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DISPOSITIONS OF PARTNERSHIP INTERESTS — NAVIGATING THE AMENDMENTS TO SECTION 100 OF THE *INCOME TAX ACT*[1]

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In its 2012 Budget, the federal government implemented a number of changes to the taxation of partnership interests and their disposition. Some of the most significant changes were the proposed amendments to section 100 of the *Income Tax Act* (the "Act") with respect to the taxation of capital gains on the disposition of partnership interests to specified persons. The amendments are designed to prevent the conversion of recapture and other income gains on the assets of the partnership into capital gains through the disposition of the partnership interest instead.

Speaking generally, a taxpayer will hold a partnership interest as capital property, regardless of whether the partnership holds non-depreciable capital or inventory assets (or depreciable assets). That means that a partner can in essence convert income into capital gains by transferring inventory or depreciable assets to a partnership and then selling the partnership units.

Parliament knows that sort of conversion can take place, but the Act does not prevent it, presumably because at some point the partnership will sell the inventory and the then current partner will have to include the inventory gain in income, so all that is at stake is a deferral of the tax on the other 50% of the income rather than an exemption. Additionally, when one considers that the amount of gain potentially taxable may have been doubled when the first partner rolled the inventory into the partnership and took back a partnership interest with a low adjusted cost base and high value, the deferral is relatively inconsequential.

Apart from section 100, however, the possibility exists that a partner could sell the partnership interest to a non-resident or a tax-exempt person. Under some circumstances, that new partner would not pay tax on the income allocated to him or her when the partnership sells the inventory. That would be too good to be true.

To prevent that, subsection 100(1) (prior to the proposed amendments) set out the calculation of a taxpayer's taxable capital gain on the disposition of an interest in a partnership where that partnership interest was disposed of to a person exempt from tax under section 149. His or her gain would be equal to (a) $^1/_2$ of such portion of the taxpayer's capital gain as may reasonably be regarded as attributable to increases in the value of any property of the partnership that is capital property other than depreciable property, plus (b) the whole of the remaining portion of that capital gain. In other words, the proceeds were deemed to include 100% of the gain to the extent that the gain was attributable to depreciable assets held by the partnership, thereby replicating the tax effect the partner would have had had the partnership sold the depreciable assets and allocated the recapture to him or her.

Prior to proposed amendments, subsection 100(1) applied only to direct transfers of partnership interests, assuming the general anti-avoidance rule ("GAAR") did not apply. As such, the only due diligence a practitioner needed to do with respect to determining whether subsection 100(1) would apply was to inquire whether the purchaser was a tax-exempt entity. Consequently, a vendor could transfer its partnership interest indirectly to a tax-exempt entity by transferring it to a trust or partnership in which that entity was a beneficiary or partner and avoid the application of subsection 100(1) to the disposition. While the Canada Revenue Agency scrutinized these transactions to determine whether they were caught by any specific anti-avoidance provisions or under GAAR, the Department of Finance determined that legislative changes were necessary to limit the amount of tax leakage on the disposition of partnership interests.[2] The Department of Finance also noted that non-resident purchasers were being used to convert income gains on the assets of a partnership into capital gains through the disposition of the partnership interest instead and that dispositions to such persons should also be caught by subsection 100(1).[3]

As a result, subsection 100(1.1) was enacted to expand the categories of transferees that cause subsection 100(1) to apply on the disposition of an interest in a partnership. As of August 14, 2012, subsection 100(1) applies to dispositions of partnership interests to non-residents,[4] partnerships in which non-residents or tax-exempt entities are partners,[5] and trusts of which tax-exempt entities are beneficiaries,[6] as well as continuing to apply to dispositions to tax-exempt entities. The trust and partnership categories were added to prevent non-residents and tax-exempt entities from acquiring partnership interests indirectly through fiscally transparent entities. The application of subsection 100(1) to dispositions of partnership interests to non-residents is relatively straightforward. However, the amendments to include dispositions to certain trusts and partnerships are significantly more complex, particularly where the beneficiaries or partners of such entities are themselves partnerships or trusts.

Paragraph 100(1.1)(*c*) causes subsection 100(1) to apply where a vendor sells his or her interest in a partnership to another partnership and a tax-exempt entity[7] or a non-resident[8] has an interest in the purchasing partnership, regardless of the value of the interest such entity has in the purchasing partnership. Furthermore, subsection 100(1) will apply to the sale of a partnership interest to another partnership if any one of the purchasing partnership's partners is a trust that has a beneficiary that is either another trust or a tax-exempt entity and if the fair market value of the interests of those beneficiaries exceeds 10% of the fair market value of all of the beneficiaries' interests in the trust.[9] It is critical to note that if a trust has another trust as a beneficiary, and the interest of that beneficiary exceeds 10% of the fair market value of all of the beneficiaries' interest in the trust, and if the first trust has an interest in a purchasing partnership, then the purchasing partnership will be included in paragraph 100(1.1)(*c*) and the disposition will be subject to subsection 100(1), regardless of whether a tax-exempt entity is a beneficiary of the second trust.

The sale of a partnership interest by a taxpayer to another partnership will also be caught by paragraph 100(1.1)(*c*) if one or more partnerships has an interest in the purchasing partnership and any one of the entities referenced in subparagraph 100(1.1)(*c*)(i), (ii), or (iii) has an interest in that partnership, including an indirect interest through another partnership. In the case of stacked partnerships, this means that if any partner in the chain is a tax-exempt entity, non-resident, or trust meeting the conditions set out in subparagraph 100(1.1)(*c*)(iii), then the vending partner will be caught by paragraph 100(1.1)(*c*) and the disposition will be subject to subsection 100(1). As such, due diligence as to the ultimate owners of the purchaser of partnership interests must be carried out where there are stacked partnerships, particularly as there is no minimum ownership threshold. This will be particularly difficult where the purchasing partnership is widely held and, even more so, where such partnership is publicly traded.

Similarly, paragraph 100(1.1)(*d*) deals with indirect acquisitions of partnership interests using trusts. It is important to note that paragraph 100(1.1)(*d*) includes trusts only where the beneficiaries are tax-exempt entities,[10] partnerships in which a trust or a tax-exempt entity has an interest and the fair market value of the interests exceeds 10% of the fair market value of all of the partners' interests in the partnership,[11] or trusts where one of the beneficiaries is either another trust or a tax-exempt entity and the fair market value of the interests of those beneficiaries exceeds 10% of the fair market value of all of the beneficiaries' interests in the trust.[12] However, paragraph 100(1.1)(*d*) does not include a trust merely because it has a non-resident beneficiary. While the Department of Finance Explanatory Notes do not explain the reason for this, one can only assume that it is because accrued income gains on the assets of a partnership cannot be avoided by a non-resident through the use of a trust, due to Part XII.2 tax.[13]

While the addition of paragraph 100(1.1)(*d*) is meant to prevent vendors from disposing indirectly of their partnership interests to tax-exempt entities and therefore avoiding subsection 100(1), paragraph 100(1.1)(*d*) is drafted such that it will include *any* trust that has a tax-exempt entity as a beneficiary. For example, a family trust in which one of the discretionary beneficiaries is a charity would be included under paragraph 100(1.1)(*d*), even if the trustees have never allocated any income to that beneficiary and have no intention of allocating income to that beneficiary. As noted above with respect to paragraph 100(1.1)(*c*), in the case of stacked trusts it may not matter whether any tax-exempt person has an ultimate interest in one of the trusts for the trust to be included under paragraph 100(1.1)(*d*). If the purchaser is a trust with a partnership as a beneficiary, for example, and another trust holds 10% or more of the fair market value of all the interests in the beneficiary partnership, then the purchaser trust will be included under paragraph 100(1.1)(*d*) and subsection 100(1) will apply to the vending partner, regardless of whether the second trust has any tax-exempt beneficiaries.

New subsections 100(1.2) and (1.3) set out two exceptions to the application of subsection 100(1). Subsection 100(1.2) sets out a *de minimis* exception where a taxpayer disposes of 10% or less of its partnership interest to a partnership or trust included under either paragraph 100(1.1)(*c*) or (*d*). Curiously, this *de minimis* exception does not apply where the 10% or less sale is directly to a non-resident or tax-exempt entity. This exception also does not apply where the purchasing trust is a discretionary trust with respect to either income or capital.

Subsection 100(1.3) applies where the purchaser of the partnership interest is a non-resident and partnership property is used, both immediately before and after the acquisition of the partnership interest, in carrying on business in Canada through a permanent establishment and that property represents 90% or more of the fair market value of all the assets of the partnership. It appears that this exemption was included because under Article XIII of Canada's income tax treaties, non-residents are taxed in the same manner as Canadian residents on income earned from the disposition of such assets. However, in its submissions on the 2012 Budget proposals, the Joint Committee noted that this exemption is unduly narrow and should be expanded to include all taxable Canadian property and non-depreciable capital assets, as non-residents would be taxed in the same manner as Canadian residents on the disposition of taxable Canadian property and the taxation of gains attributable to non-depreciable capital assets is not altered by subsection 100(1), so no tax leakage would occur.[14] Finance did not alter the amendments to take that suggestion into account. The Explanatory Notes for subsection 100(1.3) provide no guidance on why the exemption was limited in this manner.[15]

Additionally, the exception in subsection 100(1.3) is limited to direct acquisitions by non-residents. This means that if the purchaser is a partnership with a non-resident partner, this exception will not be available regardless of whether the asset conditions in paragraphs 100(1.3)(*a*) and (*b*) are met. The reason for this discrepancy is unknown; it would have been easy to expand the exception to "a person referred to in paragraph (1.1)(*b*) or subparagraph (1.1)(*c*)(ii)".

The purpose of the amendments to section 100 is clear: to prevent a taxpayer from avoiding an income inclusion by disposing of an interest in a partnership to non-residents or, indirectly, to tax-exempt entities instead of selling the assets of the partnership to such purchasers. However, it is questionable whether the amendments are the most effective way of achieving that purpose. As noted by Blanchet[16] and the Joint Committee, the limitations on the exceptions in subsection 100(1.2) and (1.3) appear to be arbitrary and are not in line with the harm the amendments are intended to prevent.

The amendments to subsection 100(1) and the addition of subsections 100(1.1) to (1.3)[17] are of critical importance to both tax practitioners and corporate lawyers, as significantly more due diligence must now be carried out. First, it must be ascertained whether the purchaser of the interest is a purchaser described in subsection 100(1.1). Where the purchaser is a partnership, practitioners must ensure that they look through the entity to determine whether *any* one of the partners is a non-resident, tax-exempt entity or trust. With respect to a trust, it is crucial for practitioners to remember that even if a tax-exempt entity is just one of many discretionary beneficiaries of the trust, this will cause the purchaser to be subject to subsection 100(1). Finally, practitioners must be cognizant of the limitations on the exemptions set out in subsections 100(1.2) and (1.3), remember that subsection 100(1.2) applies to acquisitions by non-discretionary trusts and partnerships only, and recall that subsection 100(1.3) applies to direct acquisitions by non-residents only — not to indirect acquisitions by non-residents through another partnership.

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Notes:

[1] Joel Nitikman of Dentons Canada LLP, Vancouver, reviewed previous drafts of this article.

[2] Department of Finance, 2012 Federal Budget, Annex 4: Notice of Ways and Means Motion, paragraph 26.

[3] *Idem*, paragraph 24.

[4] Paragraph 100(1.1)(*b*).

[5] Paragraph 100(1.1)(*c*).

[6] Paragraph 100(1.1)(*d*).

[7] Subparagraph 100(1.1)(*c*)(i).

[8] Subparagraph 100(1.1)(*c*)(ii).

[9] Subparagraph 100(1.1)(*c*)(iii).

[10] Subparagraph 100(1.1)(*d*)(i).

[11] Subparagraph 100(1.1)(*d*)(ii).

[12] Subparagraph 100(1.1)(*d*)(iii).

[13] Blanchet, J., "Transactions Involving Interests in Partnerships", draft paper presented to the Canadian Tax Foundation's 63rd Tax Conference, 2012, at footnote 16.

[14] Joint Committee on Taxation of the Canadian Bar Association and the Canadian Institute of Chartered Accountants, "Re: August 14, 2012 Draft Legislative Proposals To Amend the *Income Tax Act* (Canada)," submission to Brian Ernewein, General Director, Tax Policy Branch, Tax Legislation Division, Department of Finance, September 13, 2012.

[15] Department of Finance, Explanatory Notes relating to the *Income Tax Act* and Regulations, August 14, 2012 at 23.

[16] See Footnote 13 above.

[17] The Department of Finance also added two anti-avoidance provisions in subsections 100(1.4) and (1.5). These provisions are not dealt with in this article, as they are in relation to the dilution, reduction, or alteration of a partner's interest in a partnership *other than* by way of a disposition for the purposes of avoiding the application of subsection 100(1). For further details on these rules, please see Kevin Yip, "Recent Legislation Affecting Partnerships and Foreign Affiliates — Subsection 88(1) and Section 100" in "Corporate Tax Planning," (2013), Vol. 61, No. 1, *Canadian Tax Journal*, 229.

DEPARTMENT OF FINANCE INVITES COMMENTS ON PROPOSED TREATY SHOPPING PREVENTION MEASURES

On August 12, 2013, the Tax Legislation Division of the Department of Finance's Tax Policy Branch announced it was inviting comments regarding proposed preventative measures pertaining to tax "treaty shopping". When non-residents not otherwise entitled to the benefits of a tax treaty with Canada seek — by way of an entity resident in a country with which Canada has concluded a tax treaty — to access indirect and unintended tax treaty benefits, tax treaty shopping is generally said to occur. Having previously made clear its preference for using bilateral tax treaties as a means of reducing Canadian tax imposed on residents of trading partners, the Canadian government is now seeking measures to protect the integrity of its 90-country-strong treaty network from those third-country residents who seek to access indirectly the benefits of that network by treaty shopping.

This request for comment is in conjunction with Finance Canada's release of its "Consultation Paper on Treaty Shopping — The Problem and Possible Solutions". While stakeholders are invited to comment upon any element of Finance Canada's consultation paper, specific questions highlighted to be commented upon include the following:

> ***Question 1*** *— The Government invites stakeholders to comment on the advantages and disadvantages of a domestic law approach, a treaty based approach, or a combination of both.*
>
> ***Question 2*** *— The Government invites stakeholders' comments on the relative merits of the various approaches to treaty shopping identified by the OECD as well as whether there are other approaches and types of rules that should be considered by Canada in evaluating how best to address the problem of treaty shopping.*
>
> ***Question 3*** *— The Government invites stakeholders' views on whether a general approach is preferred over a relatively more specific and objective approach.*
>
> ***Question 4*** *— The Government invites stakeholders' views on whether a main purpose test, if enacted in domestic tax laws, would be effective in preventing treaty shopping and achieving an acceptable level of certainty for taxpayers.*
>
> ***Question 5*** *— The Government invites input on which of the approaches (a main purpose approach or a more specific approach) strikes the best overall balance between effectiveness, certainty and simplicity, and ease of administration.*

> ***Question 6*** *— For stakeholders who favour a more specific approach over a main purpose approach, the Government invites input on the design of the conditions and the exceptions (e.g., the substantive business operations and derivative benefits exceptions) under a more specific approach as well as any other exceptions that should be considered under this approach with a view to ensuring the measure is effective and applies in a reasonably straightforward manner with predictable outcomes.*
>
> ***Question 7*** *— The Government invites stakeholders to comment on whether or not a domestic anti-treaty shopping rule should apply if a tax treaty contains a comprehensive anti-treaty shopping rule.*

The closing date for comments in the Department of Finance's consultation is December 13, 2013. Input can be submitted via email to Treaty.Shopping-Chalandage.Fiscal@fin.gc.ca, by fax to 613-992-2036, or in writing addressed to Treaty Shopping, Department of Finance, L'Esplanade Laurier, 17th Floor, East Tower, 140 O'Connor Street, Ottawa, Canada, K1A 0G5.

With the consent of submitting parties, the Department of Finance will post received comments on its website; parties so interested should provide comment electronically in plain text or PDF format, clearly indicate a preference that the submission be posted on the website, and clearly provide their name/the name of the organization they represent.

CRA ANNOUNCES TAXPAYER RELIEF PROVISIONS AVAILABLE TO CANADIAN TAXPAYERS AFFECTED BY THE DISASTER IN LAC-MÉGANTIC

On July 25, 2013, the Honourable Ministers of National Revenue and International Development and the Member of Parliament for Mégantic-L' Érable announced that taxpayer relief provisions are available to Canadian taxpayers who have been affected by the disaster in Lac-Mégantic. The Canada Revenue Agency will review taxpayer relief requests on a priority and case-by-case basis for applications to have interest/penalties waived or cancelled where taxpayers were unable to file returns/make payments on time owing to the disaster. Taxpayers can request such relief in writing using form RC4288, Request for Taxpayer Relief. Information Circular IC 07-1 (in conjunction with the information on the revised 10-year limitation period for interest relief) provides additional information on taxpayer relief provisions. For direct support in relation to taxpayer relief or any other federal tax obligation, impacted businesses can telephone 1-888-699-0735, extension 6312.

CRA ISSUES GUIDANCE FOR DRAFTING CHARITABLE REGISTRATION "PURPOSES"

On July 25, 2013, the Canada Revenue Agency issued Guidance CG-019, *How To Draft Purposes for Charitable Registration*. Guidance CG-019 replaces a number of previous policy summaries and statements, including Policy Statement CPS-004, *Applicants with Broad Object Clauses*; Summary Policy CSP-C01, *Charitable Purposes*; Summary Policy CSP-O01, *Objects (Charitable)*; Summary Policy CSP-O02, *Objects (Broad and Vague)*; and Summary Policy CSP-O03, *Objects (Standard)*. The purposes of an organization are the objectives that it is created to achieve, and Guidance CG-019 provides a recommended approach to drafting purposes (sometimes referred to as "objects") for

- organizations intending to apply for charitable registration under the *Income Tax Act*, and
- registered charities that are amending their existing purposes.

An organization's governing document(s) — which can include letters patent, articles of incorporation, trust, or constitution — must clearly state each of an organization's purposes. Canadian law requires that, to be registered as a charity under the *Income Tax Act*, an organization's purposes be exclusively charitable and define the scope of activities that can be engaged in by the organization. All of a registered charity's resources must be devoted to these activities, subject to limited exceptions.

RECENT CASES

Whether Minister justified in reassessing beyond normal reassessment period on ground taxpayer knowingly made a misrepresentation

During 2004, the taxpayer disposed of a one-half interest in a rental property he owned. His accountant erroneously advised him that instead of reporting the resulting capital gain in his 2004 return, he could defer reporting it until the year in which he disposed of the other half of the property. His accountant prepared his 2004 return on this basis, after discussing the matter thoroughly with him. In reassessing the taxpayer for 2004 beyond the normal reassessment period, the Minister added the unreported proceeds of disposition of the one-half interest in the taxpayer's property to his income for 2004. The taxpayer appealed to the Tax Court of Canada.

The taxpayer's appeal was allowed. The taxpayer had not been neglectful or careless, but had followed the professional advice of his accountant after a thorough discussion. Paragraph 152(4)(*a*) permits reassessments beyond the normal reassessment period where "the taxpayer or person filing the return" has made "any misrepresentation that is attributable to neglect, careless, or wilful default . . .". In this case, the taxpayer had made no misrepresentation, although his accountant who prepared the return clearly did so. The phrase "taxpayer or person filing the return" in paragraph 152(4)(*a*) is not, however, broad enough to encompass persons preparing the return, such as the taxpayer's accountant. The Minister, therefore, could not justify the reassessment beyond the normal reassessment period under subparagraph 152(4)(*a*)(i), and it was vacated accordingly.

— *Aridi*, 2013 DTC 1123

Minister failed to assess taxpayer with all due dispatch by implementing policy to delay processing of returns to discourage participation in certain tax shelter programs

The taxpayer commenced a judicial review application primarily to obtain *mandamus* to compel the Minister to examine her 2010 tax return. This was a test case where the Minister delayed examination of tax returns where certain claims were made for charitable donation tax credits. The underlying issue related to the taxpayer's participation in a tax shelter called Global Learning Gifting Initiative, where participants would donate cash and then receive further charitable credits by way of gifts-in-kind for software licences. Canada Revenue Agency ("CRA") offices in Winnipeg, Manitoba implemented a new policy to delay refunds until an audit was completed. At issue was whether the new policy was consistent with subsection 152(1) that the Minister assess "with all due dispatch".

The taxpayer's application was allowed. The CRA's new policy was aimed primarily to deter taxpayers from participating in the tax shelter program and was inconsistent with the federal and national nature of the Minister's obligation. Further, the delay in assessing the taxpayer was not truly related to examining her return and ascertaining her tax liability. The taxpayer was entitled to a declaration that the Minister failed to comply with the duty to assess with all due dispatch.

— *Ficek*, 2013 DTC 5104

Minister's GAAR-based assessments recharacterizing capital gains realized by family trust as dividends and imposing kiddie tax on trust's minor beneficiaries vacated

The taxpayers' father, Dr. G, was a dentist whose practice was managed by a management corporation ("FHDM"). A family trust was settled by Dr. G's mother (the "Trust"), of which the taxpayers, as family members, were minor beneficiaries who held all of the common shares and all of the class C preferred shares of FHDM. FHDM issued class D preferred shares with a low paid-up capital and a high redemption value to the Trust by way of stock dividend on its common shares. The Trust allocated to the taxpayers capital gains it realized during 2003, 2004, and 2005 on its non-arm's length sales of class D preferred shares to Dr. G (the "Gains"). The Minister recharacterized these Gains under the general anti-avoidance rule ("GAAR") as dividends in the Trust's hands. This resulted in the imposition on the taxpayers of a tax on "split income" under section 120.4 (i.e., the so-called "kiddie tax"). On the taxpayers' appeals to the Tax Court of Canada, they conceded the existence of a "tax benefit" and an "avoidance transaction", so that the only issue was whether there had been abusive tax avoidance for purposes of subsection 245(4).

The taxpayers' appeals were allowed. Tax planning, in itself, is not inherently abusive for GAAR purposes. Nor does surplus stripping inherently constitute abusive tax avoidance, or abusive tax avoidance exist only because a taxpayer may have abused some broad policy not itself grounded in the provisions of the *Income Tax Act*. Furthermore, a broad policy against income splitting, grounded in specific provisions other than section 120.4, has not been recognized. In addition, the wording of section 120.4 as it stood in 2003, 2004, and 2005 did not apply to the gains realized by the Trust. The 1999 Budget supplementary information did not suggest that Parliament intended the section to be applicable to all types of income splitting involving minors, but only to specifically targeted dividend income, partnership income, or trust income consisting of dividends. Admittedly, amendments to section 120.4 enacted in 2001 extended its coverage to capital gains realized on the non-arm's length disposition of shares of private corporations. Accordingly, had these amendments been in place during 2003, 2004, and 2005, the Gains would have been subject to the split income tax under section 120.4. It was reasonable to infer, therefore, that Parliament intended not to cover capital gains when section 120.4 was first enacted. All of the foregoing observations led to the conclusion that the transactions giving rise to the Gains in this case did not circumvent the application of section 120.4 in a manner that constituted abusive tax avoidance contrary to the provisions of subsection 245(4). The Minister's assessments were vacated accordingly.

— *Gwartz*, 2013 DTC 1122

Taxpayer was more like employee than independent contractor and, therefore, determined to be a personal services business

The corporate taxpayer was reassessed for 2007 to 2009 for amounts claimed as expenses and claims for the small business deduction under subsection 125(1). The Minister argued that the taxpayer was a personal services business and denied the expenses under paragraph 18(1)(*p*). Without the taxpayer, its owner and manager, A, would be an employee of the Canada Revenue Agency and the Canada Mortgage and Housing Corporation, the entities to which it provided service. The taxpayer argued that the intention of the parties to the commercial arrangement was that of an independent contractor and not employee. The Minister argued that based on the test in *Wiebe Door Services Ltd v. MNR* (87 DTC 5025), the taxpayer was an employee for all intents and purposes.

The taxpayer's appeal was dismissed. On a balance of probabilities, the taxpayer would be reasonably regarded as an employee of his clients and, consequently, the taxpayer was a personal services business. Accordingly, the small business deduction and related expenses were disallowed.

— *Gomez Consulting Ltd.*, 2013 DTC 1125

Plan did not qualify as employee profit sharing plan and CPP contributions required

The corporate taxpayer was appealing a Tax Court decision that upheld an assessment for CPP contributions with respect to amounts it claimed had been paid to an employee profit sharing plan ("EPSP"). The respondent held that there was no valid EPSP and as such the CPP contributions were payable. J was a chartered accountant who set up the taxpayer corporation to provide accounting services. The taxpayer entered into an EPSP trust indenture, and in 2009 made four payments totalling $120,100 that were allocated and paid out to J.

The taxpayer's appeal was dismissed. To be a valid EPSP, payments must be computed by reference to profits and be required to be made by the employer to the trustee of the plan. The employer must elect that payments are to be made out of profits (which was not done here) or the arrangements must satisfy the condition that payments are computed by reference to profits. The trust indenture provided that payments were to be computed by reference to a formula or be a minimum of $100 per participating beneficiary for each year. No formula was ever established and basing the payments on the number of participating beneficiaries does not meet the requirement that it be based on profits. The trust indenture also provided that the payments were to be no less than 1% of the profits earned, which could have created an obligation to make this minimum payment. However, based on the financial statements, that minimum amount would have been $1,578. The amounts totalling $120,100 that were paid by the taxpayer were arbitrary and were not made with any reference to profits earned. Accordingly, the payments were contributory salary and wages of J, subject to CPP contributions.

— *Gary Jackson Professional Corporation*, 2013 DTC 5108

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