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A WHOLE NEW WORLD — TIME FOR YOUR CLIENTS TO REVISIT THEIR WILL (AND TRUST) PLANNING

— Michael Goldberg, tax partner, Minden Gross LLP, MERITAS law firms worldwide and founder of "Tax Talk with Michael Goldberg", a quarterly conference call about current, relevant and real life tax situations for professional advisors who serve high net worth clients.

In 2013 the Department of Finance proposed to eliminate most tax benefits that have traditionally been available to certain trusts formed on the death of an individual (in this article referred to as "Testamentary Trusts") so that Testamentary Trusts, which include an individual's estate as well as trusts created under the terms of an individual's will for his or her spouse and/or other persons, would be taxed in a manner similar to trusts that are not Testamentary Trusts.

Notwithstanding much critical commentary, the 2014 Budget announced plans to implement the proposals. By December 16, 2014, the entire legislative process had run its course and Bill C-43, *Economic Action Plan 2014 Act, No. 2*, was enacted as the law of the land, though its application in connection with Testamentary Trusts will be delayed until 2016.

As bad as the original proposals were thought to be, the final legislation not only implemented the proposals but went far beyond their original scope in ways that will broadly and generally negatively impact traditional will planning as well as planning involving so-called "life time trusts" (these are self-benefit trusts, *alter ego* trusts, and joint partner trusts, but are not ordinary discretionary family trusts typically set up for an estate freeze or other planning).

Although there is no way to adequately address the legislative changes in this short article, some of the more critical changes that will impact Testamentary Trusts are highlighted below.

> (1) The income of a Testamentary Trust that is a spousal trust in the year of death of the beneficiary spouse will be deemed to be the income of the deceased beneficiary spouse and not the spousal trust. This rule may result in significant inequitable consequences in situations where the deceased beneficiary spouse's heirs (who effectively end up paying the tax) are different from the residuary beneficiaries of the spousal trust (who will receive the assets of the spousal trust).

(2) Access to many traditional tax saving testamentary tax-planning practices will only be available to a "graduated rate estate" ("GRE"). Only estates of deceased persons that meet certain criteria can qualify as GREs, and GREs can only last for up to the first 36 months of a qualifying estate. Other Testamentary Trusts, such as spousal, family, or insurance trusts formed under a decedent's will, will not qualify as GREs, though certain trusts formed under a will for the benefit of disabled persons will, with limitations, be able to qualify as GREs.

(3) The ability of a Testamentary Trust to enjoy the annual savings that come from being taxed at graduated tax rates (about $23,000 on the first $135,000 of income earned in Ontario in 2014) will only be available to GREs which, as noted above, can only exist for the first 36 months of a qualifying estate.

Another significant problem with Bill C-43 is that it was enacted without provisions that would "grandfather" situations where wills can no longer be changed, for example, because the maker of the will is dead or incapacitated. Consequently, in these situations it may not be possible to take any steps to address the legislative changes, which could give rise to adverse tax results and, in some situations, potentially lead to unnecessary litigation.

As a result of these legislative changes, all advisers should consider contacting their clients to encourage them to review their wills in 2015, before Bill C-43 comes into effect for these purposes on January 1, 2016. Also, since the changes enacted in Bill C-43 will impact lifetime trust planning, advisers who employ such trusts should also encourage their clients to review whether those trusts will continue to meet their client's planning needs.

DECEASED'S EX SEEKS LIFE INSURANCE PROCEEDS

In *Milne Estate v. Milne*, 2014 BCSC 2112, the deceased had agreed to a Consent Order (the "Order"), the terms of which obligated him to maintain a life insurance policy (the "Policy") with his wife (Sheerie) as the beneficiary, for as long as he was required to pay child and or spousal support. Less than a year later, he changed the beneficiary of the Policy from Sheerie to his new partner.

Arguing that the terms of the Order were unambiguous, Sheerie took the position that she was entitled to the face value of the Policy ($500,000). There was, in fact, no dispute that at the time of his death, the deceased was required to maintain Sheerie as the beneficiary of the Policy, since he was obligated to pay ongoing child support pursuant to the Order. Had he not breached the Order by removing Sheerie as the beneficiary, the death benefit of $500,000 would have passed to Sheerie outside the estate of the deceased. Given this breach, Sheerie advanced the two following alternative positions.

(1) The deceased's obligation pursuant to the Order to maintain Sheerie as the beneficiary under the Policy created a constructive trust in her favour.

(2) The Order was a contract made in the course of family law proceedings and therefore the breach of the Order is a breach of contract that entitled Sheerie to damages from the estate equal to the proceeds of the Policy.

In dealing with the issue of a constructive trust, the Court cited and followed the Supreme Court of Canada decision in *Soulos v. Korkontzilas*, [1997] 2 S.C.R. 217. In *Soulos*, the Supreme Court held that under the broad umbrella of good conscience, constructive trusts are recognized as a remedy for wrongful acts like fraud and breach of a duty of loyalty, as well as to remedy unjust enrichment. However, the Court was careful to avoid inviting judges to impose such a trust whenever and wherever they believe justice requires it. Generally, the following four conditions should be satisfied before imposing a good conscience constructive trust.

(1) The defendant must have been under an equitable obligation, that is, an obligation of the type the courts of equity have enforced, in relation to the activities giving rise to the assets in his hands.

(2) The assets in the hands of the defendant must be shown to have resulted from deemed or actual agency activities of the defendant in breach of his equitable obligation to the plaintiff.

(3) The plaintiff must show a legitimate reason for seeking a proprietary remedy, either personal or related to the need to ensure that others like the defendant remain faithful to their duties.

(4) There must be no factors which would render imposition of a constructive trust unjust in all the circumstances of the case (e.g., the interests of intervening creditors must be protected).

The Court in this case found that these conditions were not met because, while it is possible that a fiduciary relation might exist between separated or divorced spouses, once formalized in a separation agreement, the duties and obligations are primarily contractual and equity will not apply. Accordingly a constructive trust was not appropriate.

Regarding the breach of contract argument, the Court agreed that the failure to maintain the Policy in the name of Sheerie resulted in a breach of the Order for which the estate was liable for damages. The issue was whether the estate was liable for the full amount payable on death under the Policy, or only such amounts as the deceased was liable for under the Order, being primarily support obligations? The answer depended on whether the parties objectively intended for the deceased's obligation to maintain the Policy for the benefit of Sheerie to be security for his support obligations or for it to be independent of the latter.

After reviewing the terms of the Order and the surrounding circumstances, the Court concluded that the parties clearly intended the deceased's insurance obligation to be independent and not just as security for his outstanding support obligation. Accordingly, Sheerie was awarded damages in the amount equal to the face value of the policy — $500,000, payable from the estate of the deceased.

IT'S NOT JUST ABOUT MONEY — ESTATE PLAN MEETS SPOUSAL CHALLENGE

The recent case of *Lafleur Estate (Re)*, 2014 ABQB 698, serves as reminder that dependants' relief applications are not limited to situations involving destitute surviving spouses or needy children.

The Applicant ("Yuliya") brought an application under Alberta's *Dependants Relief Act*, claiming that her deceased husband ("Bradley") failed to make adequate provision for her proper maintenance and support as his surviving spouse and dependant. The Respondent was Bradley's father, the executor of his will, and the Trustee of three Trusts established by Bradley's will for the benefit of Yuliya (the "Spousal Trust") and each their two children (the "ML Trust" and the "JL Trust", respectively). The principal asset held by the trusts was shares in Bradley's operating company (LCS).

According to the Respondent, Bradley left his spouse over $2,000,000, more than half of which she had converted to her own use since his death. Yuliya sought to have property that was put in trust for her and the two children, the LCS Class E Preferred shares, transferred directly to her. She said she needed this property to adequately provide for her children. If successful in her application, she would receive the shares in LCS and the residue of the estate unencumbered by any trusts.

The Court surmised that "the real issue" was that, although Bradley's estate plan left Yuliya and the two children the beneficial owners of the majority of the shares of LCS, it left her father-in-law, the Respondent, with the majority of the voting shares: "He runs the LCS business and he distributes funds from LCS by monthly dividend payments to the Family Trust and the annual payments from LCS profits to the ML, JL, and Spousal Trusts. Yuliya would prefer to have absolute control over this business and its profits." The question was wheter this was something that could be achieved under the *Dependants Relief Act*.

Counsel for Yuliya argued that in *Tataryn v Tataryn* [1994] 2 SCR 807, 116 DLR (4th) 193, the Supreme Court of Canada considered that the origin of dependants' relief was in the women's rights movement and that the needs-based analysis of "adequate provision" was rejected in favour of an analysis based on current societal norms. Counsel further argued that, like the wife in the Tataryn case, the testamentary trusts in the present case failed to recognize Yuliya's deserved and desirable independence; they left both her and the children vulnerable and at the mercy of the Trustee, a situation that was undignified and paternalistic. She was confined to such sums as he sees fit for the adequate provision for either her or the children. The children are the only other claimants, and their needs become her needs. Yuliya, it was argued, was an exemplary mother.

"Exemplary" or not, the Court did not accept Yuliya's argument that, since she was the caregiver and guardian of her children, her interests and those of the children were identical. Bradley's intention, as derived from his will, was to ensure that a portion of his estate would be preserved for the children of their marriage and would not be vulnerable to claims of a third party with whom she might become legally involved, such as a new partner. (Bradley was 33 years old when he died and Yuliya was a similar age – so, it was possible that she might remarry.) The Court noted Yuliya might choose to share all property that she owns with a new partner, or she may be required to do so by the operation of matrimonial law, and her interests therefor would diverge from those of her children. The Court accepted that Bradley established the Trusts through the will to secure income adequate to the on-going needs of his wife and children, and the future educational needs of his children, against any incursion upon those assets by a third party that might be able to lay claim to them by dint of a relationship with Yuliya.

The Court concluded that in the main, Yuliya had not demonstrated that Bradley failed to make adequate provision for the proper maintenance and support of her so as to warrant additional provision. However, the broad interpretation of the term "adequate provision" in the *Dependants Relief Act*, as commended by *Tataryn*, involved contextual judgment based on contemporary community standards. This approach suggested that Yuliya should be able to make a life for herself, freely and independently. Therefore, the Court directed that any property held in the Spousal Trust be in the absolute control of Yuliya, except for the LCS Preferred Class E shares. This is to say, the Court struck a balance between Bradley's legitimate testamentary intentions and Yuliya's equally legitimate desire get on with her life freely and independently.

PECORE APPLIED

In the recent case of *Midtdal v Pohl*, 2014 ABQB 646, the issue was whether or not a certain transfer gave rise to a resulting trust — nothing less than the family farm was at stake.

Gordon and Vivian were married in May 1974, two years after the death of Vivian's first husband. Vivian had five children by her first marriage, the oldest being Melva (the Defendant). At the time of his marriage to Vivian, Gordon owned six quarter sections of land he had purchased from his father. He eventually transferred title to the lands to himself and Vivian as joint tenants. Gordon and Vivian later built a house on one of these sections (the "Home Quarter"). On June 4, 2004, Gordon and Vivian executed transfers of land adding Melva as a joint tenant to the title to the Home Quarter.

The issue was whether, as Gordon maintained, a resulting trust arose from Gordon and Vivian's transfer of a joint interest in the Home Quarter to Melva such that the beneficial ownership of the Home Quarter remained with Gordon and Vivian, or, as Melva maintained, whether the transfer of a joint interest was an outright gift to Melva.

The evidence indicated that Gordon and Vivian had a close relationship with Melva and her husband Dennis. Of the children, only Melva and Dennis were actively engaged in farming.

On June 4, 2007, Gordon and Vivian executed transfers of land creating a joint interest for Melva with them in the Home Quarter. After the transfer, Gordon continued to reside on the land, farm it, pay property taxes and home-related expenses, and receive oil lease revenues. He never reported a disposition of the Home Quarter on his tax return.

Counsel for Gordon suggested that the transfer was simply part of an "estate planning" decision. It was a choice made by Vivian and Gordon to avoid using their wills in relation to the disposition of their land but rather the vehicle of survivorship under a joint tenancy. It was argued that this estate planning decision was not sufficient to discharge the presumption of a resulting trust.

Counsel for Melva submitted that Gordon and Vivian's intentions had to be considered as of the time of the transfer of the joint interest in June 2004 to Melva. At that time, the Supreme Court of Canada's decision in *Pecore v. Pecore*, 2007 SCC 17, had not yet been decided and, in cases such as this, the law provided that the presumption of advancement applied unless it could be established that beneficial interest remained with the transferor. This was the reason the lawyer retained in relation to the transfer, appeared to have discussed the prospect of a letter of agreement preserving the beneficial title in Gordon and Vivian, as evidenced by his handwritten note. However, if advice regarding retaining beneficial title had ever been given orraised, there was no evidence that Gordon and Vivian ever acted on it.

It being determined that the transfer of title to the Home Quarter section was gratuitous, the Court noted that Melva, as an independent adult child, had the onus of proving that the intention of Gordon and Vivian was to gift a joint interest in the Home Quarter to her. Per *Pecore*, the close relationship between Gordon and Vivian and Melva and Denis could be considered, but it was just one factor among others.

Another critical aspect of *Pecore* noted by the Court was Rothstein J's discussion of a situation where the transferor placed assets into a joint account with the transferee with the intention of retaining exclusive control of the account until his or her death, at which time the transferee would take the balance through survivorship. He noted that one of the difficulties in these circumstances is that the beneficial interest of the transferee appears to arise only on the death of the transferor, leading some judges to conclude that the gift of survivorship is testamentary in nature and must fail as a result of not being in proper testamentary form. He went on to find, at para 48, that:

> . . . the rights of survivorship, both legal and equitable, vest when the joint account is opened and the gift of those rights is therefore inter vivos in nature. This has also been the conclusion of the weight of judicial opinion in recent times.

Considering all the evidence, the Court concluded that the situation in this case was analogous to that in *Pecore*. Melva was judged to have rebutted the presumption of a resulting trust. Gordon and Vivian's transfer of a joint interest in the Home Quarter to Melva constituted an irrevocable *inter vivos* gift and the right of survivorship vested when the gift was made.

It remains to note that, whenever a gratuitous transfer of joint ownership is on the table, the intentions of the transferor(s) should be carefully documented. There is every chance that this will serve to avoid estate litigation.

MINISTER APPLIES GAAR TO SUCCESSFULLY CHALLENGE STRUCTURED LIQUIDATION

***Descarries et al. v. The Queen*, 2014 DTC 1081 (Tax Court of Canada — Informal Procedure)**

The taxpayers in this case were siblings who inherited shares in a Canadian corporation, Oka Inc. ("Oka"), on the death of their father in 1982 and who appear to have wanted to realize the value of their interest in the company in cash during the mid-2000s. At the time, the value of Oka on a liquidation basis was $617,466 and, because the paid-up capital ("PUC") of the siblings' Oka shares (representing all the issued and outstanding shares in the company's capital) was only $25,100, a straight redemption of the siblings' shares for consideration equal to $617,466 would have triggered a subsection 84(3) deemed dividend of $592,362. Such a redemption would also have triggered an aggregate capital loss of $336,366 for the siblings, but it is not clear whether the siblings had, or were anticipating realizing, any capital gains against which the capital loss could be applied.

On the advice of a tax adviser, the siblings implemented a plan during 2005 that was designed to provide a better overall tax result than a straight redemption of the Oka shares or other direct distribution of the company's assets to its shareholders. The sequence of transactions saw them realize the value of their original Oka shares as a capital gain on the disposition of those shares in consideration for shares of Oka in two newly created classes, but also contemplated that they would suffer an offsetting capital loss on the redemption of shares in the capital of newly created 9149-7321 Quebec Inc. ("Newco") that the siblings received in 2005 in exchange for the new Oka shares. The series of transactions also caused the siblings to collectively realize a deemed dividend of $265,505 in 2005.

As discussed in greater detail below, the tax plan revolved around the application of paragraph 84.1(2)(*a*.1) of the *Income Tax Act* (the "Act") on the exchange of Oka shares for Newco shares. The share exchange involved two classes of Newco shares and the tax plan relied on paragraph 84.1(2)(*a*.1) applying to limit the amount of the PUC attributable to one class of the Newco shares (representing 44% of the Newco shares) such that, on the redemption of that class of Newco shares, approximately 96% of the redemption proceeds would be a deemed dividend and only the balance would be proceeds from the disposition of the shares on the redemption after taking into account the deemed dividend.

What follows is an overview of the background and sequence of transactions that were undertaken by the relevant parties pursuant to the tax plan. Oka was established in 1946. Prior to implementing the tax plan, the siblings held all 4,000 shares in the capital of Oka, acquiring 3,178 shares on their father's death in 1982 and the remaining 822 shares either from a third party or treasury. As of December 2004, the siblings' 4,000 Oka shares (Class A common shares) had an aggregate fair market value of $617,466, adjusted cost base ("ACB") of $361,658, and PUC of $25,100.

On March 1, 2005, the taxpayers exchanged their 4,000 Class A common shares for 269,618 Class B and 347,848 Class C preferred shares. Typically, the rollover in section 86 would have applied to this type of exchange, but the parties filed an election to have subsection 85(1) apply with an elected amount equal to the $617,466 fair market value of the 4,000 Class A common shares. The exchange resulted in the taxpayers having a capital gain of $255,808 reflecting the difference between the deemed proceeds of disposition for the Class A common shares equal to the elected amount ($617,466) and the $361,658 ACB of those shares. The Class B preferred shares received on the exchange had an ACB to the taxpayers of $269,618 and PUC of $10,960, and the Class C preferred shares received on the exchange had an ACB to the taxpayer of $347,848 and PUC of $14,140.

On March 15, 2005, the taxpayers then transferred all of their Oka shares to Newco in exchange for Class A common shares and Class B preferred shares in Newco. The transfers to Newco were staged such that, first, 117,728 (approximately 44%) Oka Class B preferred shares and 151,889 (approximately 56%) Oka Class B preferred shares were transferred in consideration for 269,618 Newco Class B preferred shares and, second, all remaining Oka Class B and Class C preferred shares were transferred in consideration for 347,848 Newco Class A common shares. Since the taxpayers' ACB for their Oka Class B and Class C preferred shares was equal to the value of the Newco shares received, there was no gain or loss on the exchange. The only aspect of the step that was relevant to the intended tax result was the adjustment that would be have to be made to the PUC of the Newco shares received on the transfer, as discussed below.

The taxpayers' ACB for their Newco Class A common shares was equal to the $347,848 ACB (and fair market value) of the Oka shares that were exchanged for the Newco Class A common shares, and the ACB for the Newco Class B preferred shares was equal to the $269,618 ACB (and fair market value) of the Oka shares that were exchanged for the Newco Class B preferred shares.

As the siblings' transfer of Oka shares to Newco was a non-arm's length sale of shares contemplated by section 84.1 of the Act, the Act required the PUC attributable to the Newco shares issued on the transfer to be computed by reference to the restrictions in that section. Where section 84.1 applies, the general rule is that the PUC of the newly issued shares is limited to the greater of the PUC and the ACB of the shares that were transferred for the newly issued shares. In this case, the general rule would have resulted in the PUC attributable to each class of Newco shares being equal to the siblings' ACB of the Oka Class B and Class C preferred shares that were transferred in consideration for Newco shares of the particular class. However, where the transferred shares can be traced to shares that were acquired from someone with whom the transferor did not deal at arm's length and who owned those original shares on December 31, 1971 (i.e., V-Day), paragraph 84.1(2)(*a*.1) requires the taxpayer's ACB (solely for the purposes of computing the PUC attributable of the newly issued shares) for the transferred shares to be reduced by the amount of the unrealized, accrued gain on the original shares as at December 31, 1971, less certain adjustments.

The adjustment under paragraph 84.1(2)(*a*.1) applied in the case of these taxpayers because they had acquired 3,178 of their 4,000 Oka Class A common shares on the death of their father and he owned those shares on December 31, 1971. Based on the relevant tax history surrounding the ownership of the 3,178 Oka shares, the corresponding ACB reduction required by paragraph 84.1(2)(*a*.1) was $269,618, which the tax advisers purported to fully apply to the computation of the PUC attributable to the 269,618 Newco Class B preferred shares based on the ordering of the March 15, 2005 share exchanges. The application of paragraph 84.1(2)(*a*.1) resulted in the taxpayers' ACB in the Oka Class B and Class C preferred shares that were exchanged for the Newco Class B preferred shares being nil for the purposes of the general rule in section 84.1 and, since the PUC attributable to the transferred shares was greater than their ACB after taking into account paragraph 84.1(2)(*a*.1), the PUC of the Newco Class B preferred shares was equal to the $10,960 PUC attributable to the Oka shares transferred to Newco on that transfer.

There was no paragraph 84.1(2)(*a*.1) adjustment required in connection with the issuance of the Newco Class A common shares and, consequently, the PUC of those shares was equal to the $347,848 ACB of the Oka shares that Newco received on the exchange.

On March 29, 2005, Newco redeemed its 347,848 Class A common shares for $347,848. Since the redemption price was equal to the PUC and the taxpayers' ACB for their Class A shares, there was no deemed divided or capital gain as a consequence of the redemption. At the same time, Newco also redeemed 196,506 (of the 269,618) Class B preferred shares for $196,506, which resulted in a $188,518 deemed dividend under subsection 84(3). Since the deemed dividend caused the taxpayers' proceeds of disposition from the redemption of the Class B preferred shares to be reduced to $7,988, the redemption also triggered a $188,518 capital loss given the taxpayer's $196,506 ACB for the Class B preferred shares. The capital loss partially offset the $255,808 capital gain the taxpayers realized on the March 1, 2005 exchange of Oka Class A commons shares for the Oka Class B and C preferred shares.

Finally, at the end of 2008, Newco redeemed its remaining 73,112 Class B preferred shares for $73,112, giving rise to a deemed dividend under subsection 84(3) and capital loss to the taxpayers of $70,140 and $70,140, respectively. It is not clear from the reported decision, but there are indications that the capital loss was carried back to offset the portion of the 2005 capital gain triggered by the implementation of the tax plan that was not already covered by the capital loss created on the redemption of the Newco Class B preferred shares in 2005.

The Minister reassessed the siblings to treat them as having received a deemed dividend on their Oka shares pursuant to subsection 84(2), alleging that the amounts received on the redemption of the Newco shares were in fact amounts received as a distribution to shareholders on the winding-up of Oka. The Minister relied on the general anti-avoidance rule ("GAAR") in section 245 of the Act as an alternative basis for the reassessment.

The Tax Court (per Hogan J) began its analysis by setting out the requirements for subsection 84(2) to apply. The Minister argued that the time of the "distribution" for the purposes of subsection 84(2) was the time when Newco redeemed its shares. The Tax Court cited the decisions in *Merritt* (2 DTC 561), *MacDonald* (2013 DTC 5091), and *McNichol* (97 DTC 111) as standing for the proposition that in order for there to be a "distribution" within the meaning of subsection 84(2), there must a gain for the shareholders and a loss for the corporation. The Tax Court then went on to note that at the alleged time of the distribution, Oka was still a creditor of Newco, such that its "overall total assets remained unchanged" (paragraph 27). Oka's assets were reduced only after Newco's debt was extinguished through a merger that took place on December 15, 2006. Accordingly, the Tax Court found that there was no "distribution" for the purposes of subsection 84(2) in the present case.

The Tax Court also noted that, in order for subsection 84(2) to apply, the "distribution" must occur simultaneously with a winding-up, discontinuance, or reorganization of a business. The Tax Court found that in Oka's case, the business continued to be carried on after the alleged distribution such that this requirement was not met.

On the GAAR, the taxpayers conceded the existence of an "avoidance transaction". Justice Hogan relied on the statements made by Justice Hershfield in *MacDonald* (2012 DTC 1145) and on his own statements in *Gwartz* (2013 DTC 1122) to reiterate that there is no overarching policy in the Act against surplus stripping and, on that basis, concluded that there was no abuse of subsection 84(2) in this case.

The Tax Court then went on to consider whether there was a misuse or abuse of section 84.1. Hogan J began his analysis by reiterating that he caveated his statements in *Gwartz* (2013 DTC 1122) on the policy objectives of subsection 84(2) by stating that while there is no overarching policy in the Act against surplus stripping, taxpayers must still respect the object and spirit of sections 84.1 and 212.1.

Hogan J stated that the negative tax consequences under section 84.1 notably arise where either the non-share consideration or the PUC of the shares issued by the purchaser corporation or both exceed the greater of the PUC and the ACB of the subject shares. He reiterated that, pursuant to paragraphs 84.1(2)(*a*) and (*a*.1) and subsection 84.1(2.01), adjustments are made to the computation of the ACB of the subject shares for these purposes, particularly so that any value accruing prior to V-Day or any ACB created by the use of the lifetime capital gains exemption is not included in computing the ACB of the subject shares. He cited the Department of Finance's comments in its technical notes to section 84.1 as support for his interpretation of the purpose of these provisions.

Hogan J found that using the taxable share exchange to step up the ACB of the Oka common shares allowed Newco to issue the Class A common shares with maximum ACB and PUC. Hogan J then noted that the tax adviser was cognizant of the fact that the Class B preferred shares issued by Newco would be shares having a high redemption price and low PUC because of the adjustments under paragraph 84.1(2)(*a*.1) and that, as a result, their redemption would trigger a capital loss which could be used to effectively extract a portion of Oka's surpluses tax-free. That, in the Tax Court's opinion, was an abuse of section 84.1.

The assessments were thus upheld. One may argue that from a purely technical perspective, section 84.1 was not abused in the present instance given that the tax benefit realized by the taxpayers was not a tax-free return of capital and, as such, the provision operated as intended since it reduced the PUC of the Newco Class B preferred shares. However, while the means used by the taxpayers were not exactly what is contemplated by section 84.1, the taxpayers relied on paragraph 84.1(2)(*a*.1) to create a capital loss which effectively served to achieve exactly what section 84.1 is designed to prohibit, that is, a tax-free surplus strip.

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2014 CALU CONFERENCE — ALTER EGO AND JOINT PARTNER TRUSTS

In the case of *Easingwood v. Crockroft*, 2013 BCCA 182, the British Columbia Court of Appeal held that an Attorney under a general power of attorney for the individual could settle an *alter ego* trust on behalf of the individual and transfer the individual's assets into the trust. Section 73(1) of the *Income Tax Act* (the "Act") allows an individual to transfer capital property on a tax-deferred basis under certain conditions, one of which is that the transfer is a qualifying transfer as described in s. 73(1.01) of the Act. The rollover is allowed on property transferred to the individual's spouse or common-law partner, former spouse or common-law partner, a trust for the benefit of the individual's spouse or common-law partner, or an *alter ego* or joint partner trust. Section 73(1.01) requires that the property is transferred by the individual and s. 73(1.01)(*c*) requires that the trust to which the property is transferred was created by that individual. The CRA was asked if, in light of the *Easingwood* decision, would a transfer to an *alter ego* or joint partner trust that is created by an Attorney for the benefit of the individual who granted the power of attorney be a qualifying transfer under s. 73(1.01). The CRA stated that the decision in *Easingwood* was based on unique facts, and does not hold that in general an Attorney can create a trust for the grantor of the power of attorney for the transfer of property. Whether or not such a trust meets the requirements under s. 73(1.01) involves questions of law. The CRA would expect that an Attorney planning to create an *alter ego* trust would seek confirmation from a court that such action is in accordance with the terms of the power of attorney and conforms to the will of the grantor and any other relevant agreements.

2014 CALU Conference, CRA Roundtable, Question 6, May 6, 2014; CRA File Number: 2014-0523331C6

2014 CALU CONFERENCE — PENSION SPLITTING

An individual who receives eligible pension income is entitled to claim the pension credit under s. 118(3) of the *Income Tax Act* (the "Act") and may also split the income with his or her spouse or common-law partner under s. 60.03 of the Act. "Eligible pension income" is defined in s. 118(7) of the Act, and if the individual is under age 65 the amount received must meet the conditions described in the definition of "qualified pension income" in s. 118(7). Qualified pension income includes a life annuity payment out of or under a superannuation or pension plan but other types of payments such as from a registered retirements savings plan (RRSP) annuity or out of a registered retirement income fund (RRIF) are qualified pension income only if they are received as a result of the death of the individual's spouse or common-law partner. The CRA was asked if payments out of or under a locked-in retirement Income fund (LRIF) or a life income fund (LIF) which have been funded through transfers from a registered pension plan would qualify as a life annuity out of or under a superannuation or pension plan and therefore be qualified pension income for an individual under age 65. The CRA replied that LRIFs and LIFs are not defined in the Act, and are treated as RRIFs for purposes of the Act. The CRA's position is that an RRIF is not a superannuation or pension plan and so a payment from such a plan is not a life annuity payment out of or under a superannuation or pension plan. The CRA noted that annual payments from an LRIF or an LIF may vary depending on the value of the property and the amount selected by the individual within a range. As such, the CRA does not consider the income from an LRIF or an LIF to be a life annuity.

2014 CALU Conference, CRA Roundtable, Question 4, May 6, 2014; CRA File Number: 2014-0523311C6

TAX TREATMENT OF MONETARY INHERITANCES

The Minister of National Revenue confirmed that while there is no provision in the *Income Tax Act* which states that inheritances are not taxable in Canada, the CRA's position is that recipients are not required to pay tax on most gifts and inheritances. The CRA's position on voluntary transfers of real or personal property without consideration is described in paragraph 4 of IT-334R2, "Miscellaneous Receipts".

Ministerial Correspondence, May 7, 2014; CRA File Number: 2014-0525991M4

ESTATE PLANNER

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