Tax Notes

March 2021
Number 698

Wolters Kluwer

EXCHANGE OF SHARES BY A SHAREHOLDER IN THE COURSE OF A REORGANIZATION OF CAPITAL (S. 86)

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Section 86 of the *Income Tax Act* provides for a rollover where, under a reorganization of the capital structure of a corporation, a taxpayer disposes of all the shares of any particular class of the capital stock of the corporation (old shares), and as consideration therefor property is receivable from the corporation that includes other shares of the capital stock of the corporation (new shares). The section applies only where the old shares are capital property of the shareholder.

Unless subsection 86(2) applies, paragraph 86(1)(*c*) provides that the taxpayer is deemed to have disposed of the old shares for proceeds of disposition equal to the aggregate of the taxpayer's cost of the new shares and any non-share property. Accordingly, if the fair market value of the non-share property does not exceed the adjusted cost base of the old shares, the deemed proceeds of disposition of the old shares will be equal to the adjusted cost base of the old shares, and no capital gain will be realized.

Putting It Into Practice

In connection with the reorganization of the capital structure of a corporation, several points should be borne in mind:

- For section 86 to apply, a shareholder must actually dispose of their shares.
- Section 86 does not apply to the disposition of securities other than shares, such as bonds or other debt securities.
- The shares disposed of must constitute capital property of the shareholder. Where shares are other than capital property, such as where they are inventory, section 86 does not apply.
- The shareholder must dispose of *all* their shares of a particular class of the corporation's capital stock. If by inadvertence or otherwise all their shares of a particular class are not disposed of, the rollover provided by section 86 will not apply.
- Section 86 applies to non-residents as well as residents, provided all the requisite conditions of the section are met. It is not necessary that the corporation be a Canadian corporation as defined in subsection 89(1).

Unequal Exchanges

Subsection 86(2) was enacted to limit the rollover provisions of subsection 86(1) in situations where a taxpayer gifted a portion of the value of their shares to a related person. The effect of subsection 86(2) may be to force a recognition of a capital gain on the old shares and to alter the adjusted cost base of the new shares received on the reorganization.

Subsection 86(2) will apply if all of the following three conditions are met:

(1) Subsection 86(1) would have otherwise applied to the reorganization;

(2) The fair market value of the old shares before the reorganization is greater than the fair market value of the property other than shares received on the reorganization plus the fair market value of the new shares received on the reorganization; and

(3) The difference in (2) above, which is referred to as the "gift portion", can be reasonably considered to be a benefit that the taxpayer desired to have conferred upon a person related to them. See subsection 251(2) as to when persons are related.

Subsection 86(2) will apply to determine the amount of the proceeds of disposition of the old shares and to determine the adjusted cost base of the new shares received on the reorganization. The cost of property other than shares receivable for the old shares will still be determined under subsection 86(1) on the basis of its fair market value. The deemed proceeds of disposition of the old shares will be equal to the lesser of:

(a) the fair market value of the property (other than new shares) receivable for the old shares plus the gift portion; and

(b) the fair market value of the old shares immediately before the reorganization.

If the deemed proceeds of disposition would otherwise result in a capital loss on the disposition of the old shares, the capital loss is deemed to be nil.

Paragraph 86(2)(*e*) deems the new shares receivable as a result of the reorganization to be acquired at a cost equal to the amount, if any, by which the adjusted cost base of the old shares exceeds the fair market value of property other than shares receivable for the old shares plus the gift portion. If more than one class of new shares is issued, this amount will be allocated among the classes on the basis of their fair market values.

In return for the old shares which the shareholder disposes of, they must receive property from the corporation that includes other shares of the corporation's capital stock. The new shares need not be of the same class as the old shares.

Income Tax Application Rule ("ITAR") 26(27) will normally apply to prevent the realization of pre-1972 capital surplus when shares held since prior to 1972 are the subject of a reorganization. However, ITAR 26(27) does not apply if subsection 86(2) applies to the reorganization.

If the value of any non-share consideration received on the exchange exceeds the shareholder's adjusted cost base of the old shares or the paid-up capital in respect of the old shares, the shareholder may realize a capital gain and/or a deemed dividend rather than a complete rollover. Where the fair market value of the non-share property exceeds the adjusted cost base of the old shares, the taxpayer will be deemed to have disposed of the old shares for proceeds equal to the fair market value of the non-share property, so that such excess will generate a capital gain (except to the extent of a deemed dividend — see below). In this case, the new shares will have a cost of nil.

If the fair market value of any non-share property received by the taxpayer exceeds the paid-up capital in respect of the old shares, the excess will normally be treated as a deemed dividend under subsection 84(3) (on the assumption that the corporation redeems, cancels, or acquires the old shares). The amount of the deemed dividend will in turn be excluded from the proceeds of disposition of the old shares (paragraph (*j*), "proceeds of disposition", section 54).

Interaction of Section 86 With Other Rollover Provisions

Under subsection 86(3), subsections 86(1) and 86(2) are not applicable in any case where subsection 85(1) (transfer of property to corporation by shareholder) or 85(2) (transfer of property to corporation from partnership) is applicable. Further, section 51 does not apply if section 86 applies (subsection 51(4)).

Computation of Paid-Up Capital on a Reorganization of Capital Under S. 86

Subsection 86(2.1) provides rules for the computation of paid-up capital on an exchange to which subsection 86(1) has applied. In general terms, the paid-up capital of the new shares issued on the exchange is limited to the paid-up capital of the old shares less any non-share consideration.

The mechanism provided in subsection 86(2.1) is similar to that provided in a rollover made under the provisions of section 85. The paid-up capital of a particular class of shares at the time of or after the exchange is reduced by an amount determined by the formula:

$$(A - B) \times C / A$$

where

A is the increase in the paid-up capital of all shares in the capital stock of the corporation under corporate law as a result of the exchange;

B is the excess, if any, of the paid-up capital of the old shares over the fair market value of any non-share consideration given by the corporation on the exchange; and

C is the increase in the paid-up capital in respect of the particular class of shares under corporate law as a result of the exchange.

The latter part of the formula (C / A) provides for the allocation of any paid-up capital reduction among multiple classes of shares, where the transferor receives more than one class of shares on the exchange.

Paragraph 86(2.1)(*b*) provides for an increase in the paid-up capital where the paid-up capital was previously reduced under paragraph 86(2.1)(*a*) and a dividend has subsequently been recognized as a result of the application of subsection 84(3), 84(4), or 84(4.1). The amount of the increase is equal to the amount by which the actual deemed dividend exceeds the deemed dividend that would have resulted had the paid-up capital not been reduced under paragraph 86(2.1)(*a*). The increase in paid-up capital is also specifically limited to the amount of any previous reduction under paragraph 86(2.1)(*a*).

COVID-19 UPDATE

Given the rapidly changing information related to COVID-19 we are providing continuously updated information at https://blog.intelliconnect.ca/.

Federal

Canada Proposes Extension to Recovery and EI Benefits (February 19, 2021)

The Minister of Employment, Workforce Development and Disability Inclusion announced the Government of Canada's intent to introduce regulatory and legislative amendments to increase the number of weeks of benefits available for the Canada Recovery Benefit ("CRB"), the Canada Recovery Sickness Benefit ("CRSB"), the Canada Recovery Caregiving Benefit ("CRCB"), and Employment Insurance ("EI") regular benefits. As some workers could begin to exhaust their benefits in late March, this increase would ensure continued support as Canada's economy and labour force recovers.

The proposed changes would:

- increase the number of weeks available under the CRB and the CRCB by 12 weeks, extending the maximum duration of the benefits through regulation from 26 weeks to up to 38 weeks;
- increase the number of weeks available under the CRSB through regulation from the current two weeks to four weeks; and
- increase the number of weeks of EI regular benefits available by up to 24 weeks to a maximum of 50 weeks through legislation, for claims that are made between September 27, 2020, and September 25, 2021.

To ensure employees in the federally regulated private sector can access the proposed additional weeks of CRCB and CRSB without the risk of losing their jobs, the maximum length of the leave related to COVID-19 under the *Canada Labour Code* would also be extended. Provincial and territorial governments will determine whether they need to amend their job-protected leaves in order to facilitate employees' access to the proposed additional weeks of CRSB and CRCB benefits.

Subject to the legislation receiving Royal Assent, in addition, self-employed workers who have opted in to the EI program to access special benefits would be able to use a 2020 earnings threshold of $5,000, compared to the previous threshold of $7,555. This change would be retroactive to claims established as of January 3, 2021, and would apply until September 25, 2021.

Increased Compensation for the Audiovisual Sector (February 10, 2021)

The Minister of Canadian Heritage announced that $50 million has been added to the initial funding for the Short-Term Compensation Fund for Canadian Audiovisual Productions ("STCF"). The fund was launched last fall to support audiovisual industry productions during the COVID-19 pandemic. The STCF funding has increased to $100 million, which allows more productions to make use of the program during the busiest time of the year for the industry. Telefilm, which administers the program, can now compensate a production company whose project had to be abandoned or interrupted due to a confirmed COVID-19 diagnosis on the set or an outbreak on the production team.

CERB Repayments Forgiven for Self-Employed Individuals (February 9, 2021)

The CRA announced that self-employed individuals who applied for the Canada Emergency Response Benefit ("CERB") and would have qualified based on their gross income will not be required to repay the benefit if they also met all other eligibility requirements. This applies whether the individual applied through the CRA or Service Canada.

Therefore, self-employed individuals whose net self-employment income was less than $5,000 and who applied for the CERB will not be required to repay the CERB, if their gross self-employment income was at least $5,000 and they met all other eligibility criteria.

Some self-employed individuals whose net self-employment income was less than $5,000 may have already voluntarily repaid the CERB. The CRA and Service Canada will return any repaid amounts to these individuals.

Interest Relief on Tax Debt From Pandemic Support (February 9, 2021)

The CRA will provide targeted interest relief to Canadians who received COVID-related income support benefits. Once individuals have filed their 2020 income tax and benefit return, they will not be required to pay interest on any outstanding income tax debt for the 2020 tax year until April 30, 2022.

To qualify for targeted interest relief, individuals must have had a total taxable income of $75,000 or less in 2020 and have received income support in 2020 through one or more of the following COVID-19 measures:

- the Canada Emergency Response Benefit ("CERB");
- the Canada Emergency Student Benefit ("CESB");
- the Canada Recovery Benefit ("CRB");
- the Canada Recovery Caregiving Benefit ("CRCB");
- the Canada Recovery Sickness Benefit ("CRSB");
- Employment Insurance ("EI") benefits; or
- similar provincial emergency benefits.

The CRA will automatically apply the interest relief measure for individuals who meet these criteria.

Also, any CRA-administered credits and benefits normally paid monthly or quarterly, such as the Canada Child Benefit and the GST/HST tax credit will not be applied to reduce individuals' tax debt owing for the 2020 tax year. Canadians are strongly encouraged to file their tax returns by the filing deadline to ensure that their benefit payments continue without interruption.

Regional Relief and Recovery Fund Expanded (February 5, 2021)

The federal government announced an expansion of the Regional Relief and Recovery Fund ("RRRF") to align with the increased funding available under the Canada Emergency Business Account ("CEBA"). This follows the government's intention in the Fall Economic Statement to increase RRRF funding by $500 million nationally, including over $250 million for Western Canada. This will make a total of more than $800 million available to meet strong demand to help Western Canadian small businesses and organizations with liquidity needs that cannot be met by other federal support programs.

New applicants to the RRRF can now request up to $60,000 in interest-free, repayable support, up from $40,000 previously. Existing RRRF recipients can now apply for additional funding of up to $20,000 if they continue to suffer eligible COVID-19-related losses. Additional fully repayable liquidity support over $60,000 may also be available for eligible applicants.

With many travel and public health restrictions in place, Canada's tourism sector has been particularly hard-hit by the pandemic. Therefore, a minimum of 25% of RRRF funding across Canada is earmarked for local tourism-related businesses and organizations to help them prepare for the industry's recovery.

Waiver of One-week Waiting Period for EI (January 29, 2021)

In response to the increase in people needing support, the Minister of Employment, Workforce Development and Disability Inclusion announced Employment Insurance ("EI") regulations will be amended to temporarily waive the waiting period for EI claimants who establish a new claim between January 31, 2021, and September 25, 2021. This includes claimants of regular, fishing, and special benefits. This temporary measure will not change the total weeks of EI benefits for which claimants are entitled, nor the service standard for payment. Claims will be automatically processed with this new waiver, meaning workers are not required to take additional steps to receive the support they need.

Highly Affected Sectors Credit Availability Program (January 27, 2021)

The government will work with financial institutions to create the Highly Affected Sectors Credit Availability Program ("HASCAP") — a new program for the hardest hit businesses across Canada, including those in sectors, like tourism and hospitality, hotels, and arts and entertainment, that rely on in-person service. Through HASCAP, the Business Development Bank of Canada ("BDC") will work with participating Canadian financial institutions to offer government-guaranteed, low-interest loans of up to $1 million. Hard-hit businesses, like a chain of hotels or restaurants with multiple locations under one related entity, could be eligible for up to $6.25 million.

To be eligible for HASCAP, businesses need to show a year-over-year revenue decline of at least 50% in three months, within the eight months prior to their application. They must also be able to show their financial institutions that they previously applied for either the Canada Emergency Wage Subsidy or the Canada Emergency Rent Subsidy. Eligible businesses can start applying February 1 at principal financial institutions and more widely by February 15. Interested businesses should contact their primary lender to get more information and to apply. More information is available at www.bdc.ca/hascap. The Office of the Superintendent of Financial Institutions has issued direction to federally regulated deposit-taking institutions on how to treat new loans to businesses through the HASCAP — see www.osfi-bsif.gc.ca/Eng/osfi-bsif/med/Pages/hascap-nr.aspx.

Provincial

Alberta

Additional COVID-19 Support for Alberta Small Business (February 17, 2021)

Starting in mid-April, the Enhanced COVID-19 Business Benefit will provide payments of up to $10,000 to eligible small and medium businesses most affected by the pandemic and ongoing public health restrictions. Businesses can use these funds as they see fit to help offset the costs of re-opening, and implementing public health measures including:

- physical barriers;
- purchasing personal protective equipment and disinfecting supplies;
- paying rent and employee wages;
- replacing inventory; and
- expanding online business or e-commerce.

The benefit will provide funding to businesses that have experienced a revenue reduction of at least 60%. Payments will be calculated based on 15% of the eligible business's monthly revenue, up to a maximum of $10,000. To be eligible for the Enhanced COVID-19 Business Benefit, applicants must:

- be a business, cooperative, or non-profit organization with fewer than 500 employees;
- demonstrate a revenue reduction of at least 60%; and
- report the levels of provincial and federal support received, to ensure no more than 80% of revenue was covered by these supports.

The government of Alberta has committed $120 million in funding for the Enhanced COVID-19 Business Benefit. Applications will open in mid-April 2021.

Critical Worker Benefit (February 10, 2021)

The Critical Worker Benefit is a joint federal-provincial program that will see $465 million go to approximately 380,000 Alberta public and private sector workers as $1,200 cash payments. The benefit will be available to workers in the health care, social services, education, and private sectors who deliver critical services to Albertans or support food and medical supply chains. To be eligible for the benefit, employees must have worked a minimum of 300 hours during the period of October 12, 2020, to January 31, 2021.

The following are the provincial government's estimates of how many workers will receive the benefit:

- 161,000 health care sector workers;
- 45,000 social services sector workers; and
- 36,000 education sector workers.

Also, eligible private sector workers making $25 per hour or less will qualify for the benefit. These workers include:

- critical retail workers in grocery stores, pharmacies, and gas stations;
- private health provider workers, such as dental assistants, massage therapists, and medical administration assistants;
- food manufacturing and processing workers;
- truck transportation workers, such as truck drivers and delivery and courier services drivers; and
- warehouse and storage workers, such as shippers and receivers.

Eligible public sector employees do not need to apply to receive the benefit. Employers will automatically receive the payment through the Government of Alberta to distribute to their eligible employees. Employers will be responsible for distributing the $1,200 Critical Worker Benefit to their eligible employees.

Private sector employers can apply on behalf of eligible employees at alberta.ca/criticalworkerbenefit as of February 17. Employers have until March 19 to apply.

British Columbia

New Pilot Program Supports Small and New Farmers (February 12, 2021)

Successful applicants of the new Small Farm Business Acceleration Pilot Program are receiving funding for farm infrastructure and equipment to help them grow their farm businesses and support local food supply and rural economies. This one-year pilot program is supporting 64 small and new farmers with diverse farm businesses throughout the province. This funding will strengthen a variety of farm growth projects to help enhance crop and livestock productivity, increase sales, and diversify market channels. Buying infrastructure and equipment, like greenhouses, will support rural economic development and contribute to local food production. A small farm is defined as one with a total annual gross revenue of less than $60,000 in the last two years. The program will cover 50% to 75% of total approved project costs to a maximum of $17,500 for individual farm businesses.

New Launch Online Grant (February 3, 2021)

The new Launch Online Grant program is designed to help over 1,500 eligible small and medium-sized BC businesses adapt to changes in consumer behaviour and pivot to market their products online.

The BC government is investing $12 million to help businesses launch or upgrade an online store that will provide the platform they need to increase their sales revenues, become more competitive, and grow. Up to 25% of the program funds will be reserved for regional and Indigenous businesses.

These grants will provide business owners, including those in hard-hit sectors such as retail, tourism, and restaurants, with up to $7,500 to build or improve their online store and promote BuyBC at a local, national, and international level.

Grant recipients can use the funding for a variety of online-related expenses, including pictures, creating an online inventory system, advertising costs, subscription costs of an e-commerce platform, and training staff to manage the website.

As part of the program, successful applicants must use one or more local BC service providers to complete their online store. Through this model, the grant funding can be reinvested in BC-based marketing and technology companies to generate revenues for local companies and help secure and grow jobs.

The program is administered by Alacrity Canada. Small and medium-sized businesses are encouraged to apply online at: www.launchonline.ca.

The program is based on a first come, first-served basis. The program will run until March 31, 2021, or until all funds are distributed.

Eligibility criteria for businesses include having:

- a goods and services tax number and paying taxes in BC;
- generated sales of more than $30,000 in either 2019 or 2020;
- one to 149 employees (applications can be submitted by sole proprietors); and
- repeatable products, or in the case of artists and jewellers, individual items that have slight differences (e.g., paintings and rings).

As part of the application, businesses must develop a grant proposal that indicates how they plan to use the funds.

B.C. Supply Chain Resiliency and Value-Added Manufacturing Grant (January 21, 2021)

The B.C. Supply Chain Resiliency and Value-Added Manufacturing Grant project commits up to $14.25 million in provincial funding to generate new economic opportunities. The project consists of three parts:

- Building Strong Supply Chain Grants — The province is investing up to $4 million to support eligible industry and trade associations and groups in collaboration with grants of up to $400,000 to support industry in strengthening supply chain resilience.
- Accelerating Manufacturing Scale-Up Grants — The province is investing up to $10 million to support eligible small and medium-sized manufacturing businesses with funding of up to $250,000 to prototype, pilot, or demonstrate new technologies, commercialize new technologies and/or products, improve market access, and identify and implement operational improvements.
- BC Supply and Value Chain Analysis — The province is investing $250,000 to analyze opportunities to strengthen strategic BC supply chains as part of a provincial recovery that aims to increase supply chain competitiveness and resilience, and identify related advanced-manufacturing opportunities.

Expressions of Interest for the Building Strong Supply Chain Grants will be accepted until February 18, 2021. For details, visit www2.gov.bc.ca/gov/content/economic-recovery/supply-chain-resiliency-grant. BC is currently seeking a proponent through a request for proposal to support delivery of the Accelerating Manufacturing Scale-Up Grants; for application details, visit www2.gov.bc.ca/gov/content/economic-recovery/supply-chain-resiliency-grant.

Small and Medium-Sized Business Recovery Grant Now Accessible to More Businesses (January 21, 2021)

The BC government has enhanced the Small and Medium-Sized Business Recovery Grant program to make it easier for businesses to qualify and has increased support for those in the hard-hit tourism sector. Adjustments made to the program include a streamlined application process and simplified criteria. The criteria have been expanded from a minimum revenue drop of 50% to a drop of 30%. Additionally, the previous three-year operation requirement has been reduced to 18 months. This means businesses only need to have been in operation nine months before the pandemic to apply for the grant. Businesses impacted by the pandemic will be eligible to receive a grant of up to $30,000. The grant for the tourism sector has been increased, meaning those hardest-hit businesses in the tourism sector will be eligible for a grant of up to $45,000. The revised application process and eligibility criteria are now in place.

Ontario

Ontario Expands Eligibility for Main Street Relief Grant (February 16, 2021)

The Ontario government is expanding the number of small businesses that can apply for the Main Street Relief Grant to help offset the costs of purchasing personal protective equipment ("PPE") to cautiously and gradually reopen in parts of the province. Small businesses with two to 19 employees in all eligible sectors — expanded from two to nine employees — including those in the arts, entertainment, and recreation sectors, can now apply for up to $1,000 in financial support. This one-time grant reimburses main street businesses for up to $1,000 in PPE costs incurred since March 17, 2020. Eligible businesses for the Main Street Relief Grant now include those with two to 19 employees in the following sectors:

- retail trade;
- accommodation and food services;
- repair and maintenance;
- personal and laundry services;
- gyms and yoga studios; and
- arts, entertainment, and recreation.

Extended Electricity Relief (February 10, 2021)

The Ontario government is once again extending electricity rate relief for families, small businesses, and farms to support those spending more time at home while the province maintains the Stay-at-Home Order in the majority of public health regions. The government will continue to hold electricity prices to the off-peak rate of 8.5 cents per kilowatt-hour until February 22, 2021. This lower rate is available 24 hours per day, seven days a week for time-of-use and tiered customers.

The off-peak rate has been in effect since January 1, 2021, providing families, farms, and small businesses with immediate electricity rate relief. During this period, the off-peak price will continue to be automatically applied to electricity bills of all residential, small business, and farm customers who pay regulated rates set by the Ontario Energy Board and get a bill from a utility.

Support for Agricultural and Horticultural Societies (January 26, 2021)

The Ontario government is investing $5 million to help offset revenue losses for eligible agricultural and horticultural societies impacted by the necessary cancellation of fall fairs and exhibits during the COVID-19 pandemic restrictions. The funding is flowing through the Agricultural and Horticultural Support and Recovery Funding Initiative (see www.omafra.gov.on.ca/english/rural/returns/agandhortguide.htm for details). Societies have been unable to hold revenue-generating events over the past 10 months due to health and safety concerns around COVID-19. This one-time initiative features two funding streams:

- $1.8 million Base Support Funding will provide eligible agricultural societies with $7,000 and eligible horticultural societies with $1,140 to support their continued delivery of agricultural and horticultural education across Ontario; and

- $3.2 million Hardship Funding for eligible agricultural societies will provide additional support, which will be based on their reported gate receipts from 2019. This will help offset operating losses, liabilities, and fixed overhead costs.

Funding is expected to be completed before March 31, 2021.

Québec

Support for Tourism Businesses (February 18, 2021)

On February 18, 2021, the Minister of Tourism announced an increase in the forgivable portion of loans granted under the tourism component of the Temporary Concerted Action Program for Enterprises ("PACTE"), as well as support to cover the energy costs of companies admitted to this program. In order to better meet the needs of tourism businesses, the ceiling for the forgivable portion of loans will be increased from $100,000 to $250,000.

In addition, the PACTE tourism component will now provide forgiveness on energy expenditures. As a result, tourism businesses that have an active file in the program will have access to 100% equivalent forgiveness of their monthly energy expenses incurred between January 1, 2021, and June 30, 2021, up to $35,000/month, for a maximum of $210,000 per establishment. This delisting may be requested as of July 2021. Lastly, the PACTE tourism component will now be accessible to lodges with four or more bedrooms, to companies with four or more tourist residences, as well as to hotel establishments with 300 or more bedrooms.

New Relieving Measures To Help Individuals (February 12, 2021)

Individuals who have received COVID-19 assistance benefits will be exempt from paying interest on their 2020 tax balance for a one-year period. This measure is intended to provide relief to those who have been impacted by the pandemic. Specifically, individuals who received the Canada Emergency Response Benefit, the Canada Emergency Student Benefit, the Canada Recovery Benefit, the Canada Recovery Caregiving Benefit, the Canada Recovery Sickness Benefit, employment insurance benefits (including maternity and paternity benefits), or the Incentive Program to Retain Essential Workers and who will have a tax balance owing on their 2020 income tax return will be entitled to an interest holiday until April 30, 2022. To be eligible for this measure, individuals must have earned a total taxable income of $75,000 or less in 2020.

Online Pre-filled TP-64.3 Forms (January 26, 2021)

A new online service is available (in French only, at www.revenuquebec.ca/fr/acces-au-service-demander-des-formulaires-conditions-generales-demploi-tp-64-3-preremplis/) to help employers complete form TP-64.3-V, *General Employment Conditions*, for their employees who are working from home. The service lets employers save time by completing multiple copies of the form at once. If only some employees are working from home, employers can use the 2020-10 version of form TP-64.3-V instead of the online service. A minimum of information is required. Until further notice, employers can sign this version electronically and send it securely to their employees.

Saskatchewan

Small Business Support Extended (January 29, 2021)

The government announced a further extension to the Saskatchewan Small Business Emergency Payment ("SSBEP") program. The program was originally launched in April 2020, then renewed in December 2020. With this extension, businesses will be eligible for an additional payment for January 2021.

Business restrictions in public health orders have been expanded since the SSBEP program was renewed in December and businesses are encouraged to re-evaluate their eligibility for both the December and January payments.

The SSBEP program has provided $5.9 million in assistance to 1,521 applicants for the December period. With the public health order extended, more businesses in the province have been impacted. This phase of the program will accept applications for the December and/or January payment until March 2, 2021.

Applicants will be eligible for up to $5,000 per month in funding, and those who qualified for the December intake of the SSBEP will not have to re-apply for January. However, businesses will be contacted to attest that they remain eligible for the January payment.

For more information on the SSBEP program, businesses can visit www.saskatchewan.ca/small-business-emergency-payment, call 1-800-667-6102, or email ssbep@gov.sk.ca.

FOCUS ON CURRENT CASES

This is a regular monthly feature examining recent cases of special interest, coordinated by *Tony Schweitzer* of Dentons Canada LLP. The contributors to this feature are from Dentons Canada LLP, Montreal, Toronto, Calgary, and Vancouver.

Eyeball Networks Inc. v. The Queen, 2021 DTC 5011 (Federal Court of Appeal)

On January 29, 2021, the Federal Court of Appeal ("FCA") reversed the decision rendered by the Tax Court of Canada ("TCC") in *Eyeball Networks Inc. v. The Queen*.[1] The FCA decided that a set-off and cancellation of promissory notes effected as part of a related-party butterfly transaction under paragraph 55(3)(*a*) of the Act[2] did not trigger the application of subsection 160(1). In addition to restoring the world of butterflies to the way it was, the decision clarifies how a transfer can occur for the purposes of subsection 160(1) and when the value of the consideration received is to be ascertained.

Background

In 2002, Eyeball Networks Inc. ("Newco") acquired certain online video-conferencing business assets from a related corporation ("Oldco") as part of a series of transactions effecting a related-party spin-out under paragraph 55(3)(*a*). At all relevant times, the same individual (Mr. Piche) was the sole shareholder, director, and officer of both Oldco and Newco. Simplified, the spin-out was effected on a single day through the following steps:

(1) Mr. Piche froze his interest in Oldco by exchanging his existing shares for new growth shares and fixed-value, redeemable, preferred shares having a redemption value equal to $30 million (the "Oldco Pref Shares").

(2) Mr. Piche then transferred the Oldco Pref Shares to Newco in exchange for Newco issuing shares to Mr. Piche that purported to have an identical value.

(3) Oldco then transferred its business assets to Newco in exchange for Newco assuming certain liabilities of Oldco and issuing fixed-value, redeemable, preferred shares (the "Newco Pref Shares") to Oldco having a redemption value of $30 million, being the difference between the value of the transferred assets and the assumed liabilities. The transfer was effected under subsection 85(1) utilizing appropriate price adjustment mechanisms.

(4) Newco and Oldco then cross-redeemed their respective Newco Pref Shares and Oldco Pref Shares in consideration for the issuance of promissory notes (respectively, the "Newco Note" and "Oldco Note"), each note having a face value equal to the aggregate redemption values, being $30 million.

(5) Newco and Oldco then entered into a "Mutual Debt Cancellation Agreement" pursuant to which the Newco Note and Oldco Note were set-off against each other and surrendered for cancellation.

Over the course of 2003 and 2004, the CRA issued notices of reassessment to Oldco assessing tax, interest, and penalties in the aggregate amount of $126,000 in respect of its 2000 – 2002 taxation years. Oldco, having no valuable assets, failed to pay the reassessed amounts. In 2014, the CRA assessed Newco under subsection 160(1) as being liable to pay the amounts reassessed against Oldco, on the basis that Oldco had transferred its valuable assets to Newco as part of a series of transactions the net result of which was that Oldco was left with assets having only a nominal value and its subsisting tax debts.

Uncontested evidence established that (a) following the completion of the above transactions, Newco continued to operate the transferred business with limited success and Oldco was left with assets having nominal value, (b) the spin-out was effected for business purposes and not tax-planning, (c) Mr. Piche was unaware of the subsisting tax liability of Oldco at the time of the spin-out in 2002, and (d) Newco's assumption of Oldco's liabilities did not include any tax liabilities.

TCC Decision

Subsection 160(1) provides that, where a person transfers property to a non-arm's length person "directly or indirectly, by means of a trust or by any other means whatever", the transferee is jointly and severally liable with the transferor to pay any amount that the transferor was liable to pay under the Act for the taxation year in which the transfer

[1] 2019 DTC 1112.

[2] *Income Tax Act*, RSC 1985, c. 1 (5th Supp.), as amended (the "Act"). All statutory references herein are to the Act.

occurred, to the extent that the transferred property's fair market value ("FMV") "at the time it was transferred" exceeded the FMV of the consideration received by the transferor "at that time".

It was not disputed that the first three criteria established by *The Queen v. Livingston*[3] for the application of subsection 160(1) had been met: (1) Oldco was liable for tax at the time of the transfer; (2) there was a transfer of property from Oldco to Newco; and (3) Oldco and Newco were not dealing at arm's length. The issue was whether the fourth criteria had been met: Did the FMV of the property transferred to Newco exceed the FMV of the consideration received from Newco for the transferred property? This criterion requires the Minister to ascertain the FMVs of the transferred property and consideration received, and determine the moment in time at which those FMVs are relevant for the purposes of subsection 160(1).

The TCC considered the following issues in reaching its conclusion on whether the fourth criteria was met:

(1) Was the Minister entitled to look to the overall result of the series of transactions comprising the spin-out in determining whether Oldco received consideration with an FMV less than the FMV of the property it transferred to Newco?

(2) If not, did any particular step of the spin-out result in a transfer of property by Oldco to Newco for consideration having an FMV less than that of the transferred property at the moment in time it was transferred?

In respect of the first issue, the TCC considered whether the phrase in subparagraph 160(1)(*e*)(i), "at the time it was transferred", afforded the Minister the ability to look to the net result of a series of transactions in applying section 160. The Court concluded that on a textual analysis, the phrase was properly interpreted as referring to the moment in time that a particular transfer was effected.

On a contextual analysis, the TCC concluded that the introductory phrase in subsection 160(1), "by any other means whatever", did not warrant an expansive view of the relevant time period, as section 160 made no reference to any series of transactions, nor did it refer to any purpose of the transfer that might be ascertained only by looking to the net result of a series of transactions. While the phrase "by any other means whatever" provides an expansive view as to the manner in which a transfer could be considered to have been effected, the TCC found that it did not operate to expand the time frame in which the FMVs of the transferred property or consideration could be ascertained. The TCC noted that, while the FCA in *The Queen v. 594710 British Columbia Ltd.*[4] had relied on the phrase "by any means whatever" to expand the relevant time in which an FMV could be ascertained under subsection 160(1), it had done so in the context of a GAAR analysis, which was necessarily broader than a non-GAAR analysis.

On a purposive analysis, the TCC considered the conclusions reached in other decisions[5] and concluded that the purpose of section 160 is to prevent taxpayers from thwarting the Minister's efforts to collect tax debts, and matter-of-factly concluded that this purpose did not mandate an expansive view of the relevant time period. The TCC, therefore, concluded that subsection 160(1) required the Minister to examine the "separate nature of each and any event that created an identifiable transfer" and precluded the Minister from assessing "the net result of a series of transactions in applying section 160".

In respect of the second issue, the TCC found that the spin-out consisted of three separate, identifiable transfers from Oldco to Newco: (1) the transfer of the business assets from Oldco to Newco; (2) the transfer of the Newco Pref Shares from Oldco to Newco on the cross redemption; and (3) the set-off and cancellation of the Newco Note. Regarding the first transfer, the TCC concluded that the price adjustment clause operated to ensure that the value of the Newco Pref Shares would always equal the FMV of the transferred assets. Regarding the second transfer, the TCC concluded that the FMV of the Newco Note was equal to the FMV of the redeemed Newco Pref Shares.

The third identified transfer had not been pleaded by the Crown, but was found by the TCC nonetheless to be determinative of the taxpayer's case. The TCC concluded that the set-off of the Notes was effected by Oldco surrendering the Newco Note to Newco for cancellation in consideration for Newco surrendering the Oldco Note to Oldco for cancellation and that the FMV of the Oldco Note at the time of this transfer was nominal as a result of Oldco then having only nominal assets, whereas the FMV of the surrendered Newco Note was higher by a significant amount, as a result of Newco having acquired all of Oldco's valuable assets. Accordingly, the TCC confirmed the

[3] 2008 DTC 6233 (FCA).

[4] 2018 DTC 5111 ("*594710 BC*").

[5] *9101-2310 Quebec Inc. v. The Queen*, 2013 DTC 5172 (FCA); *Heavyside v. The Queen*, 97 DTC 5026 (FCA); *Livingston v. The Queen*, 2008 DTC 6233 (FCA); and *McLarty Family Trust v. The Queen*, 2012 DTC 1123 (TCC).

Minister's assessment of Newco under subsection 160(1) on the basis that Oldco had transferred the Newco Note to Newco for surrender and cancellation in consideration for the transfer and surrender of a near-valueless Oldco Note.

The taxpayer appealed to the FCA.

FCA Decision

The issues before the FCA were the same as those before the TCC.

Newco appealed on the basis that (1) the TCC held incorrectly that the FMV of the Oldco Note was less than the FMV of the Newco Note at the time of the mutual set-off and cancellation; and (2) even if the FMVs of the Notes were not identical at the time of set-off, the Oldco Note and Newco Note were nonetheless *bona fide* debts paid by mutual set-off and the payment of a debt cannot trigger subsection 160(1).[6] In reply, the Crown submitted that the TCC had erred in its consideration of the first issue, arguing that when a transfer is effected through a number of preordained transactions that together result in the transferor's consideration being depleted, the "time of the transfer" under subsection 160(1) requires one to look at the net result of the whole of the transactions, as the adequacy of the consideration can be determined only by looking at the overall result. The Crown argued that the TCC's contextual analysis of the phrase "by any means whatever" was too narrow, and that a purposive analysis dictated that it must be interpreted broadly to prevent taxpayers from thwarting the Minister's ability to collect tax debts.

The FCA held that the TCC had not erred in its consideration of the first issue. The correct time at which to ascertain FMVs for purposes of subsection 160(1) is the moment the transfer is effected. The TCC was correct in concluding that the phrase "directly or indirectly, by means of a trust or any other means whatever" broadens the notion of transfer to capture all forms of transfers, including those effected through the combined effect of multiple transactions. However, the FCA confirmed that "it has no bearing on the manner in which the adequacy of the consideration given for the property transferred is to be determined." That must be determined at the time that the transfer is effected, which under both common and civil law occurs at an instant in time. The FCA noted that to attempt to broaden the statutory language beyond this moment in time would introduce considerable uncertainty, as the value of any asset can fluctuate considerably throughout any given span of time.

The FCA also clarified the TCC's suggestion that the FCA in *594710 BC* had employed a broadened time period in its subsection 160(1) analysis (which the TCC stated was applicable only in a GAAR analysis). The FCA noted that *594710 BC* dealt with circumstances where a transfer was effected by a combination of transactions: a stock dividend followed by a share redemption. While the introductory language "by any other means whatever" enabled the Court to identify the transfer that occurred as a result of the combination of these transactions, it was still required to assess the FMV of the consideration at the moment in time when the transfer was effected, being the moment the redemption price was paid and the property changed hands.

The FCA held further that the TCC had not erred in its finding that Oldco had received adequate consideration on both the transfer of the business assets to Newco and on the surrender of its Newco Pref Shares in consideration for the Newco Note. The Crown conceded the adequacy of the consideration on these transfers.

Last, the FCA agreed with both of Newco's grounds for appeal. It found that the TCC had erred in holding that the FMV of the Newco Note exceeded that of the Oldco Note at the time of their set-off and cancellation, as the cross-held Notes were backed by the same assets such that whatever FMV one Note had could not be less than that of the other. The FCA further agreed with the taxpayer, finding that, irrespective of the Notes' FMVs, *Mullins* and *D'Argys* established that payment of a *bona fide* debt cannot trigger the application of subsection 160(1).

The FCA then considered a further argument advanced by the Crown: If the Oldco Note had value, then Oldco's redemption of the Oldco Pref Shares in consideration for the issuance of the Oldco Note resulted in Oldco transferring a valuable Oldco Note to Newco in consideration for receiving its Oldco Pref Shares, which had no value to Oldco. The FCA agreed that the Oldco Shares had no value to Oldco, but concluded that subsection 160(1) looked to the FMV of the consideration "given", not received, reflecting settled Canadian law that:

> . . . when dealing with property whose value varies depending on who holds it, it is the value of the property as it stands in the hands of the transferor at the time of the transfer that governs . . . Conversely, when dealing with consideration capable of similar variations, it is the value of the consideration as it stands in the hands of the transferee at the time of the transfer that governs.

[6] Relying on *Mullins v. Canada (MNR)*, 91 DTC 173 (TCC) ("*Mullins*") and *D'Argys v. Canada (MNR)*, 92 DTC 1710 (TCC) ("*D'Argys*").

Conclusion

While all appears to once again be well with the beloved butterfly, the FCA qualified its closing words adding that: "subject to circumstances allowing for the GAAR to be invoked, subsection 160(1) as presently framed does not capture the depletion of corporate assets that results from a share redemption."

— *Ron Dueck, Partner, Dentons Canada LLP, Vancouver*

CIBC v. The Queen, 2021 GTC 1002 (Federal Court of Appeal)

Introduction

On January 22, 2021, the Federal Court of Appeal ("FCA") overturned the decision rendered by the Tax Court of Canada ("TCC") in *Canadian Imperial Bank of Commerce v. The Queen*[1] (Decision under Appeal) and concluded that the service provided by Visa to the Canadian Imperial Bank of Commerce ("CIBC") was an exempt supply of a "financial service" as defined under the *Excise Tax Act*[2] ("ETA"). As a result, CIBC was entitled to the rebate applications it filed for GST/HST paid in error on fees charged by Visa from 2003 to 2013 (the "Fees").

The FCA distinguished the case at bar with the decision rendered in *Great-West Life Insurance Company v. The Queen*[3] and confirmed that Visa provided a service whose predominant element went beyond mere cost savings and logistics. As virtually every business in Canada deals with payment processors, this key decision sheds more light on what distinguishes a financial service from a service merely administrative in nature.

Background

CIBC issued Visa-branded credit cards to its customers and paid the Fees to Visa to participate in the Visa payment system, a set of instruments, procedures, rules, and technology ("Visa System"). The Visa System allows Visa credit cardholders to immediately access credit granted by their financial institution, CIBC in this case, wherever merchants ("Participating Merchants") accept Visa as a payment for any given purchase.

The Visa System's rules, which are contractually binding by-laws, operating regulations, guides, and directives established by Visa, are circulated among the Visa System participants and govern their participation in the Visa System. Visa ensures compliance with the Visa System's rules of all participants and may modify such rules without the participant's approval. The evidence presented before the TCC, however, established that such rules are in fact relatively static. Visa also proceeds with risk assessments regarding the participants to the Visa System, including the investigation, assessment, and monitoring of the credit-worthiness of Participating Merchants ("Merchant Risk").

Issue

The central question in this case was whether the service CIBC acquired from Visa ("Visa Service") in consideration of the Fees came within the definition of a "financial service" provided in the ETA and was therefore not subject to GST/HST.[4]

The expression "financial service" is defined under subsection 123(1) of the ETA (the "Definition"). A service is a financial service if it is included under at least one of the paragraphs (*a*) to (*m*), while not excluded by one of the paragraphs (*n*) to (*t*) of the Definition. Pursuant to paragraph (*t*) of the Definition and section 4 of the *Financial Services and Financial Institutions (GST/HST) Regulations*,[5] any administrative service is excluded from being a "financial service", except, among other things, if the administrative service is supplied by a "person at risk".

TCC Decision

In the Decision under Appeal, the TCC concluded that the Visa Service did not constitute a financial service as defined under the ETA.

[1] 2018 GTC 19.

[2] R.S.C. 1985, c. E-15.

[3] *Great-West Life Insurance Company v. The Queen*, 2015 GTC 71 (affirmed by the FCA in *Great-West Life Insurance Company v. Canada*, 2016 GTC 1039) ("*Great-West*").

[4] Subsection 123(1) and Schedule V, Part VII of the ETA.

[5] SOR/91-26 [P.C. 1990-2735, December 18, 1990].

Both parties agreed that the supply of the Visa Service constituted a single compound supply. After accepting that Visa provided one single compound supply, whose predominant element only should be taken into account when determining whether it constituted a supply of a financial service under the ETA, the TCC concluded that while the Visa Service fell within paragraphs (*a*), (*i*), and (*l*) of the Definition, it was however excluded under paragraph (*t*) of the Definition and the Regulations.

Despite the fact that it described the Visa Service as "an essential part of the ability for CIBC to offer credit card based services to their clients",[6] giving "CIBC customers the ability to purchase goods and services anywhere in the world without CIBC having to individually contact each merchant to set up payment arrangements with them"[7] and that "If CIBC was forced to create such a payment network on its own, even if technically feasible, this network would invariably be much less widely accepted than the ones offered by Visa",[8] the TCC concluded that the Visa Service was essentially "cost saving and logistical simplification",[9] "with minimal decision making involved",[10] and therefore, referring to the *Great-West* decision, merely administrative in nature. Stating that Visa was not a "person at risk" as defined under the Regulations, the TCC then concluded that the Visa Service did not qualify as a financial service for GST/HST purposes.

FCA Analysis

Since the determination that the Visa Service is included in paragraphs (*a*), (*i*), and (*l*) of the Definition was not challenged in the appeal, the main issue raised before the FCA was to determine whether such service was subsequently excluded from the Definition by virtue of paragraph (*t*) of the Definition and the Regulations.

In a unanimous decision, the FCA agreed with the TCC interpretation of an "administrative service" but considered that the TCC judge made a palpable and overriding error in concluding that the Visa Service was an administrative service. More particularly, the FCA ruled that the evident contradiction between the TCC's findings that, on one hand, the Visa Service formed an essential part of the ability for CIBC to offer to its client a credit card based service and, on the other hand, the same supply was "quintessentially administrative in nature", warranted the Court's intervention.

Distinguishing the present case from the *Great-West* case, the FCA confirmed that the evidence presented before the TCC showed that the benefit provided to CIBC by the Visa Service, including the provision by Visa to CIBC of a reputable worldwide network as well as Visa's monitoring of Merchant Risk on behalf of CIBC, went beyond a mere administrative service. The FCA also concluded that the fact that the Visa System operated with minimal decision making involved, as was the case in *Great-West*, was not sufficient to support the conclusion that the Visa Service was only administrative in nature since Visa set and maintained decision-making authority in the application of the Visa System rules.

It should be noted that considering the FCA concluded that the Visa Service was not an administrative service, it was no longer required to determine if Visa was a "person at risk" as defined under the Regulations.

Conclusion

Since, there was no dispute before the FCA as to whether the Visa Service fell within paragraph (*a*), (*i*), and (*l*) of the Definition and considering that the application of the exclusion set forth in paragraph (*t*) of the same Definition was not established, the Visa Service to CIBC constituted a financial service under the ETA. As such, no GST/HST was payable on the Visa Service, and CIBC was allowed to claim a refund for the GST/HST paid in error in respect of such service.

— *Manon Jubinville and Camille Janvier-Langis, Partners, Dentons Canada LLP, Montreal*

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[6] Paragraph 92 of the Decision under Appeal.

[7] Paragraph 95 of the Decision under Appeal.

[8] Paragraph 95 of the Decision under Appeal.

[9] Paragraph 116 of the Decision under Appeal.

[10] Paragraph 117 of the Decision under Appeal.

Dow Chemical Canada ULC v. The Queen, 2021 DTC 1001 (Tax Court of Canada)

Introduction

The Tax Court of Canada is a statutory court under section 101 of the *Constitution Act, 1867*.[1] That means that its powers are limited to those set out in its enabling statute, the *Tax Court of Canada Act*.[2] Section 12 of that Act gives the Court original jurisdiction to hear and decide tax appeals, but does not make it a court of equity nor does it confer on the Court the right to judicially review an action or decision of the Minister of National Revenue or of the Canada Revenue Agency. That is why, for example, decisions of the Minister not to waive interest or penalties must be judicially reviewed in the Federal Court rather than the Tax Court. Such a decision is not incorporated into an assessment and therefore there is nothing to appeal to the Tax Court of Canada.

On the other hand, section 18.5 of the *Federal Courts Act*[3] provides that if a matter may be appealed to, *inter alia*, the Tax Court of Canada, then it cannot be the subject of judicial review in the Federal Court.

Accordingly, whenever the Minister makes a tax decision, one must go through an analysis to decide whether it should be challenged by way of judicial review in the Federal Court or an appeal to the Tax Court.

In *Dow*, the Minister exercised discretion under subsection 247(10) of the Act[4] not to allow a downward adjustment. The issue was, is this reviewable in the Federal Court or appealable to the Tax Court?

Somewhat surprisingly, the Court held that the Minister's decision was within the Tax Court's exclusive appellate jurisdiction.

Equally surprisingly, having decided that the taxpayer could appeal the assessment, including the failure to allow a downward adjustment, to the Tax Court and having assumed the responsibility under section 171 of allowing, dismissing, or varying the appeal, the Court stated that, while the Minister's discretion under subsection 247(10) is a matter of the "correctness" of the assessment, this does not mean that there is necessarily a "correct" answer.

Downward Transfer Pricing Adjustment

Where a taxpayer transacts with a non-resident person, with whom the taxpayer does not deal at arm's length, under terms or conditions that do not reflect arm's length terms or conditions, the Minister may assess the taxpayer under subsection 247(2) by increasing or decreasing the amounts charged in the transaction to reflect arm's length terms and conditions (a "Transfer Pricing Adjustment"). Transfer Pricing Adjustments, whether upward or downward, are adjustments in the computation of a taxpayer's income, not adjustments to a taxpayer's tax liability directly.

If read in isolation, subsection 247(2) mandates a Transfer Pricing Adjustment automatically, regardless of whether the adjustment results in an increase or decrease in a taxpayer's income or loss.

However, it cannot be read in isolation; subsection 247(10) provides that a Transfer Pricing Adjustment that reduces a taxpayer's income or increases a taxpayer's loss (a "Downward Transfer Pricing Adjustment") shall be made only if ". . . in the opinion of the Minister, the circumstances are such that it would be appropriate that the adjustment be made."

Section 18.5 of the *Federal Courts Act*

As noted above, the effect of section 18.5 of the *Federal Courts Act*, as it applies to this decision, is that the Minister's discretionary decision under subsection 247(10) is not subject to judicial review to the extent it may be appealed to the Tax Court.

In *Westminster Savings Credit Union v. Canada (Attorney General)*,[5] the Court held that section 18.5 should be interpreted to preclude parallel proceedings in the Federal Court and the Tax Court "in respect of substantially the same underlying issue". In that decision, the Minister had issued a letter stating that the taxpayer was not a "credit union"

[1] R.S.C. 1985, App. II, No. 5.

[2] R.S.C. 1985, c. T-2.

[3] R.S.C. 1985, c. F-7.

[4] *Income Tax Act*, RSC 1985, c. 1 (5th Supp.) as amended (the "Act"). Unless otherwise noted, all statutory references herein are to this Act.

[5] 2019 DTC 5135 (FC).

under the *Excise Tax Act*.[6] The taxpayer applied to the Federal Court for judicial review of that letter. By the time the matter came on for hearing, the Minister had assessed the taxpayer under the *Income Tax Act* on the basis that it was not a credit union. The Court held that, as the definition of "credit union" under the *Excise Tax Act* adopts the definition of "credit union" in the Act, an appeal to the Tax Court of the income tax assessment would resolve the issue under both statutes and hence section 18.5 applied to preclude judicial review. The Court stated that allowing the taxpayer's application for judicial review would run counter to the approach of interpreting section 18.5 to preclude parallel proceedings "in respect of substantially the same underlying issue".

Tax Court Decision

As stated above, under section 12 of the *Tax Court of Canada Act*, the Tax Court has exclusive appellate jurisdiction to determine the correctness of assessments issued under the Act, which entails determining whether the facts and applicable law support the assessment.[7] In *Dow*, the Court held that as the Minister's decision under subsection 247(10) is an essential component of an assessment and goes to the correctness of that assessment; it follows that a challenge to the Minister's exercise of discretion under subsection 247(10) falls within the appellate jurisdiction of the Tax Court.

The Court's view was that the Minister could not issue a final assessment without taking into account her decision not to allow a Downward Transfer Pricing Adjustment. More specifically, where the criteria exist for a potential Downward Transfer Pricing Adjustment, the Court interpreted subsection 247(10) as mandating the Minister to form an opinion as part of the assessment process. It follows, held the Court, that an assessment cannot be correct if it is issued before the Minister forms an opinion under subsection 247(10).

The Court also considered the fact that, in exercising discretion under subsection 247(10), the Minister is neither required nor permitted to form any opinion or make any determination on the appropriate amount of a Downward Transfer Pricing Adjustment. The Minister only forms an opinion on whether making the Downward Transfer Pricing Adjustment is appropriate in the circumstances. The Court distinguished these two types of discretions and held that the Minister's lack of discretion to determine the amount of a Downward Transfer Pricing Adjustment does not remove the matter from the Tax Court's jurisdiction.

A Reasonable Application of "Correctness"?

Under subsection 247(10), the Minister has the discretion to make a binary decision (i.e., to allow the Downward Transfer Pricing Adjustment, or not). If there were a "correct" decision, then the alternative decision would be incorrect. In such a case, the Minister would have no discretion to make a decision under subsection 247(10), which is not its intended effect.

For the Minister to retain her discretion under subsection 247(10), she must be able to choose between the two options, assuming such a decision is defensible in respect of the facts and law and considering the existence of justification, transparency, and intelligibility within the decision-making process.

Given that this is the language of judicial review (see *Canada (Minister of Citizenship and Immigration) v. Vavilov*),[8] the Court's decision that the Minister's discretionary decision could be appealed is surprising.

Conclusion

While this decision is perhaps welcome, it strains the usual understanding of how the Minister's discretionary decisions may be challenged. Time will tell if future judges adhere to this decision or distinguish it out of existence.

— *Francis Chang, Articling Student, Dentons Canada LLP, Vancouver*

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[6] R.S.C. 1985, Chapter E-15.

[7] *JP Morgan Asset Management (Canada) Inc. v. Minister of National Revenue*, 2014 DTC 5001 (FCA).

[8] 2019 SCC 65.

CURRENT ITEMS OF INTEREST

Online Accounts Locked (February 16, 2021)

The Canada Revenue Agency ("CRA") has locked thousands of online accounts after an internal investigation found some user credentials may be in the hands of "unauthorized" individuals. The CRA stated the accounts had not been compromised, but were vulnerable. The move prompted an e-notification from the CRA to affected users advising that their email address had been removed from their account. Directions how to regain access to their online accounts will be mailed to affected taxpayers.

Excise Duty Rates (February 12, 2021)

The CRA updated the webpage www.canada.ca/en/revenue-agency/services/forms-publications/publications/edrates/excise-duty-rates.html, which provides the rates of all excise duty imposed under the *Excise Act, 2001* on spirits, wine, tobacco products, and cannabis products and under the *Excise Act* on beer.

CRA Cancels APA Cost Recovery Charges

The CRA's advance pricing arrangement ("APA") program is intended to help provide certainty regarding transfer pricing issues. To participate in the program, taxpayers must normally pay a cost recovery charge at the beginning of the APA process. However, effective immediately the CRA has cancelled cost recovery charges for APAs.

The decision to cancel cost recovery charges for APAs is a result of a detailed review of the CRA's Competent Authority Services Division's current APA cost-sharing model with taxpayers and an analysis of best practices amongst other tax administrations' APA programs.

Because of the pandemic, the CRA has adapted to using online remote collaboration tools. When the pandemic is over the CRA will continue to consider alternatives to travel, but it will also continue conducting domestic and foreign site visits and visit other tax jurisdictions for negotiations when required. The CRA will incur those travel costs.

If a taxpayer has already remitted a cost recovery charge for an existing APA, the unused portion will be refunded upon conclusion of the APA and no further charges will be made to the taxpayer's account. Where taxpayers have recently received conditional acceptance letters, they will not be required to submit the cost recovery charge, and any cheque that may have already been submitted but not processed will be returned.

RECENT CASES

Appeal allowed with respect to application of gross negligence penalties

This is an appeal of a decision by the Tax Court of Canada against the appellant on June 27, 2019, confirming the inclusion of shareholder's benefits in the appellant's income for taxation years 2007 to 2011, as well as the application of gross negligence penalties. During the years 2007 to 2011, various amounts were withdrawn from the account of the appellant's corporation and transferred to the appellant's personal account or the accounts of his immediate family members, and the appellant's corporation (M.D. Consulting) paid certain personal expenses. The appellant was reassessed to include amounts totalling $2,864,209 in his income as well as gross negligence penalties. The appellant argued that the assessments for taxation years 2007 to 2010 were statute-barred and that the Tax Court judge had wrongfully transferred the onus of proof from the Minister to the appellant. The appellant also argued that amounts transferred from his corporation to himself or members of his family were repayments of loans made to the corporation and not taxable shareholder's benefits.

The appeal was allowed in part. The Federal Court of Appeal ("FCA") stated that in listing the issues, the Tax Court judge should have recognized that for four of the five taxation years that were before him, the Minister had the onus of proving that there was a misrepresentation and that such misrepresentation was attributable to neglect, carelessness, or wilful default (there being no allegation of fraud in this case) in order to justify reassessment of statute-barred taxation years. However, in the view of the Court, this did not affect the outcome of the case in relation to the question of whether the statute-barred years could have been reassessed. After reviewing the facts and evidence, the FCA concluded that there was sufficient evidence before the Tax Court judge for him to conclude that the Minister had satisfied this onus. The appellant had made a misrepresentation in his tax returns for 2007 to 2010 by not reporting the amounts that were transferred to him and his family by the corporation, which, based on the evidence as presented, were not, on a balance of probabilities, repayments of amounts due to him. This misrepresentation was attributable to the neglect or carelessness of the appellant in not properly maintaining a shareholders' loan account. Effectively, it is clear from the evidence presented at the hearing that there is no dispute that the appellant withdrew the amounts in question from his corporation during the taxation years in issue. There is also no dispute that no shareholders' loan account ledger that accurately reflected the amounts withdrawn was presented to either the auditor for the Canada Revenue Agency or the Tax Court. On the other hand, the Court allowed the appellant's appeal in relation to the application of gross negligence penalties. The Court stated that it is important to recognize that the statutory requirements for reassessing a statute-barred year are not the same as the statutory requirements for assessing gross negligence penalties. The requirements for reassessing a statute-barred year are met if the misrepresentation is attributable to neglect or carelessness, without the need to consider whether the misrepresentation was attributable to wilful default or whether the taxpayer committed fraud (which in and of themselves could also justify the reassessment of a statute-barred year). Therefore, neglect or carelessness should not be confused with gross negligence. Conduct that would justify the assessment of a gross negligence penalty is conduct that is tantamount to intentional acting. Conduct that would be tantamount to intentional acting to avoid the payment of taxes on money that is withdrawn from a corporation is different from careless or neglectful conduct. Since the appellant's position, which he maintained throughout the Tax Court hearing and in the FCA appeal, was that he was simply repaying himself amounts that he had previously advanced to the corporation, there is no basis for the conclusion that the appellant "admittedly knew he received" shareholder benefits. The appellant's failure to maintain proper records does not establish that his failure to include the amounts withdrawn in his income demonstrated "a high degree of negligence tantamount to intentional acting" or that he was indifferent as to whether he complied with the Act. The appellant's failure to include the amounts reassessed in his income, in the circumstances of this case, did not amount to gross negligence.

Deyab v. The Queen

2021 DTC 5001

Decision to deny interest relief was reasonable

In the mid-1980s, the appellants invested in a scheme that was ultimately determined to be fraudulent. Tax losses and deductions claimed by the appellants were disallowed by the CRA. The TCC dismissed the appellants' tax appeals. The appellants also sought relief under subsection 220(3.1) of the *Income Tax Act* from the interest that had accrued on their unpaid taxes. The request was considered by three different officials within the CRA and the appellants received some 15 years of interest relief as a result of the first two administrative reviews. The third review determined that no additional interest relief was warranted; this decision was affirmed by the Federal Court (2019 DTC 5103). The appellants appealed from that judgment, asserting that the CRA's decision to deny them further interest relief was unreasonable and the CRA official carrying out the third administrative review failed to consider their request for relief in light of paragraph 26(a) of CRA Information Circular 07-1R1, "Taxpayer Relief Provisions". This provision states that interest may be waived or cancelled if it resulted from processing delays on the part of the CRA that result in the taxpayer not being informed, within a reasonable time, that an amount was owing.

The appeal was dismissed. In determining whether to grant taxpayer relief pursuant to subsection 220(3.1), the Minister does not have a free hand to do whatever she wants, to act on a whim, or to unthinkingly rubber-stamp an earlier assessment. The Minister's discretion must also be genuinely exercised, and must not be fettered or dictated by policy statements such as Information Circular 07-1R1. While it is true that the third administrative reviewer did not make express reference to this provision in his decision, it is clear that he considered whether the appellants should receive additional interest relief in light of delays on the part of the CRA in processing their tax returns. The delegate considered the appellants' submissions and explained why he was not persuaded that any additional relief was warranted. His decision was transparent, intelligible, and justified. Both the rationale for rejecting the appellants' relief request and the outcome to which it led were reasonable, and no basis was shown to warrant the judicial intervention. The Federal Court thus did not err in finding the Minister's delegate's decision to be reasonable, and the appeal was dismissed.

Belchetz v. The Queen

2021 DTC 5003

Court used residual discretion to allow fresh evidence

The Crown sought an order pursuant to Rule 351 of the *Federal Courts Rules* granting leave to present fresh evidence and an order pursuant to Rule 343(3) to determine the content of the appeal book as proposed. The only issue in dispute concerned the fresh evidence. The decision under appeal was the Tax Court of Canada's dismissal of the Crown's motion to amend its reply to the notice of appeal to add new allegations and arguments (2020 DTC 1087), including an argument that a loan in issue in the taxpayer's appeal was a sham (the "Sham Argument"). The taxpayer opposed the introduction of the Sham Argument on the basis that it would require evidence of subjective intentions and purpose at the time of the transactions in question, and the primary person with such knowledge, Robert Pomeroy, had died. The taxpayer supported its opposition with excerpts from the transcript of a 2018 examination for discovery of Mr. Pomeroy. In the reasons dismissing the Crown's motion to amend its reply, the Tax Court agreed that Mr. Pomeroy's testimony would be important to the Sham Argument, and allowing the amendment to add that argument after Mr. Pomeroy's death would be unjust to the taxpayer. The Crown then requested leave of the Federal Court of Appeal to introduce the entirety of the transcript of Mr. Pomeroy's 2018 discovery (the "New Evidence"). The Crown argued the New Evidence was important to demonstrate that Mr. Pomeroy had little knowledge of the transactions in question, and therefore he could not have given evidence of importance to the appeal before the Tax Court. The Crown planned to rely on the New Evidence to overcome the Tax Court's finding that the taxpayer would suffer an injustice if the amendment was allowed.

The motion was allowed. The parties cited different authorities for the legal test applicable to a motion to adduce fresh evidence. The Court preferred the legal test set out in *Coady v. Canada (Royal Mounted Police)*, 2019 FCA 102: the evidence (1) could not have been adduced at trial with the exercise of due diligence; (2) is relevant in that it bears on a decisive or potentially decisive issue on appeal; (3) is credible in the sense that it is reasonably capable of belief; and (4) is such that, if believed, could reasonably have affected the result in the court. If the evidence fails to meet the foregoing criteria, courts still possess a residual discretion to admit the evidence on appeal. Such discretion should be exercised sparingly and only in the "clearest of cases", where the interests of justice so require. Because the parties cited different authorities for the legal test in the present motion, they had not addressed each of the four requirements enumerated in *Coady*. The credibility of the New Evidence was not in dispute, so the Court of Appeal distilled the taxpayer's opposition to the motion into three points: the Crown failed to meet the requirements that (a) the New Evidence could not have been adduced before the Tax Court with the exercise of due diligence; (b) the New Evidence was relevant in that it bears on a decisive or potentially decisive issue on appeal; and (c) if believed, the New Evidence could reasonably have affected the result in the court below. The Court found the Crown failed to prove (a), which meant it failed the *Coady* test. However, *Coady* recognizes the courts' residual discretion to admit new evidence on appeal, sparingly, and only in the clearest of cases. In exercising this discretion in an appeal of an interlocutory decision, the Court stated these requirements should not be applied strictly — regard must be had for the limited opportunity for putting forward all the material as at trial. On balance, the Federal Court of Appeal found that the interests of justice required that the Court exercise its residual discretion to admit the New Evidence, and issued an order to that effect.

The Queen v. Pomeroy Acquireco Ltd.

2021 DTC 5002

TAX NOTES

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