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2026 STEP Canada / CRA Roundtable

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Unless otherwise stated, all legislative references hereafter are to the *Income Tax Act,* R.S.C. 1985, c.1 (5th Supp.), as amended (the "Act").

QUESTION 1. Qualified Disability Trusts

To be a qualified disability trust ("QDT"), a number of conditions must be met including that the trust must be a testamentary trust that arose on and as a consequence of a particular individual's death. It is also the case that only one trust can be a QDT for a particular disabled beneficiary.

Assume divorced parents (and possibly grandparents) would like to contribute to a trust for the benefit of a disabled child and so coordinate their wills so that the first to die creates a trust for the benefit of the disabled child and the surviving parent contributes to the trust from their estate. For example, each will provides that if the deceased is the first to die, the trust is to be created and funded with assets from that deceased's estate. If the deceased is not the first to die, the will provides that assets are to be contributed to the trust created under the terms of the will of the first to die.

Assuming such planning works for legal purposes under the applicable provincial rules, and that all of the other conditions for a QDT are met, would the CRA agree that the trust created under the terms of the will of the first parent to die can continue to qualify as a QDT after it receives a contribution from the estate of the surviving parent after their death?

[1] We gratefully acknowledge the following CRA personnel who were instrumental in helping us prepare for the Roundtable: Mélanie Beaulieu, Marina Panourgias, Katie Campbell, Irina Schnitzer, Dawn Dannehl, Aleksandra Bogdan, Katie Robinson, Steve Fron, Todd Baldwin, Phil Kohnen, Stéphane Prud'homme, Urszula Chalupa, Patrick Bilodeau, Jean Lafrenière, Laurence Gagné, Olivier Bergeron, Nathalie Aubin, Yves Moreno, Angelina Argento, Kanwal Graham, Sophie Larochelle, Pierre Girard, Gillian Godson, Mei Ng, Kate Li, Serena Tan, François Fournier-Gendron, Antonio Aprile, Chris Deutsch, Justin Lawson, Richard Archambault, Joseph Armanious, and Nicolae Oanea.

CRA Response

Generally, a QDT for a taxation year is a testamentary trust that arose on and as a consequence of the death of a particular individual, that jointly elects, with one or more beneficiaries under the trust, to be a QDT for the year. In addition, several other conditions must be satisfied for a trust to qualify as a QDT.

In particular, subparagraph (a)(i) of the definition of QDT in subsection 122(3) requires that the trust is, at the end of the trust year, a testamentary trust that arose on and as a consequence of a particular individual's death. The term testamentary trust is defined in subsection 108(1). A testamentary trust means a trust or estate that arose on and as a consequence of the death of an individual, subject to the exclusions set out in paragraphs (a) to (d) of that definition. Paragraph (b) of that definition, applicable to trusts created after November 12, 1981, excludes a trust from the definition of testamentary trust if any property is contributed to it otherwise than by an individual on or after the individual's death and as a consequence thereof.

A contribution to a trust by an individual on or after the individual's death and as a consequence thereof does not disqualify a trust as a testamentary trust as defined in subsection 108(1) provided the trust otherwise so qualifies. Paragraph 248(8)(a) treats a transfer, distribution or acquisition of property under or as a consequence of the terms of the will or other testamentary instrument of a taxpayer as a transfer, distribution or acquisition of the property as a consequence of the death of the taxpayer. Therefore, when an individual bequeaths property in their will to an existing testamentary trust, the contribution does not disqualify the existing trust as a testamentary trust because the contribution is made by an individual on or after that individual's death and as a consequence thereof. As such, in the case where the existing testamentary trust was a QDT, since the contribution does not disqualify the existing trust as a testamentary trust, the contribution will not disqualify the trust from continuing to qualify as a QDT.

As an example, where Parent A is the first to die and a QDT is created under the terms of their will, a subsequent bequest to the QDT pursuant to the terms of Parent B's will would not disqualify the trust from being a testamentary trust or a QDT since the contribution will be made by an individual on or after that individual's death and as a consequence thereof. Similarly, if any other individual (e.g., grandparent) bequeaths property in their will to the child's existing QDT, the contribution would not disqualify the QDT provided the contribution is made by an individual on or after that individual's death and as a consequence thereof.

However, the question of whether a transfer is made by an individual on or after that individual's death and as a consequence thereof is a question of fact and law that can only be determined after a review of all the facts and circumstances applicable to a particular situation.

QUESTION 2. <u>Filing Requirements of a Testamentary Trust</u>

It is common for a testamentary spousal trust (or "first generation trust") to provide that, after the death of the spouse, any remaining property be held in one or more separate trusts for the benefit of the successor or remainder beneficiaries (each a "Successor Trust"). For example, when a surviving parent dies, it is not uncommon for the remaining trust property to pass to Successor Trusts for each of the children and/or more remote issue to be held by the trustees until they reach an identified age.

Where the terms of a testamentary spousal trust as described in subsection 70(6) provide the trustees with the discretion to make capital distributions to the spouse while alive, it is possible that no property may be in the trust at the time of the spouse's death so that the Successor Trusts are never funded.

1. Assuming a Successor Trust is not a trust described in any of paragraphs 150(1.2)(a) to (r), while the surviving spouse is alive, is the Successor Trust required to file a T3 *Trust Income Tax and Information Return* ("T3 Return"), including Schedule 15, *Beneficial Ownership Information of a Trust* ("Schedule 15")?

2. Assuming the following facts, can the CRA advise when the 21-year deemed disposition rule in subsection 104(4) would apply to the Successor Trust?

    - the estate of the first spouse to die is created on July 1, 2015 (i.e., the date of death);
    - the testamentary spousal trust meets the conditions in subsection 70(6), and is funded on August 1, 2015;
    - the surviving spouse passes away on April 15, 2025;
    - the Successor Trust is created on February 15, 2026; and
    - both the testamentary spousal trust and Successor Trust are resident in Canada.

3. Would the answer to Part 2 change if, instead of a testamentary spousal trust, the first generation trust is for the benefit of a non-spouse lifetime beneficiary?

CRA Response

Part 1.

A testamentary trust is defined in subsection 108(1) as a trust that arose on and as a consequence of the death of an individual, subject to certain conditions. Consequently, the estate of a deceased individual and other trusts created under the terms of the will of that individual will generally be testamentary trusts, subject to certain exceptions.

Although a testamentary trust arises on and as a consequence of the death of an individual, it must be noted that the definition of "testamentary trust" in subsection 108(1) does not contemplate the timing of the creation of such a trust.

It has been our long standing view that, generally, trusts created out of the residue of an estate arise on the death of an individual. As stated in CRA document 2016-0634871C6, ultimately it is a question of legal fact as to when such trusts are established and this will determine the filing requirements for tax returns under the Act.

That said, there may be situations where the creation date of a testamentary trust is not concurrent with the testator's date of death. For example, in the case of a Successor Trust as described in the scenario provided, wherein certain terms of a will may provide that on the death of the first generation income and capital beneficiary (in this case, the spouse or common law partner), the trustee is to divide the remaining property into equal parts to be held in a new trust for the interest of each child, such a trust may be viewed as being created at a later point in time than the testator's date of death.
Although the CRA has traditionally not attributed any tax consequences to the transition from estate administration to trust administration, the date of the creation of a testamentary trust is relevant for the application of the trust reporting rules in section 150 of the Act and in subsection 204.2(1) of the *Income Tax Regulations* (the "Regulations")

Paragraph 150(1)(c) requires a trust to file a return of income in prescribed form and that contains prescribed information for each taxation year of the trust, unless one of the exceptions provided for in paragraph 150(1.1)(b) applies to the trust for the particular taxation year. However, where a trust is resident in Canada and an express trust, or, for civil law purposes, a trust other than a trust that is established by law or by judgement, subsection 150(1.2) denies the application of the exceptions in subsection 150(1.1), unless the trust meets one of the exceptions listed in subsection 150(1.2) for the particular taxation year.

The exceptions provided for in subsection 150(1.2) also serve another purpose: where applicable, they also exempt a trust from the additional information reporting requirements imposed by subsection 204.2(1) of the Regulations.

Where none of the exceptions listed in subsection 150(1.2) apply to that trust for a particular taxation year, the trust will be obligated to file a return of income pursuant to paragraph 150(1)(c) in respect of that taxation year. Additionally, section 204.2 of the Regulations will apply to the trust. Accordingly, the Successor Trust will be required to file a T3 Return, including Schedule 15, for each taxation year ending after its creation date in which it does not meet any of the exceptions listed in subsection 150(1.2). In a situation where the Successor Trust does meet one of the exceptions listed in subsection 150(1.2), consideration would need to be given to the exceptions in subsection 150(1.1).

Part 2.

Subsection 104(4) provides for a deemed disposition date for every trust.[2] However, generally, where capital property, land included in inventory, Canadian resource property or foreign resource property is transferred at a particular time by a trust to another trust in circumstances in which subsection 107(2) or 107.4(3) or paragraph (f) of the definition of disposition in subsection 248(1) applies, the rules in subsection 104(5.8) will apply for the purposes of, *inter alia*, subsection 104(4).

For the purposes of subsection 104(4), the first day (the "disposition day") that ends at or after the transfer that would be determined in respect of the Successor Trust is deemed pursuant to subsection 104(5.8) to be the earliest of:

- The 21-year deemed disposition date of the testamentary spousal trust ending at or after the transfer, as determined by subsection 104(4), which is April 15, 2046 (21 years after the date of death of the surviving spouse) [104(5.8)(a)(i)(A)]; and
- The 21-year deemed disposition date of the Successor Trust ending at or after the transfer, as determined by subsection 104(4), which is February 15, 2047 (21 years after the creation of the Successor Trust) [104(5.8)(a)(i)(B)].

This will be April 15, 2046, which is 21 years after the date of death of the surviving spouse in this case.

Part 3.

Where the first generation trust is a trust other than a testamentary spousal trust (i.e., created under the terms of the will of an individual for a person other than a spouse or common law partner), for the purposes of subsection 104(4), the first day (the "disposition day") that would be determined in respect of the Successor Trust is deemed pursuant to subsection 104(5.8) to be the earliest of:

- The 21-year deemed disposition date of the first generation trust ending at or after the transfer, as determined by subsection 104(4), which is July 1, 2036 [104(5.8)(a)(i)(A)]; and
- The 21-year deemed disposition date of the Successor Trust ending at or after the transfer, as determined by subsection 104(4), which is February 15, 2047 [104(5.8)(a)(i)(B)].

This will be July 1, 2036, which is 21-years after the date of death of the testator in this case.

[2] The definition of "trust" in subsection 108(1) does not include certain trusts for the purposes of, *inter alia*, subsection 104(4).

QUESTION 3. Deemed Resident Trust and Section 150

For estate planning purposes, an individual resident in Canada establishes a U.S. resident trust that will be a beneficiary under that individual's last will and testament. The trust is settled with a $20 bill. Such planning is typical for individuals providing a legacy for a child who is a U.S. person so that the legacy received is not part of that child's estate for U.S. estate tax purposes. No other property will be transferred to the trust until after the individual dies. As such, until other property is transferred, the trust will have no income or gains.

Pursuant to subsection 94(3), the trust will be deemed to be resident in Canada and, pursuant to subparagraph 94(3)(a)(vii) will be subject to the obligations under Division I as if a resident of Canada.

Can the CRA confirm that if the only property of the trust in a particular tax year is the $20 bill, the trust is exempt from filing a T3 Return by virtue of subsection 150(1.1) assuming it meets all the conditions of that subsection? Can the CRA also confirm that the trust is not obligated to comply with section 204.2 of the Regulations (i.e., filing a Schedule 15)?

CRA Response

Where subsection 94(3) applies to a non-resident trust for a tax year, the trust is deemed to be resident in Canada throughout the year for the purposes specified in paragraph 94(3)(a), including for the purpose of determining the rights and obligations of the trust under sections 150 to 180.

In general, subsection 150(1) requires taxpayers to file a return of income for each tax year on or before a specified date or within a specified time period. Pursuant to paragraph 150(1)(c), in the case of an estate or trust, a return of income shall be filed within 90 days from the end of the year. Subsection 150(1.1) provides exceptions, subject to subsection 150(1.2), to the filing requirements in subsection 150(1).

Subsection 150(1.2) operates in a manner that limits the exceptions in subsection 150(1.1), such that the filing requirements in subsection 150(1) may continue to apply if the trust is resident in Canada and is an express trust, or for civil law purposes a trust other than a trust that is established by law or by judgement, unless the trust is a trust described in any of paragraphs 150(1.2)(a) to (r).

The exception in paragraph 150(1.2)(b) applies where a trust holds assets with a total fair market value that does not exceed $50,000 throughout the year. If a particular trust meets this exception, or one of the other exceptions listed in subsection 150(1.2), subsection 150(1) will not apply where the trust also meets one of the exceptions in subsection 150(1.1).

Since the trust is deemed to be resident in Canada pursuant to subsection 94(3), it would be required to file a T3 Return pursuant to paragraph 150(1)(c) unless the exception in paragraph 150(1.1)(b) also applies. In particular, a trust is required to file a T3 Return for a tax year where:

- tax is payable under Part I by the trust for the year, or
- the trust has a taxable capital gain or disposes of capital property in the year.

Since the only property of the trust in the tax year is the $20 bill, the trust is a trust described in paragraph 150(1.2)(b) for the particular tax year. Further, since the trust has not realized any income or gains and has not disposed of any capital property in the tax year, the exception in paragraph 150(1.1)(b) applies. As such, the trust will not be required to file a T3 Return pursuant to subsection 150(1) for the particular tax year.

Subsection 204.2(1) of the Regulations applies in respect of a trust, other than a trust described in any of paragraphs 150(1.2)(a) to (r), that is required to file a T3 Return pursuant to subsection 150(1). Since the trust is described in paragraph 150(1.2)(b), and is not required to file a T3 Return pursuant to subsection 150(1), it is also not required to file Schedule 15 for the particular tax year.

Additionally, since the T3 Return is both a return of income and an information return, the statutory requirement to file a T3 Return exists, pursuant to section 204 of the Regulations, where the trustee has control of, or receives income, gains or profits in the trustee's fiduciary capacity, or in a capacity analogous to a fiduciary capacity. However, in this particular case, provided that the trustee does not have the control of, or receive income, gains or profits in the trustee's fiduciary capacity, the trust will also not be required to file a T3 Return pursuant to section 204 of the Regulations for the particular tax year.

Finally, a trust deemed to be resident in Canada pursuant to subsection 94(3) is not considered to be resident in Canada for the purposes of section 233.2. Accordingly, the $20 settlement constitutes a contribution to a non-resident trust under subsection 94(1), such that subsection 233.2(4) would require the settlor to file Form T1141 for the year of contribution and subsequent years provided the filing conditions continue to be met and no exclusion applies.

QUESTION 4. *Vefghi* Case and Timing of Dividend Payments

The Federal Court of Appeal in *Canada v. Vefghi Holding Corporation*[3] held that the relevant time for determining whether a payer corporation ("Opco") is "connected" with a corporate beneficiary ("Benco") receiving the dividend income as a distribution from a shareholder trust is the last day of the trust's taxation year (the trust's "Particular Taxation Year"); that is the day the corporate beneficiary is deemed to have received a taxable dividend by interpreting subsection 104(19). As a result, the Federal Court of Appeal concluded in the *Vefghi* decision that the connected test for the purposes of Part IV tax must be conducted at the end of the trust's Particular Taxation Year.

1. Can the CRA confirm whether the same rationale would apply to capital dividends, having the meaning assigned in subsection 83(2), received by Benco by way of distributions from the trust? Specifically, when would Benco include the capital dividend received in its capital dividend account as defined in subsection 89(1) ("Capital Dividend Account")?
2. Assume the trust realized a capital gain on the disposition of a capital property in a Particular Taxation Year and distributes the whole of the capital gain (the taxable and non-taxable portions) to Benco before the end of that Particular Taxation Year. Can the CRA confirm when Benco would include the non-taxable portion of the capital gain in its Capital Dividend Account?
3. Assume the trust is a graduated rate estate ("GRE"), as defined in subsection 248(1), with an off-calendar year end of, say, February 28 and Benco has a December 31 calendar year end. If the GRE earns a taxable dividend or realizes a capital gain in the period from March 1 to December 31 in a particular year, and distributes those amounts to Benco before the end of December 31 of that year, in what year does Benco report the income or taxable capital gains?

[3] 2025 FCA 14 (the "*Vefghi* decision"). An application for leave to appeal to the Supreme Court of Canada ("SCC") was filed. As of this date, the SCC has not yet ruled on the application for leave to appeal.

CRA Response

For Part 1 and Part 2, it is assumed that Benco is a private corporation, as defined in subsection 89(1), and is entitled to maintain, and make additions to, a Capital Dividend Account at all relevant times.

Part 1.

It is the CRA's view that the position outlined in document 2010-0363191C6 and at paragraph 1.75 of the Folio S3-F2-C1[4] remains applicable following the *Vefghi* decision.

Provided that the trust makes the designation under subsection 104(20) in respect of the distributions made in the trust's Particular Taxation Year in favour of Benco, Benco will add to its Capital Dividend Account the lesser of the amounts described in subparagraphs (g)(i) and (ii) of the definition of Capital Dividend Account.

Benco's Capital Dividend Account cannot be increased before the end of the trust's Particular Taxation Year because the condition for the designation under subsection 104(20) cannot be satisfied before that time. Therefore, the amount thus determined under paragraph (g) of the definition of Capital Dividend Account will be added to Benco's Capital Dividend Account at the end of the trust's Particular Taxation Year.

Part 2.

It is understood that the trust has distributed the entire amount of the capital gains realized in its Particular Taxation Year in favour of Benco. We assume that one half of the amount distributed, that is, the amount of the trust's net taxable capital gains, as determined under subsection 104(21.3), is designated as a taxable capital gain of Benco under subsection 104(21).

It is the CRA's view that the position outlined in document 2023-0959591C6 and at paragraph 1.43.1 of the Folio S3-F2-C1 remains applicable following the *Vefghi* decision.

Pursuant to subsection 104(21), provided that all requirements under that subsection in respect of the distributions of the trust's net taxable capital gains realized by the trust in a Particular Taxation Year in favour of Benco are satisfied, the amount so designated by the trust under subsection 104(21) for that Particular Taxation Year will be deemed, for the purposes set out in that subsection, to be a taxable capital gain, for the taxation year of Benco in which the trust's Particular Taxation Year ends, from the disposition by Benco of capital property. The remainder of the amount distributed, that is, the amount distributed out of the non-taxable portion of capital gains of the trust, is referred to in subparagraph (a)(i.1) of the definition of Capital Dividend Account.

Benco cannot include an amount referred to in subparagraph (a)(i.1) of the definition of Capital Dividend Account in the calculation of its Capital Dividend Account before the end of the trust's Particular Taxation Year because the condition for the designation under subsection 104(21) cannot be satisfied before that time. Therefore, in determining its Capital Dividend Account, Benco will include the lesser of the amounts determined under clauses (A) and (B) so referred to in subparagraph (a)(i.1) of the definition of Capital Dividend Account at the end of the trust's Particular Taxation Year.

[4] *Income Tax Folio* S3-F2-C1 – Capital dividends, January 13, 2025 ("Folio S3-F2-C1").

Part 3.

<u>Taxable dividend</u>

As provided in subsection 104(19), for the purposes set out in that subsection, a taxable dividend received by a trust, in the trust's Particular Taxation Year, on a share of the capital stock of a taxable Canadian corporation, is deemed to be a taxable dividend on the share received by the beneficiary, in the beneficiary's taxation year in which the trust's Particular Taxation Year ends.

Therefore, provided that the trust makes the designation under subsection 104(19) and all of the requirements set out in that provision are satisfied, Benco will include the amount thus designated in its December 31 taxation year end in which the trust's Particular Taxation Year ends.

It is the CRA's view that the *Vefghi* decision does not raise any uncertainty in this regard. Moreover, Wyman W. Webb J.A. reiterates in the *Vefghi* decision at paragraph 63 that "[t]he deeming rule in subsection 104(19) of the Act is clear that the dividend is deemed to be received by the beneficiary (including a corporate beneficiary) in the taxation year of that beneficiary in which the trust's taxation year ends."

<u>Capital gain</u>

It is understood that the trust has distributed the entire amount of the capital gains realized in its Particular Taxation Year in favour of Benco. We assume that one half of the amount distributed, that is, the amount of the trust's net taxable capital gains, as determined under subsection 104(21.3), is designated as a taxable capital gain of Benco under subsection 104(21).

Subsection 104(21) provides, for the purposes set out in that subsection, that an amount in respect of a trust's net taxable capital gains for its Particular Taxation Year is deemed to be a taxable capital gain, for the taxation year of a taxpayer in which the trust's Particular Taxation Year ends, from the disposition by the taxpayer of capital property.

Therefore, provided that all of the requirements set out in subsection 104(21) are satisfied, Benco will include the amount thus designated in its December 31 taxation year end in which the trust's Particular Taxation Year ends.

It is the CRA's view that the *Vefghi* decision does not raise any uncertainty in this regard.

QUESTION 5. <u>Canadian Real Property Transferred by U.S. Person to U.S. Grantor Trust</u>

An individual is a citizen and resident of the U.S. for income tax purposes and has never been a resident of Canada for income tax purposes. The individual owns Canadian real property. For U.S. probate and tax planning purposes, the individual will settle a U.S. grantor trust by transferring the Canadian real property to the trust. The terms of the trust provide that the individual will be the trustee of the trust and the sole capital and income beneficiary of the trust during their lifetime, and that the property will be distributed to certain family members after the individual's death (also referred to as a "U.S. revocable living trust"). Central management and control of the trust will reside in the U.S.

For U.S. income tax purposes, the U.S. grantor trust is disregarded such that the individual will not be treated as having disposed of the Canadian real property. Further, the U.S. resident individual will not be making a request under Article XIII(8) of the Canada - U.S. Tax Treaty.

1. Can the CRA confirm that, even though this would not result in a disposition for U.S. tax purposes, that for Canadian income tax purposes the individual will be treated as having disposed of the Canadian real estate for fair market value proceeds?

2. Can the CRA also confirm that the individual would be obligated to comply with the reporting obligations under section 116?

CRA Response

Part 1.

It has been the CRA's longstanding opinion that a U.S. revocable living trust should be recognized for income tax purposes at the time that legal title to property is transferred to it and that the transfer of the property is at its full fair market value (and not the value of the remainder interest only). This continues to be the CRA's opinion in respect of U.S. revocable living trusts.

As stated in Document #2016-0645781C6, it is the CRA's view that a key distinguishing factor between a U.S. revocable living trust and a bare trust is that a U.S. revocable living trust generally includes beneficiaries that are contingent on the death of the settlor/grantor. As such, there is a change of beneficial ownership in respect of a transfer to a U.S. revocable living trust.

As the "Canadian real property" is real or immovable property situated in Canada, it therefore meets the definition of the term "taxable Canadian property" in subsection 248(1). Accordingly, for Canadian income tax purposes, the transfer of Canadian real property by the U.S. resident individual to the U.S. revocable living trust would constitute a disposition of taxable Canadian property for proceeds of disposition equal to the fair market value of the Canadian real property pursuant to paragraph 69(1)(b). Any taxable capital gain should be reported for Canadian income tax purposes by the individual for the taxation year in which the Canadian real property is transferred to the U.S. revocable living trust pursuant to paragraph 115(1)(b).

Part 2.

The rules of section 116 apply when a non-resident person disposes of certain taxable Canadian property, which includes real or immovable property situated in Canada. The non-resident person will be required to notify the CRA either before the disposition or within 10 days after the disposition, using form T2062, and is required to submit a payment (or acceptable security) equal to 25% of the gain on the disposition. The gain is generally calculated as the amount of the proceeds of disposition less the adjusted cost base of the property.

Since the transfer of the Canadian real property by the U.S. resident individual to the U.S. revocable living trust is a disposition of taxable Canadian property that is made to a person with whom the U.S. resident individual is not dealing with at arm's length for no proceeds of disposition (or for proceeds of disposition less than the fair market value of the property), then for purposes of subsections 116(1) and 116(3), the U.S. resident individual's proceeds of disposition are considered to be equal to the fair market value of that property, pursuant to subsection 116(5.1). In addition, the U.S. revocable living trust may have a potential liability under subsection 116(5).

QUESTION 6. <u>Timing of Trust Withholding Payment Under Part XIII</u>

Pursuant to subparagraph 214(3)(f)(i), where an amount has been made payable, but has not been paid or credited, by a trust to a non-resident beneficiary before the end of the trust's taxation year, the amount is deemed to have been paid by the trust on the day that is 90 days after the end of the trust's taxation year. This date corresponds to the deadline for filing the T3 Return for the taxation year of the trust in which the amount became payable. Pursuant to subsection 215(1), Part XIII tax shall be forthwith remitted from the date on which the amount is deemed to have been paid or credited, provided the amount was not paid at an earlier time.

Assuming that the trust has a December 31 year-end, does the CRA agree that, in the scenario described, the remittance deadline would be April 15 of the following year, in accordance with the administrative guidance in Guide T4061 *NR4 – Non-Resident Tax Withholding, Remitting, and Reporting*?

Assuming that the CRA agrees, is there a way to ensure that the CRA will not assess penalties where the remittance is received by the Minister on or before the April 15 remittance deadline?

CRA Response

Paragraph 214(3)(f) determines when income from a trust is deemed to have been paid or credited to a non-resident beneficiary for the purposes of Part XIII. The relevant time is the earliest of the times set out in clauses 214(3)(f)(i)(A) to (C). In the situation described, the amount was not paid or credited, and subparagraph 128.1(4)(a)(i) did not apply to the trust's taxation year. Accordingly, the relevant time is the day that is 90 days after the end of the trust's taxation year, which in this case is March 31.

Based on the above hypothetical facts, Part XIII tax should, under subsection 215(1), be withheld on March 31 and forthwith remitted to the Receiver General. Pursuant to the administrative policy set out in Guide T4061 *NR4 – Non-Resident Tax Withholding, Remitting, and Reporting*, if the remitted tax is received by the Receiver General on or before the 15th day of the month following the month in which the amount was paid or credited to the non-resident (April 15 in this case), the remittance will be considered to comply with subsection 215(1). In those circumstances, the CRA would not apply the penalty and interest provisions in subsections 227(9) and 227(9.2).

QUESTION 7. <u>RRSP and Named Beneficiary</u>

An individual is the annuitant of an unmatured RRSP. The designated beneficiary of the RRSP is a former spouse of the annuitant. Upon the death of the annuitant, the fair market value of the RRSP would generally be included in the deceased's final income tax return. To the extent that the payment of the RRSP proceeds to the former spouse does not exceed the amount included in income of the deceased annuitant, no tax would be withheld on the payment of the RRSP proceeds to the former spouse, and the former spouse would receive the full amount on a tax-free basis. As a result, the deceased's estate (and ultimately its beneficiaries) would bear the full tax liability associated with the RRSP, while the designated beneficiary of the RRSP would receive the proceeds of the RRSP on a tax-free basis.

Does CRA agree?

CRA Response

Where the annuitant of an unmatured RRSP dies, subsection 146(8.8) deems the annuitant to have received, immediately before death, an amount as a benefit out of or under the RRSP equal to the fair market value of all the property held in the RRSP at the time of death. Pursuant to subsection 146(8) and paragraph 56(1)(h) this amount, together with any other amounts received by the annuitant from the RRSP in the year, generally has to be included in computing the deceased annuitant's income in the year of death. The tax liability of the deceased that arose as a result of such income inclusion is generally settled using property of the estate.

Pursuant to subsection 146(8), a taxpayer is required to include in their income for a taxation year all amounts received in the year as benefits from an RRSP. The definition of "benefit" in subsection 146(1) determines what portion of an amount received out of an RRSP (if any), will be a benefit for the purpose of applying subsection 146(8). With respect to the amounts received by a beneficiary of an RRSP, pursuant to paragraph (a) of the definition of benefit, the portion of the amount that was deemed to have been received by the deceased annuitant, pursuant to subsection 146(8.8), is excluded. As a result, when the designated beneficiary (the former spouse in this case) receives an amount from the RRSP, only the portion that is not an amount deemed to have been received by the deceased annuitant by virtue of subsection 146(8.8) constitutes a benefit out of or under an RRSP. Consequently, the former spouse would receive the RRSP proceeds, equal to the fair market value of the RRSP at the time of the annuitant's death, on a tax-free basis, while the resulting tax liability arising from the deemed receipt of an amount under subsection 146(8.8) and the inclusion in income of the amount under subsection 146(8) and paragraph 56(1)(h) is generally settled using property of the estate.

In general, subsection 160.2(1) provides that where a taxpayer other than the annuitant of the RRSP, such as a designated beneficiary, receives an amount all or part of which is described in paragraph (b) therein, the taxpayer is jointly and severally liable with the deceased annuitant for the portion of the deceased annuitant's income tax that is attributable to the amount.

QUESTION 8. Acquisition of Control of Corporation

The use of *alter ego* and joint partner trusts as will substitutes is becoming more common in Canada. Such trusts often simplify personal estate planning as they cover both incapacity and death. Often the settlor will be a trustee until such time as they become incapable or die, when they will be replaced by others. After the settlor's incapacity or death, the trustee(s) will change and may in the future continue to change from time to time in accordance with the trust terms.

If the assets of the *alter ego* or joint partner trust include controlling shares of a corporation, can the CRA comment on whether there will be an acquisition of control or loss restriction event for the corporation as a result of the replacement of the trustee by:

a) a person related to the settlor?
b) a person unrelated to the settlor?
c) an independent trust company?

CRA Response:

Pursuant to subsection 248(1), the term "*alter ego* trust" refers to a trust to which paragraph 104(4)(a) applies, if read without reference to subparagraph 104(4)(a)(iii) and clauses 104(4)(a)(iv)(B) and (C). Furthermore, the term "joint spousal or common-law partner trust" ("joint partner trust") means a trust to which paragraph 104(4)(a) would apply if that paragraph were read without reference to subparagraph 104(4)(a)(iii) and clause 104(4)(a)(iv)(A).

To qualify as an *alter ego* trust, a trust, among others, must be created by a taxpayer (the "settlor") who is 65 years of age or older, for the settlor's own benefit during his or her lifetime and, under the terms of the trust deed, the settlor is entitled to receive all of the income of the trust that arises before the taxpayer's death. In addition, no person except the settlor could, before the settlor's death, receive or otherwise obtain the use of any of the income or capital of the trust[5].

[5] Clause 104(4)(a)(iv)(A)

Similarly, in the case of a joint partner trust, the terms of the trust deed must provide that the settlor or the settlor's spouse or common-law partner (the "settlor's partner") is, in combination with the settlor's partner or the settlor, as the case may be, entitled to receive all of the income of the trust that arises before the later of the death of the settlor and the death of the settlor's partner. In addition, no other person could, before the later of those deaths receive or otherwise obtain the use of any of the income or capital of the trust[6].

Paragraph 256(7)(i) applies in circumstances in which a trust, at a particular time after September 12, 2013, controls a particular corporation and the trustee or other legal representative (the trustee) having ownership or control of the trust property (i.e., including shares of the capital stock of the particular corporation held by the trust) changes.

Paragraph 256(7)(i) deems control of the particular corporation not to be acquired solely because of the change, provided that two additional conditions are met. First, subparagraph 256(7)(i)(i) requires that the change in trustees is not part of a series of transactions or events that includes a change in the beneficial ownership of the trust's property. Second, subparagraph 256(7)(i)(ii) requires that no amount of income or capital of the trust to be distributed, at any time at or after the change, in respect of any interest in the trust depends upon the exercise by any person or partnership, or the failure of any person or partnership, to exercise any discretionary power.

The question of whether the trustees of an *alter ego* trust or a joint partner trust have a discretionary power with respect to income or capital distributions is a question of fact that requires an analysis of the terms of the trust deed. However, the CRA is generally of the view that the trustees of such trust who hold a power to encroach on capital thereby hold discretionary authority with respect to the capital of the trust. Consequently, depending on the circumstances and the terms of the trust deed, the condition may not be satisfied where an *alter ego* trust or a joint partner trust is involved, with the result that paragraph 256(7)(i) would not apply to deem that no acquisition of control of the corporation has occurred. This could be the case where the trustees of such trust hold a power to encroach on income or capital. The fact that the replacement trustee is related or not to the settlor is not relevant in such case.

Where paragraph 256(7)(i) does not apply, the CRA's longstanding position[7] would continue to apply. Specifically, where the majority of the voting shares of a corporation are held by a trust, it is the trustees of the trust who have the legal ownership of the shares, who have the right to vote those shares, and who, therefore, control the corporation. Where a trust has multiple trustees, the determination as to which trustee or group of trustees controls the corporation can only be made after a review of all the pertinent facts, including the terms of the trust document. However, in the absence of evidence to the contrary, we would consider there to be a presumption that all of the trustees would constitute a group that controls the corporation.

Consequently, we would generally take the position there would be an acquisition of control in the situations described in b) and c) above. With respect to a) above, paragraph 256(7)(a) may apply, where shares are acquired by a person related to the former trustee, to deem that there be no acquisition of control.

[6] Clauses 104(4)(a)(iv)(B) and (C).
[7] STEP 2022 – Q 6 - Acquisition of control and change of trustee(s).

QUESTION 9. Trust Refreeze

The transactions and series of transactions designated by the Minister for the purposes of section 237.4 in NT 2023-02[8] (the "Designated Transactions") include transactions and series of transactions that seek to avoid or defer the 21-year deemed realization rule in subsection 104(4) or that seek to avoid the rules in subsections 107(5) and (2.1) on the distribution of trust property to a non-resident beneficiary even though the property continues to be held, directly or indirectly, by a trust or by a non-resident beneficiary.

A transaction that is the same as, or substantially similar to, the Designated Transactions, or a transaction in a series of transactions that is the same as, or substantially similar to, the Designated Transactions would constitute a notifiable transaction. Two transactions, or series of transactions, are substantially similar if they are expected to obtain the same or similar types of "tax consequences" (as defined in subsection 245(1)) to one or more persons and the transactions or series of transactions are either factually similar or based on the same or similar tax strategy. This is to be interpreted broadly, in favour of disclosure.

Paragraph 81 of the CRA guidance webpage on the mandatory disclosure rules (the "CRA Guidance")[9] states that the following transactions would not be considered substantially similar to the Designated Transactions:

> *"Generally, transactions which limit, in whole or in part, the future growth in the value of shares of Opco (common shares) by having the owner - Old Trust - exchange the common shares for new shares that have a fixed value (preferred shares) that is equal to the fair market value (FMV) of the common shares and where a New Trust subscribes to the growth in the value of shares of Opco ("a freeze") or where the Old Trust sells the common shares at FMV to the New Trust would not be considered substantially similar to NT 2023-02 insofar as no rights and restrictions are expected to avoid or defer the 21-year deemed realization rule or to avoid the rules in subsections 107(5) and (2.1) through a significant reduction in FMV."*

Can the CRA confirm that the transactions described in paragraph 81 of the CRA Guidance would not be subject to the application of the general anti-avoidance rule ("GAAR")? If the CRA is of the view that the GAAR could be applicable in certain circumstances, could it clarify what factors it would consider in making such a determination?

CRA Response

The CRA would not generally seek to apply the GAAR in circumstances where, as described in paragraph 81 of the CRA Guidance, a trust (described as "Old Trust" in the CRA Guidance) would exchange common shares it holds in a corporation for preferred shares having a redemption value and fair market value equal to the fair market value of the common shares so exchanged or where a trust would dispose of common shares it holds in a corporation to a newly formed trust for proceeds of disposition equal to the fair market value of the common shares so disposed of at that time, and where, considering all rights and restrictions applicable in the circumstances, such transactions would not be substantially similar to the Designated Transactions. This is because such transactions would not, in and by themselves, be considered to result in a misuse or abuse of subsections 104(4), 104(5.8), 107(2.1) or 107(5). However, the CRA's conclusion could differ if, after a review of the

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[8] CRA, Notifiable transactions designated by the Minister of National Revenue online: Government of Canada <https://www.canada.ca/en/revenue-agency/programs/about-canada-revenue-agency-cra/compliance/mandatory-disclosure-rules-overview/notifiable-transactions-designated-by-minister-national-revenue.html>.
[9] CRA, Mandatory Disclosure Rules – Guidance online: Government of Canada <https://www.canada.ca/en/revenue-agency/programs/about-canada-revenue-agency-cra/compliance/mandatory-disclosure-rules-overview/guidance-document.html>.

rights, restrictions, and all other relevant facts applicable in a particular case, it is determined that the transactions or series of transactions result in the same or similar types of tax consequences as those noted in the Designated Transactions.

In addition, please note that our comments are limited to the transactions specifically described in paragraph 81 of the CRA Guidance. The CRA's conclusion on the application of the GAAR could be different if it was found that the transactions formed part of a broader series of transactions. The determination of whether the GAAR would apply to any particular situation would require a full consideration of all the facts and circumstances.

QUESTION 10. <u>Notifiable Transaction: New Trusts with Corporate Beneficiaries Owned by Potential Non-Resident Beneficiaries</u>

A family trust is settled with beneficiaries that include Canadian corporations owned by one of the named individual beneficiaries. At the time of settlement, there is a possibility that this individual is planning to attend university in the U.S. and may become a non-resident of Canada in the future.

1. Because it is possible the individual beneficiary may emigrate from Canada, is Form RC312 required to be filed within 90 days of the trust's settlement to disclose a notifiable transaction (NT-2023-02)?

2. If Form RC312 was filed within 90 days of the trust's settlement and disclosed a series of transactions where:

    - a named beneficiary may emigrate from Canada within a specified timeframe, and

    - if emigration occurs, trust property will be distributed under subsection 107(2) to a Canadian corporation owned by that beneficiary within a subsequent specified timeframe,

based on paragraph 69 of CRA's *Mandatory Disclosure Rules – Guidance*, this initial disclosure describing the series satisfies the reporting obligation for each transaction in that series, provided no new transactions, parties, hallmarks, or material facts arise.

Can the CRA confirm that, in the above scenario, an amended Form RC312 is not required to be filed if the transactions occur as described in the initial disclosure?

CRA Response

Part 1.

Subsection 237.4(4) requires certain persons to file an information return in respect of a notifiable transaction. A "notifiable transaction" is generally defined as a transaction, or a transaction in a series that is the same, or substantially similar to, a transaction designated by the Minister.

NT-2023-02 designates certain transactions as notifiable, including those involving an indirect transfer of trust property to a non-resident through the use of a Canadian-resident corporate beneficiary to avoid or defer the "21-year deemed realization rule" in subsection 104(4), or to avoid the rules in subsections 107(5) and 107(2.1) even though the property continues to be held, directly or indirectly, by a trust or by a non-resident beneficiary.

Whether a filing obligation under subsection 237.4(4) exists is a question of fact.

On the facts provided, no person has yet entered into, or become contractually obligated to enter into, a transaction or transaction in a series that is the same as, or substantially similar to, the designated transaction or designated series. Indeed, there is only a possibility at the time of the trust's settlement that a beneficiary may later become non-resident. That possibility, on its own, does not establish that a notifiable transaction has been entered into, nor does it create any contractual obligation that any person has become contractually obligated to enter into one. As a result, an RC312 filing would not be required solely because the trust is settled in these circumstances.

A filing requirement may arise if the facts later establish that a person has entered into, or become contractually obligated to enter into, a transaction, or a transaction in a series, that is the same as, or substantially similar to NT-2023-02. In that case, subsection 237.4(9) would generally require the RC312 to be filed within 90 days after the earlier of the day the person becomes contractually obligated to enter into the notifiable transaction and the day on which the person enters into the transaction.

Part 2.

On the facts provided and for reasons explained above, the reporting requirement in section 237.4 has not arisen at the time of the trust's settlement. Paragraph 69 of the *CRA's Mandatory Disclosure Rules – Guidance* does not alter that result, since it presupposes that a valid reporting obligation has already arisen in respect of a disclosed transaction or series.

If the facts later establish that a person has entered into, or become contractually obligated to enter into, a transaction, or a transaction in a series, that is the same as, or substantially similar to, the designated transaction or designated series under NT-2023-02, the filing obligations, if any, will have to be determined at that time under subsections 237.4(4) and (9).

QUESTION 11. Tax ID Numbers

Part 1.

Subsection 237(1.1) requires a person (the "disclosing person") to provide its tax identification number to another person (the "collecting person") where the collecting person is required to make an information return under the Act or Regulations. Subsection 237(2) further requires the collecting person to make a "reasonable effort" to obtain the number. Failure to do so may result in the collecting person being subject to penalties, such as under subsection 162(5) for failing to provide information on a prescribed form, or under subsections 162(7) and potentially subsection 163(5) for failing to report beneficiary information on Schedule 15 of a T3 Return.

Can the CRA clarify what constitutes "reasonable effort" in this context? Specifically, if the disclosing person does not respond to repeated communications by email or mail to the last known contact information, would continuing to send notices to that address or email suffice? Or does CRA expect additional steps beyond repeated attempts to the last known contact?

Part 2.

Subsection 239(2.3) provides that it is an offence to knowingly use, communicate (or permit another to use or communicate) a tax identification number other than for a purpose required under the Act and Regulations, or otherwise by law, without the "written consent" of the disclosing person.

Can the CRA comment on what satisfies the requirement for "written consent" under subsection 239(2.3)?

CRA Response

Part 1.

Paragraph 237(2)(a) imposes an obligation on the collecting person required to make an information return pursuant to the Act or the Regulations requiring a tax identification number (i.e., business number, Social Insurance Number (SIN), or trust account number, as the case may be) of the disclosing person to make a reasonable effort to obtain the number from the disclosing person.

Whether a collecting person has made a "reasonable effort" to obtain a tax identification number for the purposes of paragraph 237(2)(a) is a question of fact. However, we offer the following comments that may be of assistance.

In our view, a collecting person will generally have made a reasonable effort where they have taken bona fide steps to request the number using the contact information reasonably available to them, and have maintained adequate records of those efforts, as stated in paragraphs 5, 10 and 11 of IC82-2R2 Social Insurance Number Legislation that Relates to the Preparation of Information Slips:

> 5. Information slip preparers have to ask their clients to give their SIN and other personal data, such as their name and address. This request can take any form that is practical for the preparers.
> ...
> 10. Information slip preparers should keep any documents they need to prove they made a reasonable effort to get their clients' SIN. For example, when they send a request by mail, the preparers should keep a record of the date of the request, an example of the request form, and the names of the people contacted (e.g., shareholders of record at the date of the request, members of a co-operative or holders of deposit accounts).
>
> 11. If clients do not respond to a SIN request, information slip preparers should not delay filing the information returns after they are due. If their clients' SIN are not available, information slip preparers should leave the SIN area of the slip blank.

In addition, an example of reasonable effort in the context of paragraph 237(2)(a) can be found on our webpage Get the social insurance number (SIN) from the individual:

> After asking the recipient for their SIN many times, you decided to contact them in writing to request their SIN. You made notes of the dates you asked for the SIN verbally, and kept copies of any written requests.

The actions suggested in your question would generally be consistent with what CRA considers to be "reasonable effort", provided that the collecting person has maintained adequate records of their efforts. However, what is reasonable in any situation can only be determined on a case-by-case basis, depending on the facts and circumstances of each case. For example, if mail sent to a disclosing person's last known address is returned undelivered, continuing to send mail only to that same address may not, by itself, be considered "reasonable effort", when the collecting person has other means of contacting the disclosing person (such as a phone number or an email address) that were left unused.

Part 2.

In general terms, it is an offence under subsection 239(2.3) for the collecting person to knowingly use or communicate the tax identification number (i.e., business number, SIN, and trust account number, as the case may be) of the disclosing person, or allow it to be communicated, without the written consent of the disclosing person, otherwise than for authorized purposes, as follows:

- as required or authorized by law;
- in the course of duties in connection with the administration or enforcement of the Act; or
- for a purpose for which it was provided by the disclosing person.

Accordingly, if a collecting person intends to use the tax identification number for a purpose other than one of the authorized purposes provided under subsection 239(2.3), “written consent” for the intended use must be obtained from the disclosing person to avoid the offence under this subsection.

Whether a collecting person has obtained “written consent” in the context of subsection 239(2.3) is a question of fact. However, we offer the following comments that may be of assistance.

Meaning of “written”

Subsection 35(1) of the *Interpretation Act* defines the term “writing” for every enactment, as follows:

> ***writing****, or any term of like import, includes words printed, typewritten, painted, engraved, lithographed, photographed or represented or reproduced by any mode of representing or reproducing words in visible form. (écrit)*

In *Foley* v. *The Queen*,[10] the Tax Court of Canada commented that the word “writing”, as defined in the Interpretation Act, includes electronic mail, and that an exchange of e-mail communication between parties can constitute a “written agreement”.

In light of the foregoing, we are of the view that “written consent” must be documented in writing, whether on paper, in an electronic record, or in other forms that represent or reproduce words in visible form. On that basis, verbal or implied consent through conduct would not be considered “written consent”.

Meaning of “consent”

In considering the meaning of “consent”, we also looked to privacy-law principles and related guidance that, while not determinative for subsection 239(2.3), support the view that consent should be clear, specific and affirmative, particularly given the sensitivity of tax identification numbers.

Based on these considerations, we are of the view that an express, opt-in consent would generally provide the clearest evidence that written consent was obtained for the purposes of subsection 239(2.3).

Whether the “written consent” requirement in the context of subsection 239(2.3) is met ultimately depends on the facts and circumstances of each case. However, CRA will generally consider the requirement to be met where the disclosing person affirmatively checks an unticked-by-default checkbox, separate from or clearly distinguished from general terms and conditions, using clear and specific language describing the particular use or communication of the tax identification number in question.

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[10] *Foley v. The Queen, 2000 CanLII 232 (TCC), <https://canlii.ca/t/1c4mh>*

QUESTION 12. <u>Schedule 15 Penalty</u>

According to information shared by the CRA with CPA Canada in August 2025, the CRA will discard Schedule 15 information in cases where filing was not required; for example, a trust that exists for fewer than three months but is still required to file a T3 Return. This approach is due to the Privacy Act, which prevents the CRA from storing Schedule 15 data when it is not required. The CRA noted that Notices of Assessment ("NOA") will indicate that Schedule 15 information was not retained.

If a prior filed Schedule 15 was not required, if such a trust later files Schedule 15 in a year where it is required and indicates "no change" from the prior year, the CRA will assess a penalty because no previous information exists on file. This is especially problematic in light of Budget 2025 changes, where bare trust filing requirements have been deferred to taxation years ending after December 30, 2026. Practitioners may have inadvertently filed Schedule 15 for bare trusts in 2024 and/or 2025 when they were not required.

1. Can the CRA confirm whether a Schedule 15 filed with a T3 Return for a bare trust's 2023 tax year was retained by the CRA? It is noted that the relief from the T3 Return and Schedule 15 filing requirement for that year was administrative with the Act requiring the filing of these forms.

2. Can the CRA confirm that they will assess a penalty in such a situation (where "no change" is marked in the later Schedule 15 in a year when it was required)? Could CRA instead provide administrative relief?

CRA Response

Part 1.

A Schedule 15 was retained by the CRA when it was filed with a T3 Return for a bare trust's 2023 tax year, unless it received the following note on its NOA:

> "Based on the information you gave us, you did not need to report beneficial ownership information this year. As a result, we did not update our records with the information you had given us. However, you may need to submit Form T3SCH15, Beneficial Ownership Information of a Trust, in future years, depending on your situation."

As standard practice, the CRA assesses a penalty where "no change" is marked on a Schedule 15 and there is no existing beneficial ownership information on file. This includes situations where the CRA did not retain prior year information as per the CRA's standing position on the Privacy Act restrictions.

Over the past two years, the CRA was made aware by external stakeholders and taxpayers that the practice of discarding voluntarily submitted beneficial ownership information was problematic because many filers weren't aware that the information was not being retained by the CRA, despite the note provided on the NOA. As such, in 2024, the CRA paused the practice of discarding the beneficial ownership information in order to re-examine its position and the risks associated with storing the information.

Following additional review and analysis, the CRA has revised its interpretation of the Privacy Act restrictions that had previously prevented storage of the beneficial ownership information, as the information was voluntarily submitted by the taxpayer in a self-assessment system. The CRA has determined that it can keep the voluntarily submitted information so that it can apply its beneficial ownership carry-forward policy in future years, if required.

The CRA now processes and retains Schedule 15s submitted voluntarily by a trust, including some of those submitted over the past two years.

Part 2.

Given the change in position vis-à-vis the Privacy Act restriction, the CRA may consider providing relief related to the Schedule 15 penalty based on the trust's specific circumstances.

Additional instructions for filers
To make sure that the CRA has the most up to date beneficial ownership information, the next time the trust files a Schedule 15 make sure to complete:

- Part A – Annual beneficial ownership information, by answering:
    - "NO" to the question "Is this the first time the trust is reporting beneficial ownership information?"
    - "YES" to the question "Has the beneficial ownership information of the trust changed since the last time it was reported?"
- Part B – Identification of reportable entities, for each reportable entity of the trust.
- Part C – Beneficiaries unable to be listed (if applicable).

If you received a note on your NOA that the CRA did not retain your beneficial ownership information and you are required to file a Schedule 15 with your next T3 Return, please submit Schedule 15 and complete Part A by selecting "Yes" to the first question about reporting beneficial ownership information for the first time, then complete Part B and C as applicable.

QUESTION 13. Determination of Electing Trust's Income

Where, in a particular year, one of the "resident contributors"[11] to a trust, which is deemed to be resident in Canada pursuant to paragraph 94(3)(a) (the "DRT"), ceases to be a "resident contributor" and there is no "resident beneficiary" under the DRT, the DRT can file an election pursuant to the definition of "electing trust" provided all of the other conditions therein have been met.

When so elected, paragraph 94(3)(f) will apply to the DRT, which generally speaking, deems a second *inter vivos* trust to be created, and removes from the taxable base of the DRT the income earned by this second trust (referred to as the non-resident portion trust).

Consider the following scenario:

- There are three "resident contributors" to the DRT, all of whom are individuals: Contributor A, Contributor B and Contributor C;
- Contributor A passed away on September 1, 2025;
- Section 94 has applied to the DRT for several years. Contributors B and C continue to be "resident contributors" to the DRT throughout the DRT's 2025 taxation year;
- Prior to the death of Contributor A, the DRT has never had a "non-resident portion";
- The "contributions" made by each of Contributor A, Contributor B, and Contributor C continue to be held in the DRT throughout the 2025 taxation year;
- All "contributions" to the DRT were direct transfers of property to the DRT;
- None of the "contributions" is a transfer described by any of paragraphs 94(2)(a), (c), (d) or (f);

[11] Each term in quotations is defined in subsection 94(1) of the Act), unless otherwise noted.

- All beneficiaries under the DRT have always been and will continue to be non-residents of Canada. Accordingly, although there are "connected contributors" to the DRT, there are no "resident beneficiaries" under the DRT; and
- The property which forms the DRT's "non-resident portion" earned dividend income of $5,000 from January 1, 2025 to August 31, 2025, and $10,000 from September 1, 2025 to December 31, 2025.

1. Can the CRA confirm what income should be reported by the DRT in its T3 Return for the particular year?

2. Can the CRA also confirm how expenses incurred in the particular year should be allocated between the DRT and the non-resident portion trust?

CRA Response

Part 1.

Paragraph 94(3)(a) deems a non-resident trust to be resident in Canada for the specific purposes mentioned therein, when the following conditions are met at a "specified time" in the trust's taxation year (normally the trust's taxation year end):

- the trust is factually a non-resident of Canada;
- the trust is not an "exempt foreign trust"; and
- the trust has either a "resident contributor" or a "resident beneficiary".

Where subsection 94(3) applies, the DRT is *inter alia,* subject to tax under Part I of the Act on its world-wide income. When certain conditions are satisfied however, a DRT may file an election to be an "electing trust".

If a trust makes a valid election in writing to have paragraph 94(3)(f) apply to it for its first taxation year in which it is deemed to be resident in Canada pursuant to subsection 94(3) and holds property that is part of its "non-resident portion", it will be deemed to have its non-resident portion be held in a separate *inter vivos* trust (the non-resident portion trust). Further, the trust will be treated as if it were two trusts, one that is deemed resident in Canada and one that is not resident in Canada for that taxation year and each subsequent taxation year.

In the present scenario, Contributor A passed away in 2025. Therefore, in that year, to be an "electing trust" the DRT must:

- for the first time, hold property which is at any time during the trust's 2025 taxation year part of the DRT's "non-resident portion";
- be deemed by subsection 94(3) to be resident in Canada *throughout* that year; and
- make a valid election to have paragraph 94(3)(f) apply to the DRT.

It has been established that the trust is a DRT throughout the DRT's 2025 taxation year; therefore, the DRT must hold property for the first time that is, at any time in 2025, part of its "non-resident portion". The "non-resident portion" of a trust at any time, is all property held by the trust to the extent that it is not, at that time, part of the "resident portion" of the trust. Therefore, the DRT's "resident portion" must first be determined which occurs at a particular time. Since Contributor A passed away on September 1, 2025, the time immediately after the death of Contributor A on September 1, 2025 will be the particular time that will be used to test whether the DRT has a "resident portion".

At the particular time, in the scenario described, the DRT holds property which has been contributed on or before the particular time to the DRT by a “contributor” that is, at that time, a “resident contributor”. This would be all property contributed to the trust by Contributors B and C.

Also, at the particular time, immediately after the death of Contributor A on September 1, 2025, the “contributions” of Contributor A would not form part of the DRT’s “resident portion”[12] since that property, which continues to be held by the DRT, is not property in respect of which a “contribution” has been made at or before the particular time to the DRT by a “contributor” who is a “resident contributor” at that time. Nor was the “contribution” made by a “contributor” who is, at that time, a “connected contributor” where there is a “resident beneficiary” under the DRT.

As noted above, Contributor A, being deceased, is not a “resident contributor” after death on September 1, 2025, and although Contributor A is a “connected contributor” to the DRT after death on that day, there is no “resident beneficiary” under the DRT.

Therefore, on September 1, 2025, at any time (after the death of Contributor A), the DRT will have a “non-resident portion”.[13]

As long as the DRT makes a valid election pursuant to the definition of “electing trust”, the DRT will be an “electing trust” for the DRT’s 2025 taxation year and for each subsequent taxation year of the DRT. As noted above, paragraph 94(3)(f) will apply to the DRT and the following will, *inter alia*, occur:

- a non-resident portion trust will be deemed to be created on January 1, 2025, for the purposes of the Act (other than for the purposes of subsection 104(2))[14] [94(3)(f)(i)];
- all of the DRT’s property that is part of the DRT’s “non-resident portion” will be deemed to be the property of the non-resident portion trust and not to be, other than for the purposes of paragraph 94(3)(f), and the definition of “electing trust”, property of the DRT [94(3)(f)(ii)];
- for greater certainty, the non-resident portion trust is deemed not to have a “resident contributor” or a “connected contributor” to it [94(3)(f)(iv)(C)];
- the non-resident portion trust is deemed to be, without affecting the liability of its trustees for their own income tax, in respect of its property an individual [94(3)(f)(v)];
- the property that becomes, at a particular time (on September 1, 2025), part of the DRT’s “non-resident portion”, is deemed to have been transferred to the non-resident portion trust at that time [94(3)(f)(vi)]; and
- the DRT and the non-resident portion trust are deemed at all times to be affiliated with each other and to not deal with each other at arm’s length [94(3)(f)(viii)].

As noted above, the DRT is deemed have transferred the property that forms its “non-resident portion” to the non-resident portion trust on September 1, 2025. Accordingly, the DRT will be considered to have disposed of that property on that date. Since the DRT and the non-resident portion trust are deemed not to deal with each other at arm’s length, subsection 69(1) will be applicable such that the DRT is deemed to have received proceeds of disposition equal to the fair market value of the property deemed to have been transferred, with the effect that any realized capital gains will be reportable by the DRT in its T3 Return for the DRT’s 2025 taxation year.

[12] See the definition of “resident portion” which provides further components of the “resident portion” which have not been referred to herein.
[13] Note that if the above two definitions were tested for at any time on August 30, 2025, the DRT would have only a resident portion as all contributions of property made before that date, or property substituted therefor, would have been made by persons who were resident contributors on August 30, 2025.
[14] The non-resident portion trust is deemed to continue in existence until the earliest of the times described in clause 94(3)(f)(i)(B).

Further, since the DRT is deemed to have transferred the property that forms its "non-resident portion" to a separate trust on September 1, 2025, any income, gains or losses realized on such property after that time will be income of the non-resident portion trust. However, such property will continue to form part of the DRT's resident portion prior to that time. Accordingly, the DRT must include the income earned on, and capital gains and losses realized on, that property during the period from January 1, 2025 to August 31, 2025 in its T3 Return for the DRT's 2025 taxation year. In respect of the scenario described, the DRT would be required to include the dividend income of $5,000 earned between January 1 and August 31, 2025 on the property transferred to the non-resident portion trust, in its T3 Return for the DRT's 2025 taxation year. The $10,000 earned between September 1 and December 31, 2025 on that property would be considered to belong to the non-resident portion trust and would only be subject to Part I tax to the extent of the application of subsection 2(3).

Part 2.

Subsection 9(1) defines a taxpayer's income for a taxation year from a business or property as the taxpayer's profit from that business or property for the year. "Profit" is not defined in the Act but has been considered by the courts. In *Canderel v. R.*, [1998] 1 S.C.R. 147, the Supreme Court of Canada laid out principles for determining profit. In particular, a taxpayer can choose any method of determining profit that provides an accurate picture of the taxpayer's profit for the year, provided that it is not inconsistent with the provisions of the Act, rules of law (i.e., case law), and well-accepted business principles.

QUESTION 14. <u>Subparagraph (g)(iv) of the Definition of Trust</u>

Consider a situation in which a trust ("Trust") was settled in the U.S. by an individual resident in Canada approximately 20 years ago. The fair market value of the trust property has increased such that there is a substantial accrued gain. Trust is not factually resident in Canada; however, Trust is considered a deemed resident trust pursuant to subsection 94(3).

Trust has two beneficiaries, who are each entitled to 50% of the income and capital of Trust. Beneficiary A is a U.S. resident for income tax purposes, whereas Beneficiary B is a resident of Canada for income tax purposes.

The deemed disposition at fair market value of the property of Trust on the 21 year anniversary of Trust, referred to in paragraph 104(4)(b), is approaching. This deemed disposition will not apply if all of the interests in Trust have vested indefeasibly pursuant to paragraph (g) of the definition of trust in subsection 108(1) and none of subparagraphs (g)(i) to (vi) apply.

For purposes of the question, assume that the interests in Trust are otherwise vested indefeasibly; however, we wish to confirm whether subparagraph (g)(iv) would apply. Subparagraph (g)(iv) applies if the total fair market value of the interests of the non-resident beneficiaries is more than 20% of the total fair market value of all of the interests in Trust. However, subparagraph (g)(iv) refers to "a trust that is at that time resident in Canada". As Trust in this case is deemed to be resident in Canada, does subparagraph (g)(iv) apply?

CRA Response

Paragraph (g) of the definition of trust in subsection 108(1) provides for a potential exception to the 21-year deemed disposition rule in paragraph 104(4)(b) where all interests of the trust at that time have vested indefeasibly.[15] Ultimately, whether a trust would fall under paragraph (g) is a question of fact and law that requires reference to the applicable law, jurisprudence, the will or trust agreement and all other relevant documents and circumstances in respect of those interests. It is also a question of fact and law as to whether a trustee has the power within the terms of a trust to vest all interests indefeasibly.

For paragraph (g) to apply, none of subparagraphs (g)(i) through (vi) can apply. Subparagraph (g)(iv) refers to:

> (iv) a trust that is at that time resident in Canada where the total fair market value at that time of all interests in the trust held at that time by beneficiaries under the trust who at that time are non-resident is more than 20% of the total fair market value at that time of all interests in the trust held at that time by beneficiaries under the trust,

Subparagraphs 94(3)(a)(i) and (ii) are relevant in determining whether the phrase "resident in Canada" includes a deemed resident trust. Subparagraphs 94(3)(a)(i) and (ii) indicate that a deemed resident trust is deemed to be resident in Canada throughout the particular taxation year for the purposes of applying section 2 and in computing the trust's income for the year. The Department of Finance Explanatory Notes to subsection 94(3) indicate that the result of the application of subparagraphs 94(3)(a)(i) and (ii) is that the trust is subject to tax under Part I "on its worldwide income for the year (including, for example, its income determined as a result of deemed dispositions under subsections 104(4) to (5.2) or 128.1(4) and,...) that is not distributed to beneficiaries of the trust or attributed to resident contributors of the trust."[16]

Subsection 108(1) provides definitions for subdivision k of Division B – Computation of Income in Part I. As the definition of trust in subsection 108(1) impacts the application of subsection 104(4), among others, it is relevant for computing Trust's income for the year. Accordingly, the application of subparagraph (g)(iv) of the definition of trust to a deemed resident trust is supported by subparagraphs 94(3)(a)(i) and (ii).

Therefore, the phrase "a trust that is at that time resident in Canada" in subparagraph (g)(iv) applies to trusts that are factually resident and those which are deemed to be resident in Canada by virtue of subsection 94(3). Since Beneficiary A's interest in the trust has a fair market value greater than 20% of the fair market value of all the interests in the trust, subparagraph (g)(iv) applies to Trust. Consequently, the exception provided by paragraph (g) cannot apply, and the deemed disposition pursuant to paragraph 104(4)(b) will apply to Trust.

QUESTION 15. <u>T1135 and Partnership</u>

A partnership is established and operated under foreign law and holds foreign investment property (for example, foreign rental real estate). Canadian residents hold over 10% of the interests in the partnership.

Does the filing requirement in subsection 233.3(3) apply to the partnership and the Canadian partners, provided they are reporting entities pursuant to subsection 233.3(1)?

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[15] For additional comments with respect to vesting indefeasibly, see 2021 STEP Question 6 (document 2021-0883021C6).
[16] The Department of Finance Explanatory Notes to Bill C-48.

If the partnership is required to file Form T1135 – *Foreign Income Verification Statement* ("Form T1135") to report its interest in the foreign property, what should be done if, in the past, the partnership did not report its interest in the foreign property, and instead relied on the fact that the Canadian partners have reported their ownership of the partnership interest on Form T1135?

CRA Response

For the purpose of our comments below, we have assumed that:

- Canadian residents are entitled to a proportional share of income or loss from the foreign partnership equal to the interest they hold in the partnership;
- Canadian residents are residents in Canada throughout the year;
- the only asset of each Canadian resident is its respective interest in the foreign partnership;
- the cost amount of the foreign rental real estate exceeds $100,000; and
- the foreign rental real estate held by the foreign partnership is not used or held exclusively in the course of carrying on an active business.

<u>Reporting obligations</u>

Pursuant to subsection 233.3(3), a reporting entity, as defined under subsection 233.3(1), must file a return in the prescribed form, in this case, Form T1135. This form requires that a reporting entity discloses its specified foreign property.

Pursuant to subsection 233.3(1), a "reporting entity" is defined as:

> "***reporting entity*** for a taxation year or fiscal period means a specified Canadian entity for the year or period where, at any time (other than a time when the entity is non-resident) in the year or period, the total of all amounts each of which is the cost amount to the entity of a specified foreign property of the entity exceeds $100,000."

For the purposes of this definition, we also note that paragraph (b) of the definition "specified Canadian entity" in subsection 233.3(1) includes a partnership where the total of all amounts, each of which is a share of the partnership's income or loss for the period of a member that is a non-resident person or a taxpayer referred to in any of subparagraphs (a)(i) to (viii), is less than 90% of the income or loss of the partnership for the period. On the assumptions above, that condition would be met.

The expression "specified foreign property" is defined under subsection 233.3(1), and its paragraph (b) provides for "tangible property, or for civil law corporeal property, situated outside Canada", which includes foreign rental real estate.

Assuming the foreign partnership is a reporting entity within the meaning of subsection 233.3(1), it would be required to report on Form T1135 its specified foreign property, including the foreign rental real estate.

By contrast, on the assumptions above, the Canadian resident partners would not qualify as reporting entities pursuant to subsection 233.3(1), as their only property is their interest in the partnership, and an interest in a partnership that is a specified Canadian entity is excluded from "specified foreign property" by virtue of the exception provided in paragraph (o) of that definition in subsection 233.3(1).

Failure to report

Subsection 162(7) imposes a penalty for failing to file Form T1135. Where the failure is made knowingly or under circumstances amounting to gross negligence, the penalties set out in subsections 162(10) and 162(10.1) apply. In the present case, the filing of Forms T1135 by the Canadian partners does not exempt the partnership from its separate obligation to file Form T1135.

Under Canada's self-assessment system, the CRA encourages reporting entities and other taxpayers to come forward and voluntarily correct their tax affairs, either by filing an amended Form T1135 to correct past filing errors or, where the eligibility criteria are met, by making an application under the Voluntary Disclosures Program ("VDP").

Additional information in regard to the VDP can be found at https://www.canada.ca/en/revenue-agency/programs/about-canada-revenue-agency-cra/compliance/voluntary-disclosures-program.html.