Tax Notes

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Wolters Kluwer

2022 ECONOMIC STATEMENT

— *Wolters Kluwer Canada*

Introduction

The Deputy Prime Minister and Minister of Finance, Chrystia Freeland, presented the 2022 Fall Economic Statement (the "Statement") on November 3, 2022. The Statement announced several new and updated tax measures. Some new legislation was also introduced. Freeland tabled Bill 32, *An Act to implement certain provisions of the fall economic statement tabled in Parliament on November 3, 2022 and certain provisions of the budget tabled in Parliament on April 7, 2022*, which passed Second Reading on November 22, 2022.

The Statement contained economic messages relating to high inflation, rising interest rates, a strong labour market, and slowing economic activity. A summary of the latest fiscal projections is provided below. Amounts are in the billions of dollars.

		Projection					
Budgetary Balance	**2021–2022**	**2022–2023**	**2023–2024**	**2024–2025**	**2025–2026**	**2026–2027**	**2027–2028**
Baseline Scenario	-90.2	-36.4	-30.6	-25.4	-14.5	-3.4	4.5
Downside Scenario	-90.2	-49.1	-52.4	-42.3	-30.4	-18.6	-8.3

All of the new tax-related announcements in the Statement are summarized below.

Extension of the Residential Property Flipping Rule to Assignment Sales

Starting on January 1, 2023, the Residential Property Flipping Rule proposed in the 2022 Budget deems profits arising from dispositions of residential property (including a rental property) that was owned for less than 12 months to be business income, subject to some exceptions.

The 2022 Fall Economic Statement proposes to extend the deeming rule to profits arising from the disposition of the rights to purchase a residential property via an assignment sale if the rights were assigned after having been owned for less than 12 months.

For the sale of constructed property, the 12-month holding period for the Residential Property Flipping Rule will reset once the taxpayer who entered into a purchase and sale agreement secures ownership of the property. This is to prevent bypassing the rule simply by holding the rights to purchase the property before it was constructed.

Automatic Advance for the Canada Workers Benefit

Rather than applying every year to receive their anticipated Canada Workers Benefit ("CWB") entitlement for a taxation year, the 2022 Fall Economic Statement proposes to automatically provide individuals an entitlement for the current taxation year through quarterly advance payments. Individuals must have received the CWB for the previous taxation year and the CRA must have received and accessed their income tax return for the previous year prior to November 1 of the current year.

For couples where both individuals are eligible, the spouse or common-law partner who claimed it using Schedule 6 of the income tax return or who received it through CRA automatic determination will receive the base CWB advance payments.

An individual who received only the disability supplement in the prior year will also receive the advance payment of the current year's supplement.

Eligible individuals will receive half of the advance payments of their estimated CWB entitlement for a year in July, October, and January. The rest of the entitlement will be calculated and paid through their tax return for the year.

In the case where a couple formed during the year and both were receiving advance payments, only the individual claiming the couple's CWB on their tax return reports the advance payments received by both partners for that year. The spouse receiving the advance payments for the disability supplement continues to report the supplement on their own return.

Eligibility to receive advance payments during the course of a year ceases where an individual is:

- incarcerated for a period of 90 days or more;
- moves out of the country; or
- dies prior to July 1.

However, the eligible spouse of an individual ineligible due to one of the reasons above could become entitled to advance payments based on their individual working income and net income for the portion of the year following the change in circumstance above. Other changes in circumstances will not affect individuals' advance payment entitlements for the current taxation year.

Advance payments start automatically in July 2023 for the 2023 taxation year. The existing option for advance payment application ends after January 1, 2023.

Tax on Share Buybacks

Following the lead in the US, the 2022 Fall Economic Statement announced that the government plans to introduce a 2% corporate tax that would apply on the net value of all types of "share buybacks by public corporations in Canada" in order to encourage corporations to reinvest their profits in their workers and businesses. No details were provided as to how this tax would be implemented or as to exactly which buybacks would be subject to the tax.

The details of this new tax will be announced in Budget 2023, and the tax will come into force on January 1, 2024.

International Tax Reform

Canada and 136 other members of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting have developed a two-pillar plan for international tax reform, which was agreed to in October 2021.

Pillar One (Reallocation of Taxing Rights)

Pillar One will ensure that the largest and most profitable global corporations, including large digital corporations, pay their fair share of tax in the jurisdictions where their users and customers are located. Significant progress has been made in establishing the technical rules of the new system, and the OECD has been conducting ongoing public consultations. The Inclusive Framework's intention is to complete multilateral negotiations so that the treaty to implement Pillar One can be signed in the first half of 2023, with a view to it entering into force in 2024.

Pillar Two (Global Minimum Tax)

Pillar Two, a global minimum tax regime, will ensure that multinational corporations are subject to a minimum effective tax rate of 15% on profits in every jurisdiction in which they operate. The 2022 Fall Economic Statement reiterates that Canada is committed to the global minimum tax on large corporations and is continuing to work closely with our international partners to develop a coordinated implementation framework, to be put in place in a timely and coordinated manner.

Alternative Minimum Tax

Through significant use of deductions, tax credits, and other ways of having income taxed at lower rates, some of the wealthiest Canadians pay comparatively little personal income tax as a share of their income. The Alternative Minimum Tax ("AMT"), which was introduced in 1986, was intended to address this and ensure that high-income Canadians could not disproportionately lower their tax bill through advantages in the tax system.

In this year's federal budget, the government committed to examining a new minimum tax regime to ensure that all wealthy Canadians pay their fair share of tax. The 2022 Fall Economic Statement reaffirms this intent, and a detailed proposal and path for implementation will be released in Budget 2023.

Excess Interest and Financing Expense Limitation

The excess interest and financing expense limitation ("EIFEL") rules were first introduced as draft legislative proposals on February 4, 2022. The Statement includes a revised version of these proposals. Initially, the EIFEL rules were scheduled to apply as of January 1, 2023. However, the implementation date has been deferred to October 1, 2023. Interested parties can send comments regarding the revised legislation to Consultation-Legislation@fin.gc.ca by January 6, 2023.

Notable changes to the latest proposed rules (compared to the February 4 version) include:

- Adding the concept of "exempt interest and financing expenses";
- Making various modifications to the definition of "adjusted taxable income";
- Adding the concept of "financial institution group entity";
- Making various modifications to the definition of "interest and financing expenses"; and
- Making many modifications related to foreign affiliates.

Mandatory Disclosure Rules

The government is delaying the coming into force date of the reporting requirements for reportable transactions and notifiable transactions until the date on which a bill implementing these changes receives Royal Assent. This delay will allow the government to fully assess feedback received via the recent consultation. However, the coming into force date for uncertain tax treatments will remain the same as described in August (i.e., taxation years beginning after 2022, with penalties only applying after Royal Assent).

New Investment Tax Credits

Investment Tax Credit for Clean Technologies

The Statement proposes to introduce a refundable clean technology investment tax credit ("ITC") equal to 30% of the capital cost of eligible equipment. The following types of equipment would be eligible for the credit:

- equipment to generate electricity from solar, wind, and water energy that is described under subparagraphs (*d*)(ii), (iii.1), (v), (vi), and (xiv) of capital cost allowance Class 43.1;
- stationary electricity storage equipment that is described under subparagraphs (*d*)(xviii) and (xix) of Class 43.1, but that does not use any fossil fuels in operation, which includes, but is not limited to, batteries, flywheels, supercapacitors, magnetic energy storage, compressed air energy storage, pumped hydroelectric energy storage, gravity energy storage, and thermal energy storage;
- active solar heating equipment, air-source heat pumps, and ground-source heat pumps that are described under subparagraph (*d*)(i) of Class 43.1;
- equipment to generate heat or electricity from concentrated solar energy;
- equipment to generate heat or electricity from small modular nuclear reactors; and
- non-road zero-emission vehicles described in Class 56 (e.g., hydrogen or electric heavy-duty equipment used in mining or construction) and charging or refuelling equipment described under subparagraph (*d*)(xxi) of Class 43.1 or subparagraph (*b*)(ii) of Class 43.2 that is used primarily for such vehicles.

The government will continue to review eligibility for relevant technologies, including the possibility of adding new ones.

The clean technology ITC would be available in respect of the capital cost of property that is acquired and that becomes available for use on or after the day that the 2023 Budget is released, where it has not been used for any purpose before its acquisition. The ITC would be gradually phased out starting with property that becomes available for use in 2032 and would no longer be in effect for property that becomes available for use after 2034. The credit would gradually phase out with a credit rate of 20% in 2032, 10% in 2033, and 5% in 2034.

The 30% credit rate for eligible investments would be contingent upon certain labour conditions being fulfilled. A 20% rate would be available to claimants that do not meet these labour conditions. The Department of Finance will consult with a broad group of stakeholders, but especially with unions, on how best to attach labour conditions to the proposed tax credit. Additional details on the labour conditions will be announced in Budget 2023.

Investment Tax Credit for Clean Hydrogen

In the 2022 federal Budget, the government announced that it would create an ITC to support investments in clean hydrogen production. The government commits that it will proceed to establish the parameters under which such a credit will be granted. Consultations will be held with stakeholders, including unions, on how best to set parameters to protect the workers in that industry. The credit is proposed to be as high as 40% for the lowest carbon intensity tier. The maximum rate will be reduced by 10% if the company does not meet certain labour conditions.

The ITC will be refundable and effective for eligible investments made as of the budget day in 2023 and will be phased out after 2030.

Income Reporting by Digital Platforms

The Organisation for Economic Co-operation and Development ("OECD") has presented Model Rules for Reporting by Platform Operators with respect to Sellers in the Sharing and Gig Economy. In compliance with these rules Canada has already enacted Subdivision e of Part IX of the *Excise Tax Act* allowing for simplified compliance with respect to application of the *Goods and Services Tax Act*.

Now, to comply with the new Model Rules that require platform operators to report certain information to the CRA and to follow due diligence procedure, the Minister has presented draft legislation which will result in new Part XX of the *Income Tax* Act, which would come into force on January 1, 2024.

Previously Announced Measures

The Statement confirmed the government's intention to proceed with a long list of previously announced tax and related measures, as modified to take into account consultations and deliberations since their release.

CURRENT ITEMS OF INTEREST

Budget Bill Tabled

Bill C-32, *An Act to implement certain provisions of the fall economic statement tabled in Parliament on November 3, 2022 and certain provisions of the budget tabled in Parliament on April 7, 2022*, passed Second Reading in the House of Commons on November 22.

Part 1 of Bill C-32 implements certain measures in respect of the *Income Tax Act* by:

- providing that any gain on the disposition of a Canadian housing unit within a one-year period of its acquisition is treated as business income;
- introducing the Tax-Free First Home Savings Account;
- phasing out flow-through shares for oil, gas, and coal activities;
- introducing a new 30% Critical Mineral Exploration Tax Credit for specified mineral exploration expenses incurred in Canada and renounced to flow-through share investors;
- introducing the Canada Recovery Dividend under which banks and life insurers' groups pay a temporary one-time 15% tax on taxable income above $1 billion over five years;
- increasing the corporate income tax rate of banks and life insurers' groups by 1.5% on taxable income above $100 million;
- providing additional reporting requirements for trusts;
- providing rules applicable to mutual fund trusts listed on a designated stock exchange in Canada with respect to amounts that are allocated to redeeming unitholders;
- providing the Minister of National Revenue with the discretion to decline to issue a certificate under section 116 of the *Income Tax Act* in certain circumstances relating to the administration and enforcement of the *Underused Housing Tax Act*;
- doubling the First-Time Homebuyers' Tax Credit;
- expanding the eligibility criteria for the Medical Expense Tax Credit in respect of medical expenses incurred in Canada related to surrogate mothers and donors and fees paid in Canada to fertility clinics and donor banks;

- introducing the Multigenerational Home Renovation Tax Credit;
- allowing access to the small business tax rate on a phased-out basis up to taxable capital of $50 million;
- modifying the computation of income as a result of the adoption of a new international accounting standard for insurance contracts;
- introducing a new graduated disbursement quota rate for charities;
- providing that the general anti-avoidance rules can apply to transactions that affect tax attributes that have not yet been used to reduce taxes;
- strengthening the rules on avoidance of tax debts;
- modifying the calculation of the taxes applicable to registered investments that hold property that is not a qualified investment;
- modifying the tax treatment of certain interest coupon stripping arrangements that might otherwise be used to avoid tax on cross-border interest payments;
- clarifying the applicable rules with respect to audits by CRA officials, including requiring taxpayers to give reasonable assistance and to answer all proper questions for tax purposes; and
- extending the capital cost allowance for clean energy and the tax rate reduction for zero-emission technology manufacturers to include air-source heat pumps.

It also makes related and consequential amendments to the *Excise Tax Act*, the *Excise Act, 2001*, and the *Income Tax Regulations*.

Part 2 amends the *Excise Act, 2001* and other related texts in order to implement changes to:

- the federal excise duty frameworks for cannabis and other products by, among other things,
  - permitting excise duty remittances for certain cannabis licensees to be made on a quarterly rather than a monthly basis, starting from the quarter that began on April 1, 2022, and
  - allowing the transfer of packaged, but unstamped, cannabis products between licensed cannabis producers; and
- the federal excise duty framework for vaping products in relation to the markings, customs, storage, and excise duty liability of these products.

Part 3 amends the *Underused Housing Tax Act* to make amendments of a technical or housekeeping nature. It also makes regulations under that Act in order to, among other things, implement an exemption for certain vacation properties.

Notable Changes in Bill C-32

Often when tax legislation is included in a bill, the proposals have been altered from their previous form. As we analyzed what was in new Bill C-32, we noticed some important changes that affect the coming into force dates of the measures. First, regarding the new reporting requirements for trusts, the application date was delayed to taxation years that end after December 30, 2023 (it was previously taxation years ending after December 30, 2022). Second, the implementation date for the new First Home Savings Account was slightly delayed to April 1, 2023 from the original date of January 1, 2023.

Indexation Adjustment for Personal Income Tax and Benefit Amounts

The CRA has published the indexed personal income tax and benefit amounts for 2023. Not unexpectedly, the indexation percentage for 2023 is much higher compared to recent prior years — 6.3%.

Increases to tax bracket thresholds, amounts relating to non-refundable credits, and most other amounts below take effect on January 1, 2023.

Increases in amounts for certain income-tested benefits like the goods and services tax credit, the Canada child benefit and Child disability benefit, take effect on July 1 to coincide with the beginning of the program year for payments of these benefits.

All of the indexed figures for 2023 are listed below.

Indexation increase per year

Indexation increase	6.3%

Tax bracket thresholds

Taxable income above which the 20.5% bracket begins	$53,359
Taxable income above which the 26% bracket begins	$106,717
Taxable income above which the 29% bracket begins	$165,430
Taxable income above which the 33% bracket begins	$235,675

Amounts relating to non-refundable tax credits

Basic personal amount for individuals whose net income for the year is greater than or equal to the amount at which the 33% tax bracket begins	$13,521
Basic personal amount for individuals whose net income for the year is less than or equal to the amount at which the 29% tax bracket begins	$15,000
Spouse or common-law partner amount (maximum) for individuals whose net income for the year is greater than the amount at which the 33% tax bracket begins	$13,521
Spouse or common-law partner amount (maximum) for individuals whose net income for the year is less than or equal to the amount at which the 29% tax bracket begins	$15,000
Spouse or common-law partner amount for individuals whose net income for the year is greater than or equal to the amount at which the 33% tax bracket begins (maximum if eligible for the Canada caregiver amount for a dependent spouse or common-law partner)	$16,020
Spouse or common-law partner amount for individuals whose net income for the year is less than or equal to the amount at which the 29% tax bracket begins (maximum if eligible for the Canada caregiver amount for a dependent spouse or common-law partner)	$17,499
Amount for an eligible dependant (maximum) for individuals whose net income for the year is greater than or equal to the amount at which the 33% tax bracket begins	$13,521
Amount for an eligible dependant (maximum) for individuals whose net income for the year is less than or equal to the amount at which the 29% tax bracket begins	$15,000
Amount for an eligible dependant for individuals whose net income for the year is greater than or equal to the amount at which the 33% tax bracket begins (maximum if eligible for the Canada caregiver amount for a dependant)	$16,020
Amount for an eligible dependant for individuals whose net income for the year is less than or equal to the amount at which the 29% tax bracket begins (maximum if eligible for the Canada caregiver amount for a dependant)	$17,499
Canada caregiver amount for children under age 18	$2,499
Age amount	$8,396
Net income threshold for age amount	$42,335
Canada employment amount (maximum)	$1,368
Canada caregiver amount for other infirm dependants age 18 or older (maximum amount)	$7,999
Net income threshold for Canada caregiver amount	$18,783
Disability amount	$9,428
Supplement for children with disabilities (maximum)	$5,500
Threshold relating to allowable child care and attendant care expenses	$3,221
Adoption expenses (maximum per adoption)	$18,210
Medical expense tax credit (3% of net income ceiling)	$2,635

Refundable medical expense supplement

Maximum supplement	$1,399
Minimum earnings threshold	$4,083
Family net income threshold	$30,964

Old age security repayment

Old age security repayment threshold	$86,912

Certain board and lodging allowances paid to players on sports teams or members of recreation programs

Income exclusion (maximum per month)	$411

Tradesperson's tools deduction

Threshold amount relating to cost of eligible tools	$1,368

Advanced life deferred annuities (ALDA)

Lifetime dollar limit	$160,000

Canada training credit (CTC)

Minimum working income threshold	$10,994
Maximum net income	$155,625

Goods and services tax/harmonized sales tax credit

Adult maximum	$325
Child maximum	$171
Single supplement	$171
Phase-in threshold for the single supplement	$10,544
Family net income at which credit begins to phase out	$42,335

Tax-free savings account

Annual TFSA dollar limit	$6,500

Lifetime capital gains exemption for qualified farm or fishing property and qualified small business corporation shares

Exemption limit	$971,190
Deduction limit (since 1/2 of the capital gain is taxable)	$485,595
Additional exemption amount for qualified farm or fishing property	$28,810
Additional deduction amount for qualified farm or fishing property (since 1/2 of the capital gain is taxable)	$14,405

Canada child benefit (CCB)

CCB (base benefit, child under age 6)	$7,437
CCB (base benefit, child aged 6 to 17)	$6,275
Adjusted family net income at which phase out begins	$34,863
Second phase out threshold	$75,537
Base phase out amount for one eligible child	$2,847
Base phase out amount for two eligible children	$5,491
Base phase out amount for three eligible children	$7,728
Base phase out amount for four or more eligible children	$9,355

Child disability benefit (CDB)

Maximum benefit	$3,173
Family net income threshold for phase out	$75,537

Increased GST/HST Credit Being Paid

On Friday November 4, the CRA began issuing one-time payments of the enhanced GST/HST credit amount that was enacted by Bill C-30.

New Prescribed Regions for Livestock Tax Deferral

Agriculture and Agrifood Canada updated its list of prescribed regions for livestock tax deferral on October 31. For the full list of regions, see agriculture.canada.ca/en/agriculture-and-environment/drought-watch-and-agroclimate/livestock-tax-deferral-provision/2022-livestock-tax-deferral-prescribed-regions.

Maximum Pensionable Earnings for 2023

The maximum pensionable earnings under the Canada Pension Plan ("CPP") for 2023 will be $66,600 — up from $64,900 in 2022. The new ceiling was calculated according to a CPP legislated formula that reflects the growth in average weekly wages and salaries in Canada.

The basic exemption amount for 2023 remains at $3,500.

The employee and employer contribution rates for 2023 will be 5.95% — up from 5.70% in 2022 — and the self-employed contribution rate will be 11.90% — up from 11.40% in 2022. The increase in contribution rate is due to the continued implementation of the CPP enhancement.

The maximum employer and employee contribution to the plan for 2023 will be $3,754.45 each and the maximum self-employed contribution will be $7,508.90. The maximums in 2022 were $3,499.80 and $6,999.60, respectively.

Progress of Legislation

Bill C-31, *An Act respecting cost of living relief measures related to dental care and rental housing*, received Royal Assent on November 17. The bill included the *Dental Benefit Act*, *Rental Housing Benefit Act*, and consequential amendments to the *Income Tax Act* and *Excise Tax Act*.

CRA Revises Information Circular

The CRA revised IC76-12R8, *Applicable rate of part XIII tax on amounts paid or credited to persons in countries with which Canada has a tax convention*, on October 26. The information circular has been revised because of changes to Canada's tax conventions as well as changes to paragraph 25 of the IC.

CRA Updates Recapture of SR&ED Investment Tax Credit Policy

The CRA updated its policy regarding the recapture of scientific research and experimental development ("SR&ED") investment tax credits ("ITCs") on October 14. Many revisions were made to the SR&ED policy, which can be found under *Appendix B — Revisions*, here: www.canada.ca/en/revenue-agency/services/scientific-research-experimental-development-tax-incentive-program/recapture-investment-tax-credit-policy.html.

FOCUS ON CURRENT CASES

This is a regular monthly feature examining recent cases of special interest, coordinated by Ron Dueck of Dentons Canada LLP. The contributors to this feature are from Dentons Canada LLP, Montréal, Toronto, Calgary, Edmonton, and Vancouver.

3295940 Canada Inc. v. The Queen, 2022 DTC 1080 (Tax Court of Canada) — GARR Applied on a Disposition of Shares Where Subsection 55(2) Did Not Apply

BACKGROUND

This case considered whether a series of transactions undertaken prior to a sale of shares, which series had the effect of reducing the vendor's capital gain on the sale by $31.5M dollars, was subject to the general anti-avoidance rule ("GAAR").

The relevant corporate structure was as follows. Gestion Micsau Inc. ("Micsau") owned 100% of the outstanding shares of 3295940 Canada Inc. ("329"), which in turn owned 2M Class B shares of Sabex Holdings Ltd. ("Holdings"), which in turn owned 100% of the outstanding shares of Sabex 2002 Inc. (the "Target"). Micsau wanted to effect the sale by way of selling the shares of 329. However, because of liability concerns, the purchaser was not interested in purchasing the shares of 329.

The parties undertook the following series of pre-sale transactions to effect the sale by way of rolling Holdings into a new corporation, 4244851 Canada Inc. ("4244"), whereby the purchaser would purchase the shares of 4244 from 329.

- On January 29, 2004, Holdings increased the paid-up capital ("PUC") of its Class B shares held by 329 by $4.0M, resulting in a corresponding increase of $4.0M to both the "safe income" attributable to those shares and 329's adjusted cost base ("ACB") in those shares pursuant to paragraph 53(1)(*b*) of the *Income Tax Act* (the "ITA").
- On June 21, 2004, Micsau incorporated 4244, in which it held a common share having nominal value.
- On June 25, 2004, Holdings redeemed 500,000 of its 2M Class B shares held by 329 for $13.31M. The Class B shares had nominal PUC and ACB. The "safe income", within the meaning of subsection 55(5) of the ITA, attributable to the redeemed 500,000 Class B shares was $1.7M. The fees relating to the transaction were $0.06M. Accordingly, 329 realized a capital gain of $11.55M (i.e., $13.31M - $1.7M - $0.06M) under subsection 55(2) of the ITA. Half of this capital gain, $5.78M, was added to the capital dividend account ("CDA") of 329 pursuant to paragraph 38(*a*) and subsection 89(1) of the ITA.
- On June 29, 2004, 329 amended its articles of incorporation to create new Class D preferred shares. These new Class D preferred shares were non-voting shares that were redeemable by the corporation or the shareholder at a price of $1 per share.
- On June 30, 2004:
  - Micsau exchanged all of its shares in 329 for 31.5M Class D preferred shares and 100 common shares of 329. The parties filed an election under section 85 in respect of the exchange using an elected amount of $48.1M, which resulted in an ACB of $31.5M for the Class D preferred shares and $16.6M for the 100 common shares. The PUC for both classes of shares remained nominal.
  - Micsau then transferred its 31.5M Class D preferred shares in 329 to 4244 in exchange for 31.5M Class D preferred shares in 4244, which were also non-voting shares that were redeemable by the corporation or the shareholder at a price of $1 per share. As the Class D shares in 4244 had an aggregate redemption value equal to the ACB of the Class D shares in 329 that were exchanged, no gain or loss was realized on this transfer.
  - 329 then disposed of its remaining 1.5M Class B shares in Holdings to 4244 in exchange for 57M Class D preferred shares and 31.5M common shares in 4244. The parties filed an election under section 85 in respect of the exchange using an elected amount of $57.0M, resulting in 329 realizing a capital gain of $53.0M. Half of this capital gain, $26.5M, was added to 329's CDA. The ACB of the 57M Class D preferred shares received by 329 was $57.0M (pursuant to paragraph 85(1)(*g*) of the ITA) and the ACB of the 31.5M common shares was nominal (pursuant to paragraph 85(1)(*h*) of the ITA). The 57M Class D preferred shares and 31.5M common shares in 4244 both had nominal PUC.
- On August 11, 2004:
  - 329 redeemed its 31.5M Class D preferred shares held by 4244 in exchange for a $31.5M promissory note, resulting in an inter-corporate deemed dividend of $31.5M pursuant to subsection 84(3) of the ITA. 329 elected for the deemed dividend to be a capital dividend.
  - 4244 similarly redeemed 31.5M common shares and 110,000 Class D preferred shares held by 329 in exchange for a $31.5M promissory note, resulting in an inter-corporate deemed dividend of $31.5M pursuant to subsection 84(3) of the ITA. 4244 elected for the deemed dividend to be a capital dividend.
  - 329 and 4244 offset and cancelled their respective $31.5M notes.
  - On August 12, 2004, Micsau transferred its 31.5M Class D preferred shares in 4244 to 329 in exchange for 31.5M Class D preferred shares in 329 on a tax-deferred basis under section 85. The parties selected an elected amount of $31.5M, which was equal to the ACB of the shares disposed of. Following this transaction, 329 held a total of 88.39M Class D preferred shares in 4244 with an ACB of $88.39M.
  - On August 13, 2004, 329 sold its $88.39M Class D preferred shares in 4244 to the purchaser for a purchase price of $88.39M. After accounting for 329's transaction costs of $0.17M, 329 realized a capital loss of $0.17M on the sale.
  - On August 16, 2004, 329 redeemed 31.5M Class D preferred shares held by Micsau for $31.5M. Pursuant to subsection 84(3) of the ITA, 329 was deemed to have paid, and Micsau was deemed to have received, a dividend of $31.5M. Pursuant to paragraph (j) of the definition of "proceeds of disposition" in section 54 of the ITA, Micsau was deemed to have disposed of its 31.5M Class D preferred shares in 329 for proceeds equal to nil. Accordingly, because the ACB of those shares was $31.5M, Micsau realized a capital loss of $31.5M. However, pursuant to subsection 112(3) of the ITA, this loss was deemed to be nil.

- On August 11, 2004:
  - 329 redeemed its 31.5M Class D preferred shares held by 4244 in exchange for a $31.5M promissory note, resulting in an inter-corporate deemed dividend of $31.5M pursuant to subsection 84(3) of the ITA. 329 elected for the deemed dividend to be a capital dividend.

  - 4244 similarly redeemed 31.5M common shares and 110,000 Class D preferred shares held by 329 in exchange for a $31.5M promissory note, resulting in an inter-corporate deemed dividend of $31.5M pursuant to subsection 84(3)) of the ITA. 4244 elected for the deemed dividend to be a capital dividend.
  - 329 and 4244 offset and cancelled their respective $31.5M notes.
- On August 12, 2004, Micsau transferred its 31.5M Class D preferred shares in 4244 to 329 in exchange for 31.5M Class D preferred shares in 329 on a tax-deferred basis under section 85. The parties selected an elected amount of $31.5M, which was equal to the ACB of the shares disposed of. Following this transaction, 329 held a total of 88.39M Class D preferred shares in 4244 with an ACB of $88.39M.
- On August 13, 2004, 329 sold its $88.39M Class D preferred shares in 4244 to the purchaser for a purchase price of $88.39M. After accounting for 329's transaction costs of $0.17M, 329 realized a capital loss of $0.17M on the sale.
- On August 16, 2004, 329 redeemed 31.5M Class D preferred shares held by Micsau for $31.5M. Pursuant to subsection 84(3) of the ITA, 329 was deemed to have paid, and Micsau was deemed to have received, a dividend of $31.5M. Pursuant to paragraph (*j*) of the definition of "proceeds of disposition" in section 54 of the ITA, Micsau was deemed to have disposed of its 31.5M Class D preferred shares in 329 for proceeds equal to nil. Accordingly, because the ACB of those shares was $31.5M, Micsau realized a capital loss of $31.5M. However, pursuant to subsection 112(3) of the ITA, this loss was deemed to be nil.

By reassessment dated November 21, 2008, the Minister of National Revenue (the "Minister") sought to apply the GAAR to add a $31.5M capital gain to 329's income.

ISSUES AND DECISION

For the GAAR to apply, three requirements must be established:

(1) there was a *tax benefit* resulting from a transaction or part of a series of transactions (subsections 245(1) and (2));

(2) the transaction is an *avoidance transaction* in the sense that it cannot be said to have been reasonably undertaken or arranged primarily for a bona fide purpose other than to obtain a tax benefit (subsection 245(3)); and

(3) there was *abusive tax avoidance* in the sense that it cannot be reasonably concluded that a tax benefit would be consistent with the object, spirit, or purpose of the provisions relied upon by the taxpayer.

The burden is on the taxpayer to refute (1) and (2) and on the Minister to establish (3).

329 conceded that the foregoing steps amounted to a series of transactions that resulted in a tax benefit and that the series included an avoidance transaction for the purposes of subsection 245(3) – the tax benefit being the $31.5M reduction of the capital gain that it would otherwise have realized if 329 had sold shares directly to the purchaser.

Accordingly, the only issue before the Court was whether the avoidance transaction abusively defeated the object, spirit, or purpose of the capital gains, capital dividend, and CDA provisions set out in sections 38, 39, 40, 83(2)), 89(1), and 55(2) of the ITA. Justice Real Favreau relied heavily on his 2016 decision in *Pomerleau v. the Queen* (2016 TCC 228) in summarizing the application of the GAAR, and on his 2017 decision in *101139810 Saskatchewan Ltd. v. The Queen*, 2017 DTC 1008 (TCC) in determining the object and purpose of subsection 55(2).

Through a textual, contextual, and purposive analysis, the Court found that the object, spirit, or purpose of subsections 83(2), 89(1), and 55(2) of the ITA is to "prevent a taxpayer from using a tax-free dividend to avoid the capital gain inherent in the shares of a corporation that is attributable to an unrealized appreciation, which would go against the principle of integration that the CDA scheme is pursuing".

The Court held that, through the series of transactions, 329 avoided the application of subsection 55(2) at the time of the cross redemption of its shares and 4244's shares by moving its CDA, which was later returned back to 329. If subsection 55(2) did apply, it would have converted the taxable dividend paid by 4244 into a capital gain. Further, moving the CDA made it possible for 329 to have an ACB in the shares that it held in 4244 equal to the FMV of such shares, thus resulting in no taxes payable on the sale of 4244's shares to Novartis. Accordingly, the Court held that, by proceeding this way, the object, spirit or purpose of subsection 55(2) was frustrated and that the GAAR should apply.

CONCLUSION

The Court held that the GAAR applied because, through a series of transactions, 329 avoided the application of subsection 55(2) by moving its CDA around and the non-application of subsection 55(2) resulted in 329 realizing a capital gain of $64.6M following the disposition of its shares in Holdings, whereas the unrealized capital gain in such shares was $96.1M.

MONY C. THE KING, 2022 DTC 5111 (TAX COURT OF CANADA) — GAAR APPLIES TO ATTRIBUTE TO TAXPAYER CAPITAL GAIN REALIZED BY TAXPAYER'S SPOUSE ON THE SALE OF SHARES

BACKGROUND

In this case, Mr. Charles Mony (the "Taxpayer") appealed a reassessment, issued on October 13, 2017, by which the Minister of National Revenue (the "Minister") attributed to the Taxpayer a capital gain of $450,373 realized by his spouse, Mrs. Isabella Vitté (the "Spouse"), on the sale of the capital stock of Créaform Inc. ("Créaform"). The Minister attributed the capital gain to the Taxpayer pursuant to the general anti-avoidance rule (the "GAAR") set out in section 245 of the *Income Tax Act* ("ITA").

On March 23, 2009, the Taxpayer received an offer from third-party investors to purchase his shares in Créaform, which was a Canadian-controlled private corporation in the business of selling digital technology for taking measurements in three dimensions. Sometime thereafter, the Taxpayer accepted this offer.

On June 25, 2009, the Taxpayer gifted to his Spouse 114,907 shares in Créaform (the "Gifted Shares"). Also on June 25, 2009, the Taxpayer sold to his Spouse another 114,907 shares in Créaform (the "Sold Shares") in exchange for an interest-bearing note (the "Promissory Note") in the amount of $985,728 (which was equal to the fair market value ("FMV") of the Sold Shares at the time). Later that same day, the Spouse sold the Gifted Shares and the Sold Shares to third-party investors for proceeds of $1,971,455.

Pursuant to subsections 73(1) and (1.01) of the ITA, the Taxpayer was deemed to have disposed of the Gifted Shares, and his Spouse was deemed to have acquired the Gifted Shares, for proceeds equal to the adjusted cost base ("ACB") of the Gifted Shares, which was $1,242. Accordingly, the Taxpayer did not realize any capital gain or loss on the transfer of the Gifted Shares.

Subsections 73(1) and (1.01) would have applied similarly to the Sold Shares as they did to the Gifted Shares, except that the Taxpayer elected under subsection 73(1) to exempt the Sold Shares from the application of that provision. Consequently, the Taxpayer sold the Sold Shares to his Spouse for proceeds equal to the FMV of the Sold Shares, which was $985,728. Because the Sold Shares had an ACB of $1,242, the Taxpayer realized a capital gain of $984,486 on which he was taxed.

Prior to the application of subsection 47(1) of the ITA, the tax attributes of the Spouse's Shares were as follows:

	Gifted Shares	Sold Shares	Total
ACB	$1,242	$985,728	$986,970
FMV	$985,728	$985,728	$1,971,456

However, because the Gifted Shares and Sold Shares were identical property, subsection 47(1) of the ITA deemed the Shares to all have the same ACB by the application of the averaging rule, regardless of how the Shares were transferred. The tax attributes of the Spouse's Shares therefore became as follows:

	Gifted Shares	Sold Shares	Total
ACB	$493,485	$493,485	$986,970
FMV	$985,728	$985,728	$1,971,456

Accordingly, the sale of the Gifted Shares and the Sold Shares by the Spouse to the third-party investors resulted in a capital gain of $900,745 calculated as follows:

	Gifted Shares	Sold Shares	Total
Proceeds (equal to FMV)	$985,728	$985,728	$1,971,455
ACB	($493,485)	($493,485)	($986,970)
Expenses	($41,870)	($41,870)	($83,740)
Capital Gain	$450,373	$450,373	$900,745

Because the Gifted Shares were previously transferred from the Taxpayer to his Spouse, the capital gain realized by the Spouse on the disposition of the Gifted Shares was deemed, pursuant to subsection 74.2(1) of the ITA, to be realized by the Taxpayer and not his Spouse. The capital gain realized by the Spouse on the disposition of the Sold Shares would have also been deemed, pursuant to subsection 74.2(1), to be realized by the Taxpayer and not his Spouse except that, pursuant to subsection 74.5(1), subsection 74.2(1) does not apply to the Sold Shares because the Taxpayer received consideration equal to FMV in exchange for the shares (i.e., the Promissory Note). Accordingly, the capital gain of $450,373 realized on the Sold Shares was not deemed to be realized by the Taxpayer but instead remained taxable in the Spouse's hands. The Taxpayer and his Spouse then each claimed the capital gains deduction under subsection 110.6(2.1) of the ITA.

By reassessment issued on October 13, 2017, the Minister sought to apply the GAAR to attribute the entire capital gain realized by his Spouse to the Taxpayer.

ISSUES AND DECISION

For the GAAR to apply, three requirements must be established:

(1) There was a *tax benefit* resulting from a transaction or part of a series of transactions (subsections 245(1) and (2));

(2) The transaction is an *avoidance transaction* in the sense that it cannot be said to have been reasonably undertaken or arranged primarily for a bona fide purpose other than to obtain a tax benefit (subsection 245(3)); and

(3) There was *abusive tax avoidance* in the sense that it cannot be reasonably concluded that a tax benefit would be consistent with the object, spirit or purpose of the provisions relied upon by the taxpayer.

The burden is on the Taxpayer to refute (1) and (2) and on the Minister to establish (3). Because a tax benefit was conceded by the Taxpayer, only (2) and (3) were issues before the Court.

Avoidance Transaction

The Court found that a series of transactions was carried out on June 25, 2009, that consisted of the following individual transactions:

(1) transfer of the Gifted Shares by the Taxpayer to his Spouse;

(2) transfer of the Sold Shares by the Taxpayer to his Spouse; and

(3) sale of the Gifted Shares and Sold Shares by the Spouse to the third-party investors.

The Court determined that transaction (3) was clearly not an avoidance transaction because its main purpose was to make a profit from the sale of shares and to bring new partners into Créaform. The Court did not make a determination with regards to transaction (1) because certain contradictions in the testimony of the Taxpayer and his Spouse made the main purpose of the transaction unclear. However, the Court held that it did not need to make a

determination with regards to transaction (1) because it determined that transaction (2) was an avoidance transaction and only one transaction needs to be an avoidance transaction for the second GAAR requirement to be met.

The Court held that the Taxpayer did not demonstrate that transaction (2) was reasonably undertaken or arranged primarily for a non-tax purpose. Instead, the Court held that the Spouse acted only as an intermediary and received no benefit from transaction (2). The proceeds the Spouse received from the sale of the Sold Shares to the third-party investors was used fully to repay the Promissory Note. If not for the application of subsection 47(1), the election under subsection 73(1) and the attribution to the Taxpayer pursuant to section 74.2, the Taxpayer and his Spouse would have received no benefit from transaction (2).

Abusive Tax Avoidance

The Court held that the Minister established that there was abusive tax avoidance on the basis of *Gervais c. Canada*, 2018 DTC 5006 (FCA) ("*Gervais*").

The facts in *Gervais* were essentially the same as in the Taxpayer's case; virtually the same series of transactions was undertaken that resulted in essentially the same tax consequences (i.e., the splitting of a capital gain between the taxpayer and his spouse due to the averaging rule in subsection 47(1) of the ITA). The only differences between *Gervais* and the Taxpayer's case were that, in *Gervais*, there was a reorganization of capital at the beginning of the series of transactions; only the spouse benefitted from the capital gains deduction in subsection 110.6(2.1); the proportion of shares donated versus the shares sold was different; and the series of transactions was carried out over several days rather than just one. The Court held that these differences were altogether minor and did not distinguish the Taxpayer's case from *Gervais*. Accordingly, the Court held that the reasoning in *Gervais* applied to the Taxpayer's case and because the Court in *Gervais* held that there was abusive tax avoidance, the same conclusion applied to the Taxpayer's case as well.

CONCLUSION

The Taxpayer undertook a series of transactions virtually identical to the series of transactions in *Gervais* which resulted in essentially the same tax consequences as *Gervais*, which included the application of the GAAR to attribute the taxable capital gain realized by his Spouse to the Taxpayer.

— Francis Chang

FORTIUS FOUNDATION V CANADA (NATIONAL REVENUE), 2022 DTC 5107 (FEDERAL COURT OF APPEAL) – INTERIM RELIEF DENIED TO CHARITY FACING CHARITABLE STATUS REVOCATION; REVOKING REGISTERED CHARITY STATUS DOES NOT CAUSE IRREPARABLE HARM, "ABSENT EVIDENCE OF UNIQUE OR SPECIFIC HARM OR DAMAGE"

BACKGROUND

The Canada Revenue Agency (the "CRA") conducted an audit of Fortius Foundation's ("Fortius") operations covering a two-year period from October 1, 2014, to September 30, 2016. The CRA determined that Fortius failed to comply with the requirements for continued registration as a charity under the *Income Tax Act* (the "ITA") on the following bases:

a) Fortius was not constituted and operated exclusively for charitable purposes;

b) Fortius failed to devote resources to charitable activities carried on by Fortius itself;

c) Fortius failed to meet the disbursement quota;

d) Fortius failed to maintain adequate books and records;

e) Fortius failed to issue donation receipts in accordance with the ITA and/or the *Income Tax Regulations* (the "Regulations"); and

f) Fortius failed to file an information return as and when required by the ITA and/or the Regulations.

On July 21, 2022, the Director General of the Charities Directorate gave notice to Fortius under subsection 168(1) of the ITA. The notice informed Fortius that its registration would be immediately revoked 30 days after the date of the notice. The Minister of National Revenue (the "Minister") advised Fortius of her intention to publish a copy of the notice in the *Canada Gazette* (the "Gazette") under paragraph 168(2)(*b*) of the ITA; revocation is effective as of the date the notice is published.

On August 18, 2022, Fortius commenced two proceedings to prevent the Minister from implementing the decision to revoke its charitable status. Fortius filed an application for an order under paragraph 168(2)(*b*) of the ITA precluding the Minister from publishing the notice until Fortius had the opportunity to pursue the objection process available under subsection 168(4) of the ITA, as well as any possible appeal of the Minister's decision to the Court under subsection 172(3) of the ITA.

Fortius also filed a motion for interim relief under Rules 372 and 373 of the *Federal Courts Rules*, seeking to enjoin the Minister from publishing the notice of its revocation in the Gazette until the Application was decided. The Minister agreed not to publish the revocation notice in the Gazette until 30 days after the Court issued its decision on the motion.

ISSUE AND DECISION

The issue before the Federal Court of Appeal was whether Fortius established that it would be just and equitable for the Court to stay the Minister's publication of the notice until the application was determined based on the tripartite test laid down in *Google Inc. v Equustek Solutions Inc.*, 2017 SCC 34 and *RJR-MacDonald Inc. v Canada (Attorney General)* (1994), 164 N.R. 1.

The Google/RJR-MacDonald test applies to applications to restrain the publication of revocation notices and motions for interim stays. Therefore, Fortius must satisfy the same three requirements for both the application and the motion:

1. There is a serious issue to be tried;
2. The publication of the notice will cause Fortius irreparable harm; and
3. The balance of convenience favours Fortius and not the Minister.

1. Serious Issue

The Minister conceded to the first requirement. The threshold to establish a serious issue is a low one and is satisfied by the moving party demonstrating only that the objection is "neither vexatious nor frivolous" based on a "preliminary assessment of the merits of the case".

2. Irreparable Harm

Irreparable harm cannot be inferred. The applicant must establish, on a balance of probabilities, that it will suffer harm of a type or nature that "cannot be quantified in monetary terms or cannot otherwise be cured". The Court may consider the interests of those who are dependent on the charity (*Glooscap Heritage Society v Canada (National Revenue)*, 2013 DTC 5029 (FCA) at 34).

Fortius raised three arguments. First, Fortius argued that if the interim stay was not granted, the application became moot, and that this result in and of itself was evidence of irreparable harm. The Court disagreed and accepted the Minister's argument that the only difference between the relief sought in the motion and the application is the "end date" of the prohibition to publish. There is no substantive difference.

The Court also stated that the legal test and criteria governing the motion and the application are identical and so was the evidence relied upon by Fortius. Therefore, the Court could not find that Fortius suffered any prejudice by being deprived of the opportunity to adduce evidence in support of its argument in the application. Further, the Court clarified that publication of the notice of revocation does not foreclose Fortius's statutory appeal rights. Fortis has the right to file an objection with the Minister and if the Minister confirms the decision to revoke, Fortius can file an appeal in the Federal Court of Appeal pursuant to subsection 172(3) of the ITA.

Second, Fortius argued that the publication would result in a loss of the statutory benefits that it enjoyed as a registered charity, and the loss of such benefits was itself evidence of irreparable harm. The Court disagreed.

Justice Rennie confirmed that the Court rejected general assertions of irreparable harm in the context of charitable status revocation on the basis that, in every case, a charity could say that its work would be seriously impaired by the Minister's revocation and any consequential reduction in donations.

The Court stated that absent evidence of unique or specific harm or damage, irreparable harm does not encompass the ordinary consequences that flow from an entity losing its registered charity status. To accept the argument that a reduction in donations, for example, invariably satisfies the second requirement of the test in all circumstances would effectively eliminate that element of the test in relation to each and every application made pursuant to paragraph 168(2)(*b*) of the ITA. The normal, foreseeable consequences associated with the exercise of the statutory powers granted by the Minister do not, in and of themselves, give rise to irreparable harm.

Third, Fortius argued that revocation of its charity status would result in an inability to raise money from donors to fund its legal expenses and to pay a revocation tax, depriving it of financial resources it needs to exercise its statutory rights of objection and appeal. The Court rejected this argument given the evidence that established the insignificance of receipted donations. Receipted donations comprised between 0.5% and 1.5% of the overall declared revenue received by Fortius between 2015 and 2021.

3. Balance of Convenience

The Court also determined that Fortius failed to satisfy the third requirement, in that the balance of convenience weighed in favour of the Minister. The Court emphasized that the public has a legitimate interest in the exercise of the CRA's statutory mandate to enforce the obligations applicable to registered charities under the ITA. The CRA's enforcement of these obligations protects both the public's confidence in registered charities as well as potential donors.

The Court added that public interest considerations take on greater resonance where the charity has enjoyed sizeable monetary benefits due to its registration as a charity. The Minister argued that the amounts in issue are sizeable, as Fortius sustained benefits of $2,379,884 and $2,656,657 during the two fiscal periods included in the CRA's audit of its operations. The Court agreed.

CONCLUSION

In summary, the Federal Court of Appeal dismissed the motion for interim relief. The evidence before the Court fell short of establishing irreparable harm warranting interim relief. Additionally, Fortius also failed to meet the burden for balance of convenience.

The reasons for the Minister's decision to revoke Fortius' charitable registration are open to review on appeal pursuant to subsection 172(3) of the ITA.

One of the takeaways from this case is that "irreparable harm" requires clear and compelling evidence. This is a highly fact specific exercise and each case must be considered in the light of the evidence and context. The Court requires specific, direct evidence demonstrating the damage to the charity's operations that would be caused by the Minister's publication of the notice. Evidence showing that a reduction in donations would entirely frustrate a charity's ability to fulfill specific obligations, for example, could presumably meet this threshold.

In *Chedar Chabad v. Canada (National Revenue)*, 2014 DTC 5048 (FCA), irreparable harm was established where the evidence showed that the majority of students attending the applicant's school relied on tuition subsidies, generated from the charity's fundraising efforts, to afford their schooling. Therefore, the Court may consider the interests of those who are dependent on the charity in the irreparable harm assessment.

— Raman Khera

RECENT CASES

Application to CRA for Relief Not Subject to Res Judicata

Applicant appealed from a Prothonotary's order granting Respondent's motion to strike on grounds of res judicata and abuse of rights. Underlying the appeal was CRA's denial of Applicant's request for relief under ITA s. 220(3.1) in respect of the 2000-2002 taxation years. He filed those returns in 2003 under the Voluntary Disclosure Program ("VDP"). CRA reassessed the 2001 return and waived late filing penalties. In 2005 CRA asked for clarification of Applicant's claimed rental expenses and reassessed after receiving no response. Applicant did not object. In 2010 he submitted a request for relief with respect to the 2000-2002 returns under s. 152(4.2). He submitted no documents, and CRA denied the request in 2011; the performance was repeated in 2014. He sought judicial review of the 2014 denial and was dismissed for not supplying requested documents or the nature and context of his expenses. In 2017 he again requested relief under s. 220(3.1). The decision underlying Respondent's motion to strike is CRA's 2019 second denial of this request. CRA stated that Applicant had failed to submit necessary supporting documents. Applicant sought judicial relief, arguing that CRA's decision was unreasonable. CRA argued that the s. 220(3.1) request for relief was the same as the s. 152(4.2) request, and was therefore res judicata.

The Federal Court allowed the appeal. It framed four issues to be decided. First, Applicant argued that res judicata could not apply in an application for judicial review; the Court rejected this argument citing Federal Court of Appeal precedent. Second, Applicant disputed the Court's ruling that his affidavit was not admissible on a motion to strike. The Court noted that this was the general rule, but canvassed the exceptions and held that the affidavit was inadmissible apart from certain correspondence. Third, the Court held that it was not "plain and obvious," the demanding criterion for a motion to strike, that the 2019 Application had no reasonable chance of success. The conditions for a judgment to satisfy res judicata were met here: the Court had jurisdiction, the judgment was final, and it was rendered in a contentious manner. As for the conditions on the action, the same parties were involved; however, the objects of the requests for relief differed. The s. 152(4.2) request was an objection to or an appeal from an assessment, but the s. 220(3.1) request was for, and limited to, relief from penalties and interest. The Court found this to be a palpable and overriding error, and allowed the appeal.

Ford v. CRA

2022 DTC 5103

Self-Funded Vehicle Was Not Tax Shelter

The Appellant claimed deductions of $30,000 per year for investments in a tax shelter he established himself. Upon reassessment of his 2014–2016 returns, the CRA disallowed the deductions, as well as business expenses of roughly $20,000 per year. On appeal, the Appellant admitted that he had set up the "shelter" in order to shield his mandatory RRIF deductions. The "shelter" was a corporation purportedly established to finance, produce, and exhibit motion pictures, in service of a long-standing dream of the Appellant.

The Tax Court dismissed the appeal. The Court followed *Paletta v. The Queen*, which distilled the exceptionally complex legislative definition of a tax shelter into four conditions: there must be (i) a property about which statements are made (ii) by a promoter (iii) under which it would be reasonable to consider an amount to be deductible that (iv) exceeded the investor's cost in the property. It concluded that conditions (i) and (iii) were not met here. As to (i), where the promoter and the purchaser are the same person, it is "conceptually" difficult to see how they could make representations to themselves. In any case, the documents the Appellant offered, specifically the "contract" between the corporation and himself, did not make any statements or representations as to the deductibility of any losses, tax credits, or other deductions that would be equal to or greater than the net cost of the investment within four years of purchasing the investment, failing (i). As to (iv), the corporation had done nothing to make movies; its only receipts were the $30,000 annual payments and its only expenditures were $400 a year it paid to the Appellant. In the corporation's properly filed tax shelter forms, it reported losses for each tax year when in fact it was increasing by at least $30,000 per year. It was apparent that the Appellant, as he admitted, had created the corporation to generate a tax deduction on his T1 return without incurring any risk. Thus, the cost of acquiring the corporation was $30,000 per year and the return was zero, failing condition (iv). The Court then turned to the Appellant's claimed business expenses. It first found that the Appellant conducted his movie-making activities more like a hobby than a business. It rejected the Appellant's claims that he worked 24/7, including in his dreams, and that 100% of his house was a workspace that generated a deduction. Finally, the CRA could reassess the 2014 records under subsection 152(4) of the *Income Tax Act*, given that the Appellant's misrepresentations were significant and were attributable to his wilful default.

Liang v. The Queen

2022 DTC 1075

Third Party Disinterested Debtor Had Discharged Debt Before Issuance of RTP

If the CRA determines that a tax debtor is a creditor with respect to a third party, it can issue a Requirement to Pay ("RTP") to that third party (a "disinterested debtor"), requiring the debtor to pay the amount owed to the Crown. Here, the CRA alleged that the Appellant, Elegant, owed the tax debtor Paragon Developments Inc. $700,000 on this basis and issued an RTP for that amount on June 1, 2017. Elegant and Paragon had entered into a "joint venture agreement" to develop land in 2007. The back and forth between the parties resulted in a $700,000 loan to correct an "anomalous" surplus. The Paragon director involved had falsely claimed to be its only director and sole authority, and when he was exposed multiple lawsuits followed, resulting in the settlement agreement.

The Tax Court allowed the appeal. It framed the question as whether Paragon could have enforced payment from Elegant on the date of the RTP, June 1, 2017. Elegant maintained that the debt was extinguished before the RTP was issued, either by repayment or under a "settlement agreement" dated October 31, 2016, rendering the RTP nugatory. The Court noted Paragon had no financial statements — cash flow, profit and loss, and the like. Thus, the Court had to construct a conjectural balance sheet from all the data before it. It noted that the 2007 joint venture agreement called

for a 50/50 distribution of assets between Elegant and Paragon, and given the history of uneven transfers disclosed by the balance sheet this worked to extinguish the debt. Furthermore, the $700,000 was not mentioned in the settlement agreement, which purported to settle all debts among the parties. The Court concluded that the debt did not exist, and that therefore the appeal succeeded.

Elegant Development Inc. v. The Queen

2022 DTC 1072

TAX NOTES

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Wolters Kluwer Canada Limited
300-90 Sheppard Avenue East
Toronto ON M2N 6X1
1 800 268 4522 tel
1 800 461 4131 fax
www.wolterskluwer.ca

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