the vacation property from the trust at fair market value, he or she will have transferred property (i.e., cash) to the trust. As the child is also the beneficiary, the cash (or property substituted for it) could revert to the child.[13]
- A beneficiary defrays the trust's expenses e.g., by advancing cash to allow the trust to pay a bill. Could subsection 107(4.1) be applicable in such circumstances? About a year ago, a release from a major accounting firm suggested that no one should put additional money or other assets into the trust, or pay the trust's expenses. While this is certainly conservative and prudent advice, another alternative may be to account for the payment as a loan to the trust. This approach may be more problematic if the trust doesn't keep books and records (this might be the case if an estate freeze is undertaken and the trust simply holds common shares acquired for a nominal amount).[14]

One would hope that the CRA would not deny the rollout of assets from the trust, e.g., prior to its 21st anniversary, on the grounds that a few cheques were made out by beneficiaries over the years.[15] But there is no denying that the prudent thing to do is to pay such expenses out of the trust's income. For example, in a freeze-type structure, dividends could be declared from time to time to defray such expenses.

- The contributor has a "veto" over the disposition of the contributed property (or the power to determine who the property can pass to); for example, the contributor is a trustee and the trust stipulates that he or she must be part of any majority decisions by the trustees. Another instance in which a contributor may fall into these circumstances is if the other trustees resign or pass away, leaving the contributor as the sole trustee or one of two trustees.

In some of the situations in respect of the last point, subsection 75(2) may technically apply, but the CRA has indicated some administrative largesse. In general, where the issue stems from the exercise of an individual's duty as a trustee, a series of technical interpretations[16] indicate that the CRA may not apply subsections 75(2) and 107(4.1).[17] According to a recent technical interpretation, this administrative largesse could occur where the transferor is one of two trustees or unanimity is required for trustees' decisions. However, the CRA's largesse would not apply where a trust expressly requires the contributor's

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consent to any decision made by the trustees as a whole (this would include the situation where the trust stipulates that decisions are made by a majority of trustees provided that the trustee-contributor is one of that majority).[18] Also, the largesse would apparently not apply where the contributor is the sole trustee.

The administrative largesse is limited to situations in which the powers that otherwise run afoul of subsection 75(2) are exercised as a trustee in a fiduciary capacity versus powers reserved in some other capacity. Accordingly, the largesse would not apply where the contributor reserves a power of appointment over the contributed property.

I would like to make one last observation: over the years, I have been surprised at the number of structures involving family trusts that have turned out to have deficiencies. Perhaps one reason is that the structures may start out as "small dollar" files. But as the client's wealth accumulates, the dollar value of the structure increases, so that what once may have been the financial equivalent of a one-room shack becomes a castle – built on a foundation of sponge. If so, it may be time to take a second look at the structure – before the CRA puts it under a microscope.

– David Louis, tax partner, Minden Gross LLP, a member of MERITAS law firms worldwide. David's practice focuses on tax and estate planning for entrepreneurs and their corporations (dlouis@mindengross.com). These topics and others will be discussed in more detail in a CCH Webinar to be presented on June 16; see page 8 for details.

Notes:

[1] For fairly recent articles on these provisions, see "Subsection 75(2): The Spoiler", Brenda L. Crockett, 2005 CTJ 3, p. 806; and "Reversionary Trust Review", Robert Spenceley, ESTATE PLANNER No. 131, December 2005, and "Reversionary Trust Update", ESTATE PLANNER No. 141, October 2006.

[2] Or other individual in respect of whom subsection 73(1) would be applicable in respect of the contributor, including a former spouse, common-law partner or qualifying spouse trust. If a trust holds identical properties, some received from the contributor, the CRA will allow the trust to identify which properties are to be distributed to the contributor/spouse, etc., so as to avoid the application of subsection 107(4.1). See Document No. 9215065, August 7, 1992.

[3] Unlike subsection 75(2), if the contributor emigrates from Canada, subsection 107(4.1) will continue to apply.

[4] See subsection 107(2.1). It appears that the result of the distribution is that the resulting income would be taxable to the beneficiary. See Document No. 9823605, May 10, 1999.

[5] Also, it is the CRA's position that, although the trust may not have had any income attributable to the settlor of the trust under subsection 75(2) of the Act, subsection 107(4.1) still remains applicable. See Document No. 9207365, July 22, 2002.

[6] Subparagraph 75(2)(*a*)(i).

[7] Subparagraph 75(2)(*a*)(ii).

[8] Paragraph 75(2)(*b*).

[9] Counter strategies may exist; these are beyond the scope of this article.

[10] Presumably, the trust will specifically provide that it is irrevocable.

[11] Per subparagraph 75(2)(*a*)(ii). Similarly, a power of appointment to be exercised through the will of a beneficiary will be problematic because the property could revert to the contributor under the will (per subparagraph 75(2)(*a*)(i)), unless the terms of the power prevents the donee of the power from appointing the contributor. However, if the property becomes part of the beneficiary's estate, the reversionary conditions in subparagraph 75(2)(*a*)(i) would not be considered to be satisfied with respect to the potential acquisition of the property by the contributor in accordance with the beneficiary's will. See Document Nos. 2002-0116535, February 19, 2002; 2002-0139205, July 22, 2002; and 2002-0162855, April 25, 2003.

Another noteworthy situation in which subparagraph 75(2)(*a*)(i) might apply is where the trust subscribes to shares of a corporation which is also a beneficiary of the trust. Although this was originally identified as problematic, in Document No. 2006-0218501E5, March 9, 2007, the CRA reconsidered its position, indicating that subsection 75 (2) of the Act should not be applied where a trust subscribed to shares of a corporation for fair market value consideration, on the premise that the corporation did not own the shares prior to their issuance to the trust. (If the shares are issued at less than fair market value, subsection 75(2) could apply, based on "*Kieboom*-type" reasoning.) The non-application of subsection 75(2) has been extended to dividends and proceeds of the redemption of the shares (see Document No. 2007-0243241C6, 2007 APFF Round Table, Question 13).

[12] In this point and the next, transactions with trustees may also be problematic, if the trustee has powers specified in subparagraph 75(2)(*a*)(ii) or paragraph 75(2)(*b*).

[13] If it did so, it appears that the property or substituted property would not be subject to subsection 107(4.1) by virtue of subparagraph 107(4.1)(*c*)(i). However, it appears that, in the absence of administrative largesse, the situation would leave other beneficiaries subject to subsection 107(4.1).

[14] It may be prudent to insert a clause in the trust that any such payment is deemed to be a loan rather than a contribution.

[15] However, in Document No. 9610435, August 13, 1996, the CRA indicates that the value of the property, nominal or otherwise, would not affect the application of subsection 107(4.1).

[16] Including Document No. 2000-0042505, April 30, 2001; Document No. 2001-0067955 January 3, 2002; Document No. 2003-0050671E5 April 5, 2004 ; Document No. 2004-0086921C6 (2004 APFF Round Table Question 24) October 8, 2004; Document No. 2008-0292061E5 October 27, 2008.

[17] For example, in Document No. 2001-0067955 the CRA indicates that, in respect of subparagraph 75(2)(*a*)(ii) (property passing to persons determined by the contributor):

> Where the beneficiaries under a trust are named in the trust indenture and cannot be modified (i.e., the person from whom the property was received by the trust cannot select additional beneficiaries after the creation of the trust), subparagraph 75(2)(*a*)(ii) is generally not considered applicable. This is true even though the person from whom the property was transferred to the trust may be able to determine the amount of the trust property that is to be distributed to beneficiaries already identified in the trust documents. However, subparagraph 75(2)(*a*)(ii) is worded broadly and there could be exceptions to this general position depending on the situation.

In respect of paragraph 75(2)(*b*) (property cannot be disposed of without the contributor's consent or in accordance with the contributor's direction):

> It is our view that the condition in paragraph 75(2)(*b*) might not be met in respect of property which is contributed to the trust by a person who is one of two or more co-trustees acting in a fiduciary capacity in administering the trust property where the property is subject to standard terms ordinarily found in trust indentures and there are no specific terms outlining how the trust property is to be dealt with

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[18] Document No. 2008-0292061E5 October 27, 2008.

Proposed Changes to Deferred Stock Option Benefits (Oh what a relief it is . . . Or is it?)

In February 2000, the federal government tabled a Budget which included provisions proposing a deferral, in certain circumstances, in respect of the employment income to be recognized where employees of a non-CCPC exercise stock options granted to them by their employer.[1] It was proposed that, where a qualifying person granted an option to issue shares of the qualifying person (or a non-arm's length qualifying person) to an employee, and the employee filed the appropriate election, the employment income which would otherwise be included in income in the year the option is exercised, would be deferred until the taxation year in which the employee disposes of, or exchanges, the shares. The deferral was to be subject to an annual limit of $100,000. It was noted that the proposed provisions were generally similar to those for incentive stock options in the United States.

The Budget 2000 documents indicated that the employee stock option provisions were being amended because many corporations used stock options to encourage their employees to take an ownership stake in the corporation, most notably in the fast growing high technology industries. It was noted that stock options provide employees with the right to acquire shares in the employer for a predetermined price, they assist corporations in attracting and retaining high caliber workers, and that the proposed amendments would make the Canadian tax treatment of employee stock options more competitive with the United States. The Budget 2000 provisions came into force effective February 28, 2000.

Fast forward to the year 2010. While the intent of these provisions may have been meritorious – the results have (in some cases) been less than desirable, particularly in the high technology industries. For example, some employees who took advantage of the special election were able to defer significant amounts of employment income, but the value of the shares acquired subsequently plummeted to a point where the income taxes payable in respect of the deferred employment income were greater than the proceeds of disposition received from the sale of the shares. Not surprisingly, some employees who disposed of their shares cried foul claiming that the tax system was operating unfairly because, in their view, they never "received" the employment income yet were required to pay income taxes on the full amount.

As advisors are aware, once a share is acquired pursuant to an employee stock option plan, a subsequent drop in the market value of the share is generally treated as a capital loss (or capital gain in the case of an increase). A significant drop in value is an unfortunate turn of events from the employee's perspective but the view of the Canada Revenue Agency is that this is a market risk the employee took when choosing to hold the shares acquired pursuant to the stock option plan. There are several technical interpretations issued by the Canada Revenue Agency addressing this issue.[2] The Department of Finance also examined this issue in 2002. The Joint Committee on Taxation submitted a letter dated March 15, 2002, recommending that the ITA be amended to allow any capital loss realized on the disposition of such shares to offset the income otherwise realized on the exercise of the option. The Department of Finance refused to provide such relief, equating employees who exercise stock options and choose to hold the shares to individuals acquiring shares with after-tax or borrowed dollars. That is, each investor who chooses to hold shares accepts a market risk in the expectation of a return on investment including future appreciation of the value of the share.

Notwithstanding the foregoing, two Remission Orders were granted in respect of former employees of SDL Optics, Inc.[3] According to the Remission Orders issued, the tax relief was in respect of employment income calculated pursuant to subsection 7(1).

Employees have made various arguments to obtain tax relief, such as claiming that the losses were on account of income and not capital. These arguments were rejected in *Ellis*[4] and *Baird*[5] but accepted in *Howard*.[6] In *Howard*, the employee was considered to be a trader or dealer with respect to his employer's shares and had special knowledge and expertise in his employer's operations and the market. As a result, the losses realized by the employee on disposition of the optioned shares were considered to be losses from a business.

Budget 2010 was tabled on March 4, 2010. It contains four significant proposed changes to the taxation of employee stock options. First, changes are proposed to eliminate the "double-dip" that may occur where an employee "cashes-out" of his or her stock options and is required to include only 50% of the employment income in income while the employer is entitled to a full deduction of the amount paid in determining its income from business. Second, changes are proposed to clarify existing withholding tax requirements to ensure that an amount in respect of tax on the full amount (not just 50%) of the employment income associated with the issuance of a share is required to be remitted by the employer at the same time as the share is issued. These measures attempt to avoid situations in which an employee is unable to meet his or her tax obligations as a result of a decrease in the value of the shares. Third, changes are proposed to eliminate the election permitting a deferral of the employment income for non-CCPCs. Finally, changes are proposed that will provide tax relief where employees elected to defer the employment income and have experienced financial loss as a result of a decline of the value of the shares acquired. These latter changes are the subject of this article.

Budget 2010 proposes that, where an employee has exercised an option to acquire shares, has made an election pursuant to subsection 7(10) in a prior taxation year to defer the employment income, and the income tax liability arising in respect of the employment income in the year the shares are sold is greater than the proceeds of disposition of the optioned shares, then the employee may choose to elect to pay a special tax for the year equal to

the proceeds of disposition, if any, from the sale or other disposition of the optioned shares. Where an employee files the proposed election the following will result:[7]

(a) in determining taxable income, the employee may claim a deduction equal to the full amount of the employment income (as opposed to 50% as currently provided by paragraphs 110(1)(*d*) and (*d*.1));

(b) an amount equal to one-half of the lesser of:

(i) the amount otherwise included in employment income;

(ii) the capital loss from the disposition of the share,

is required to be included in the employee's income as a taxable capital gain in the same taxation year as the shares were disposed of. This deemed taxable capital gain may be offset by the allowable capital loss arising from the disposition of the optioned share, provided the loss is not otherwise utilized by the employee;

(c) a special tax equal to the employee's proceeds of disposition of the optioned shares (2/3 of the proceeds of disposition for residents of Quebec) is payable in the year of disposition; and

(d) the deemed taxable capital gain is disregarded for purposes of the definition "adjusted income" for purposes of certain credits (e.g., GST).

An election filed outside of the normal reassessment period (within the meaning of subsection 152(3.1)) is considered to be an application made by the employee, under subsection 152(4.2), to the Minister of National Revenue for a determination of a refund or reduction of tax. Such a determination is at the discretion of the Minister of National Revenue and must be made on or before the day that is 10 calendar years after the end of the taxation year of the employee to which the refund or reduction relates. This will permit reassessments to occur in respect of statute-barred taxation years. Advisors should consult with their clients as soon as possible in 2010 to avoid losing the opportunity to apply these proposed provisions for the 2000 taxation year.

Only shares disposed of in respect of which the related employment income was deferred pursuant to the election in subsection 7(10) will qualify for this proposed tax treatment. Employees who disposed of such shares prior to 2010 will have the opportunity to file the proposed election on or before the filing due-date of their 2010 taxation year (April 30, 2011 or June 15, 2011, as the case may be). Individuals who have not disposed of their optioned shares prior to 2010 may choose to do so prior to 2015. They will then have until their filing due-date for the taxation year of disposition to file the proposed election adopting this treatment (generally April 30, 2015 or June 15, 2015, as the case may be). Where an individual does not dispose of his or her optioned shares prior to 2015, it appears that the employment income deferral continues until the optioned shares are disposed of, albeit without the benefit of the proposed election and tax relief.

To Elect or Not?

On its face, the proposed election appears to be quite beneficial. It would appear that choosing to pay a tax equal to the proceeds of disposition rather than paying a greater tax in respect of the employment income is a simple decision to make. What escapes the eye, however, is the value of the capital losses that are lost when the employee files the proposed election. Recall that, on filing the proposed election, the employee is deemed to have realized a taxable capital gain equal to one-half of the lesser of the employment income or the capital loss arising on the sale of optioned shares. The deemed taxable capital gain will be offset (partially or in full) by the allowable capital loss arising from the disposition of the optioned share. This begs the question – what is the value of the allowable capital loss that is used and, therefore, not available to offset other taxable capital gains? This is best illustrated by example.

Assume that an employee acquires shares pursuant to an employment stock option plan at an exercise price of $2 per share. At that time, the shares traded at $10 per share. The employee elects to defer the employment income of $8 per share (assume the 50% stock option deduction is available pursuant to paragraph 110(1)(*d*)). The employee's marginal income tax rate is 46.41%. Therefore, the tax deferral in respect of the employment income, net of the 50% stock option deduction, is $1.86 per share. The shares currently trade at $1 per share. In these circumstances, it appears beneficial to file the proposed election, as shown below:

Disposition of Share

Proceeds of disposition (POD)	$ 1.00
Adjusted cost base	10.00
Capital loss	($9.00)
Allowable capital loss	($4.50)

Tax Consequences

Tax payable on net employment income if proposed election not filed	$1.86
Tax payable if proposed election filed (POD)	(1.00)
Benefit by filing proposed election	$0.86

By filing the proposed election, the employee is deemed to have realized a taxable capital gain equal to $4 (1/2 of the lesser of the employment income and the capital loss arising on sale of the optioned shares). Therefore, the employee must use $4 of the $4.50 allowable capital loss realized on the disposition of the optioned shares to shelter the deemed taxable capital gain from immediate taxation. This leaves an allowable capital loss of $0.50 per share. Assuming the employee is able to utilize this allowable capital loss in determining taxable income in the current year, the employee's further tax savings from utilizing the allowable capital loss will amount to $0.23 per share. This is illustrated below:

Allowable capital loss from disposition of shares	$4.50
Utilized to shelter deemed taxable capital gain	(4.00)
Balance	$0.50
Potential tax savings at 46.41%	$0.23

The above analysis suggests that the proposed election is worth $1.09 to the employee ($0.86 + $0.23). Consider, however, the tax consequences arising where the employee is able to utilize the entire allowable capital loss arising from a disposition of the optioned shares as a deduction in determining the net taxable capital gains in the current taxation year. This is not an outside possibility given the rather dramatic recovery of the Canadian stock markets in 2009. By filing the proposed election, the employee will lose a $4 allowable capital loss, which is worth $1.86 ($4 × 46.41% = $1.86). The employee saves the tax on the net employment income which is also worth $1.86 (50% of $8 × 46.41%) but must pay a tax equal to the proceeds of disposition received from the sale of the shares. There is a net cash loss realized of $1 ($1.86 - $1.86 - $1) per share by filing the proposed election. Of course, this is true only if the employee had other taxable capital gains in the same year. If the employee does not expect to have taxable capital gains in the near future, then the cost of not filing the proposed election is $0.86. These concepts are illustrated by the cash flow summary below (based upon the above example):

	Proposed election	No election but other TCG	No election and no other TCG
Proceeds of disposition	$1.00	$1.00	$1.00
Tax on "net" employment income benefit	n/a	(1.86)	(1.86)
Immediate tax savings from utilizing the allowable capital loss	0.23	2.09	n/a
Tax payable due to proposed election	(1.00)	n/a	n/a
Net to employee	$0.23	$1.23	($0.86)

As indicated above, if there are no other taxable capital gains in the same taxation year, the employee is better off by $0.86 if he or she files the proposed election. However, what should the employee do if he or she expects to realize a taxable capital gain in the next year or two such that the loss preserved by not filing the proposed election can be fully or partially utilized? This requires an analysis of the time value of money to determine the value of the tax savings in today's dollars.

While the above analysis is complicated, and can be made more complicated by introducing the concept of time value of money, it does not appear that there are a significant number of circumstances where an employee would want to file the proposed election. Generally, the proposed election only makes economic sense where the employee has deferred a significant amount of employment income, the shares have suffered a significant loss of value and the employee has no reasonable expectation of realizing a taxable capital gain in the near future. In fairness to the Department of Finance, this is likely exactly what was desired. However, advisors must be careful not to rush into recommending the proposed election until they take into account potential future taxable capital gains that the client may realize. Where an employee is able to utilize the capital loss arising on disposition of the optioned shares in the same taxation year, there are no circumstances under which the employee would benefit from filing the proposed election. However, the analysis will be different from the above if the employee is not entitled to the 50% stock option deduction. Finally, advisors should consider the availability of an allowable capital loss in the year of death, which may be applied against income from any source and not just against taxable capital gains.

As a cautionary note, at the date of writing this article, the Department of Finance has not released draft legislation in respect of the tax relief in respect of deferred stock option benefits. As such, the comments contained in this article are based on the Notice of Ways and Means Motion contained in Annex 5 to the Budget 2010 documents. The draft legislation actually released may contain changes not discussed in this article.

– Mark H. Woltersdorf, Partner in the Tax Department in the Edmonton Office of Fraser Milner Casgrain LLP

Corporate Tax Rates – Status for Accounting Purposes

As subscribers to the CANADA INCOME TAX GUIDE are aware, tables prepared by PricewaterhouseCoopers LLP showing federal, provincial and territorial personal and corporate tax rates and credits for each year are reproduced in the CANADA INCOME TAX GUIDE Online and on DVD, are accessed through the "Quick Links". A new table has been added that shows the status for accounting purposes as at April 30, 2010 of corporate tax rates (general, manufacturing and processing and CCPC) from 2009 to 2014. This table can currently be accessed on CCH Online under the CANADA INCOME TAX GUIDE Quick Links.

Recent Cases

Taxpayer was entitled to a capital loss, not a terminal loss for the demolition of its hotel

After renting out a hotel it owned for 20 years, the corporate taxpayer demolished the hotel in May 2004, and

completed the construction of a new commercial building on the same property by November 2004. In reassessing the taxpayer for 2004, the Minister denied it the terminal loss claimed on its disposition of the hotel, and treated this loss as an allowable capital loss equal to one-half of the terminal loss claimed. (The terminal loss claimed was equal to the whole of the undepreciated capital cost of the hotel.) After the taxpayer's request for a determination of the loss in question, the Minister again treated the loss as an allowable capital loss, relying on s. 13(21.1)(*b*) of the *Income Tax Act* (the "Act"). The taxpayer appealed to the Tax Court of Canada.

The taxpayer's appeal was dismissed. Paragraph 13(21.1)(*a*) of the Act, which accords terminal loss treatment to losses on the disposition of a building, only applies when the land subjacent to or immediately contiguous to and necessary for the use of the building is also disposed of in the same taxation year as the one in which the disposition of the building took place. This was not the taxpayer's situation and, therefore, its argument that s. 13(21.1)(*a*) applied was untenable. The Minister, therefore, was correct in allowing the taxpayer an allowable capital loss under s. 13(21.1)(*b*), equal to one-half of the terminal loss claimed.

9136-6872 Québec Inc., 2010 DTC 1110

Transfer from an RRSP to an RPP, subsequently deregistered retroactively, was taxable

The CRA notified Canadian Corporation Creations Centre ("CCCC") that its registered pension plan (the "Plan") had been registered effective July 24, 2000. The CRA subsequently revoked the registration of the Plan retroactively to July 24, 2000 for non-compliance with the registration conditions prescribed in s. 8501(1) of the Income Tax Regulations. Before the Plan's registration had been retroactively revoked, the taxpayer transferred to it the proceeds of his RRSP totalling $12,751, and in return received a loan of $7,466 from National Business Investment, an organization associated with CCCC. In reassessing the taxpayer for 2001, the Minister added $10,665 to his income under s. 146(8) of the *Income Tax Act* (based on a calculation grossing up the amount of the loan, in the absence of information of the actual amount of the RRSP transferred). The taxpayer appealed to the Tax Court of Canada.

The taxpayer's appeal was dismissed. The rollover provisions of s. 146(16) of the Act were of no assistance to the taxpayer, since the Plan was retroactively deregistered as of the date of its registration, and therefore was never, by law, a registered pension plan when the $12,751 was transferred to it from the taxpayer's RRSP. By giving up control of the whole $12,751 in his RRSP, the taxpayer constructively received that $12,751 "as a benefit" from his RRSP. The $12,751, therefore, should have been included in his income under s. 146(8) of the Act and was also required to be included in his income under the indirect payment provisions of s. 56(2), although the Minister was limited to the amount of the assessment. The Minister's reassessment was affirmed accordingly.

Astorino, 2010 DTC 1112

Taxpayer jointly liable for tax liability of corporation that paid him dividends

The taxpayer was the sole shareholder and director of a holding corporation (the "Corporation"). The Corporation in turn held 95% of the shares of an operating corporation, SPER. During 1999, 2000, and 2001, the Corporation paid the taxpayer dividends totalling in excess of $40,000 (the "Dividends"). As of March 2, 2007, the Corporation owed tax of $18,348. The Minister assessed the taxpayer for $18,348 under the vicarious liability provisions of s. 160(1) of the *Income Tax Act*. The taxpayer appealed to the Tax Court of Canada.

The taxpayer's appeal was dismissed. For the purposes of s. 160(1), corporate dividends constitute transfers of property without consideration. In this case, the taxpayer and the Corporation were clearly not at arm's length. The Dividends did not constitute amounts paid to the taxpayer by the Corporation for work he did, despite his allegations to the contrary. The Minister's assessment was, therefore, justified under s. 160(1) of the Act and was affirmed accordingly.

Bruneau, 2010 DTC 1113

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