August 13th, 2024

Rob Demeter
Director General
Tax Legislation Division
Tax Policy Branch
Department of Finance
90 Elgin Street
Ottawa, ON
K1A 0G5

Via email: rob.demeter@fin.gc.ca

Dear Mr. Demeter:

Re: Legislation Pertaining to the New Mandatory Disclosure Rules, in Particular Reportable Transactions

Enclosed is a submission from the Tax Technical Committee of STEP Canada on the new mandatory reporting regime related to reportable transactions.

STEP Canada's membership represents a broad cross-section of professional advisors operating in the fields of estate planning and wealth management. The STEP Canada executive believes that our comments on the mandatory reporting regime and reportable transactions may be of assistance to you in augmenting the published guidance.

Several members of the STEP Canada Tax Technical Committee participated in discussions concerning our submission and contributed to its preparation, in particular:

Crystal Taylor, LLB, TEP (Felesky Flynn LLP)
Joan Jung, LLB, TEP (Miller Thomson LLP)
Sébastien Desmarais, LLB, JD (USA), LLL, TEP (TD Wealth, Wealth Advisory Services)
Kenneth Keung, CPA, CA, CFP, MTAX, LLB, TEP (Moodys Tax), Deputy Chair, STEP Canada Tax Technical Committee

We would be pleased to discuss our comments with you at your convenience.

Kindly direct any enquires to Michael Dodick, Chief Operating Officer at mdodick@step.ca.

Yours truly,

Rachel Blumenfeld, LLB, TEP
Chair, STEP Canada

Ian Lebane, LLB, LLM, TEP
Chair, STEP Canada Tax Technical Committee

Cc: Trevor McGowan, Associate Assistant Deputy Minister

Submission of the Tax Technical Committee of STEP Canada on Legislation Pertaining to the Mandatory Disclosure Rules

I. Mandatory Disclosure for "Reportable Transactions"

1. The new mandatory disclosure rules in subsection 237.3(2) of the *Income Tax Act* (Canada) ("the Act") received royal assent on June 22, 2023. The rules relating to "reportable transactions" will apply when two criteria are met:

    a. It can reasonably be concluded that one of the main purposes of entering into the transaction or series of transactions is to obtain a tax benefit; and

    b. A transaction or series of transactions has at least one of three generic hallmarks: contingent fee arrangements, confidential protection, or contractual protection.

    The first criterion paraphrases the "reportable transaction" definition in subsection 237.3(1), which technically requires an "avoidance transaction." The term "avoidance transaction" is now defined for the purposes of section 237.3 and no longer adopts the meaning assigned by subsection 245(3). As a result, for a transaction or series of transactions to constitute an "avoidance transaction" for the purposes of section 237.3, it is simply necessary that "one of the main purposes" of the transaction or series is to obtain a tax benefit. The definition of the term "tax benefit" in subsection 245(1) applies to section 237.3; in general terms, a tax benefit is a reduction, avoidance, or deferral of tax or other amount payable under the Act. A transaction that relies on subsection 107(2) could constitute an avoidance transaction for the purposes of section 237.3 on a distribution of property from or the wind-up of an estate or inter vivos trust.

2. Guidelines and examples published by the Canada Revenue Agency (CRA), first released on August 2, 2023, and updated from time to time ("the Guidance"), provide practitioners with helpful assistance in applying the new rules and the various hallmarks.

3. The submission herein relates to the contractual protection hallmark. Contractual protections include any protections such as indemnities, insurance, and compensation to protect against a failure to obtain a tax benefit.

4. In the Guidance, the CRA makes the following comment about indemnities: "Standard *commercial* indemnities provisions in standard client agreements or documentation, which do not contemplate a specific identified tax benefit or tax treatment would not, in and of themselves, result in a reporting obligation" (emphasis added).

II. Estate Administration and Wind-Up Practice

5. The role of a personal representative (PR) of an estate is to administer the estate diligently and in a timely manner. Upon completion of the administration of the estate, the PR should proceed with a distribution of the residue of the estate to the beneficiaries. Often, the sole reason for a delayed distribution is the PR's obligations under the Act.

6. Section 159 requires a "legal representative" (which includes a PR) to obtain a clearance certificate from the CRA before making a distribution of property out of an estate, and it imposes personal liability for the tax liability of the estate on the PR if the PR fails to obtain the clearance certificate.

7. The consequences of failing to comply with section 159 were highlighted in *Muth Estate*, 2019 ABQB 922. In that case, the executor of an estate held back funds for the estimated tax owing by the estate and then distributed the balance to herself and the other beneficiaries. Unfortunately, the holdback turned out to be less than the full amount owing, even though it had been estimated by an accountant. As a result, the executor sought reimbursement from the beneficiaries of their proportionate shares of the shortfall. The court concluded that the other beneficiaries were under no obligation to indemnify the executor for income tax or penalties imposed as a result of her failure to obtain a clearance certificate before distributing the estate and found that the executor was personally liable for the tax liability.

8. The section 159 rule is difficult for a PR to comply with in practice because the process of obtaining a clearance certificate can be lengthy and, in many cases, may result in the estate continuing beyond the three-year period for a "graduated rate estate." In light of the adverse tax implications for an estate that continues longer than three years, it has become standard practice for a PR to make a substantial distribution to the beneficiaries of the estate prior to receipt of a clearance certificate, and to have the beneficiaries provide the PR with an indemnity in the event that there is a tax liability payable by the estate that is not covered by a holdback. This practice of indemnifying the PR allows for the timely administration and wind-up of a deceased taxpayer's estate.

9. A PR may not be a beneficiary of the estate being administered. Where it is not, the PR does not have any financial interest in the property of the estate and is not entitled to a share of the distribution on wind-up. It is reasonable that the PR in this situation would request and receive indemnification from those who benefit from the distribution made to them on wind-up of the estate. Indeed, even if the PR is included among the beneficiaries, the PR may not be the sole beneficiary or have an interest as beneficiary that is commensurate with the potential risk facing a PR under section 159. Hence, an indemnification against subsequently assessed tax liability of the estate is commonly recommended.

10. Attached as Schedule "A" to this submission is an extract from Miller Thomson on Estate Planning (published by Thomson Reuters), chapter 8, paragraph 8.79, which highlights the recommended practice delineated above in the administration of an estate.

III. Wind-Up of an Inter Vivos Trust

11. An inter vivos trust may hold the common shares of a private corporation following the implementation of an estate freeze. It is common estate-planning practice to distribute the common shares to beneficiaries prior to the 21st anniversary of the date of settlement of the trust, in order to address the tax consequences that would otherwise arise on a deemed disposition under subsection 104(4) of the Act. The common shares may therefore represent over 20 years of growth in value. As is recommended for a PR on an estate wind-up, the trustee authorizing the distribution of property and wind-up of an inter vivos trust will typically seek an indemnity and release from the beneficiaries, regardless of whether a clearance certificate under section 159 has been obtained. A similar request for an indemnity and release is often made for a distribution prior to a wind-up event as well.

12. Attached as Schedule "B" to this submission is a sample indemnity and release that is commonly requested from trust beneficiaries.

IV. Submission and Recommendation

13. STEP Canada is particularly concerned that the use of the word "commercial" in the description of the contractual protection hallmark of the new mandatory disclosure rules may be interpreted to refer only to corporate transactions such as mergers and acquisitions and to preclude reliance upon the Guidance in the estate-planning context. The relationship

between beneficiaries of an estate and the deceased or the deceased's estate, and the relationship between beneficiaries of an inter vivos trust and the settlor, cannot fairly be described as "commercial." Rather, such relationships are more appropriately characterized as being fiduciary in nature. Further, in many circumstances, particularly where family relationships are involved, the executors of an estate or the trustees of an inter vivos trust may not take compensation for the position. Hence, it is our view that it is not correct to describe the indemnity in question as a "commercial indemnity." We therefore recommend that the Canada Revenue Agency clarify that the Guidance on the contractual protection hallmark in the mandatory disclosure rules extends to the standard indemnities provided in the estate administration and estate/trust distribution and wind-up context.

SCHEDULE "A"
Extract from Miller Thomson on Estate Planning

See attached.

Miller Thomson on Estate Planning § 8:79

Miller Thomson on Estate Planning

Martin Rochwerg, Rahul Sharma, Wendi Crowe*

Chapter 8. Taxation on Death

IV. Taxation of the Estate and Will Trusts

§ 8:79. Clearance Certificate

Subsection **159**(2) requires every legal representative to obtain a clearance certificate (Form TX21) from the Minister of National Revenue before distributing the estate.[1] The clearance certificate is evidence that all amounts for which the deceased taxpayer is or can reasonably be expected to become liable under the ***Income Tax Act*** up to the date of distribution and for which the legal representative may become liable, in his or her capacity as legal representative, have been paid or that the Minister has accepted security for the payment.

Where a clearance certificate has not been obtained, s. **159**(3) permits the Minister of National Revenue to assess the legal representative for the amount of the debt and the legal representative will be personally liable for payment of the outstanding debt to the extent of the value of the property so distributed.[2] The legal representative will not be personally liable where property never formed part of the estate or if property formed part of the estate but never within the control of the legal representative.[3]
There is no time limit for the assessment of a legal representative who has failed to obtain a clearance certificate.[4] However, the legal representative's liability is contingent upon the CRA's right to assess the deceased taxpayer and/or the estate as the primary tax debtor. In other words, if the underlying tax debt becomes statute-barred, the CRA cannot pursue the legal representative instead of the deceased taxpayer or the estate.

The liability of a personal representative is not affected by an incorrect or incomplete assessment or by the fact no assessment has been made by the CRA. Subsection **159**(2) provides that the liability of the legal representative is not only for amounts for which the taxpayer was liable under the ***Income Tax Act***, but extends to amounts which the taxpayer is or can reasonably be expected to become liable for under the ***Income Tax Act*** at or before the time the distribution is made from the estate. The debt of the taxpayer does not need to be established through an assessment in order to assess the taxpayer's legal representative.[5]

A clearance certificate can be obtained for a partial or a final distribution since it specifies the reporting periods during which the clearance certificate is applicable. The requirement to obtain a clearance certificate is mandatory in all cases, but where there are no amounts that are or can be reasonably expected to become payable or remittable, no enforcement action will be taken for the failure to obtain a clearance certificate.

The documents that should be filed with a request for a clearance certificate are outlined in Information Circular 82-6R8 — *Clearance Certificate*, dated December 10, 2010.

A legal representative should not distribute the entire estate until the appropriate clearance certificates are received, and if a partial distribution is planned, he or she should be advised to hold back a generous amount to cover any outstanding tax liability. Further, if the deceased's will does not provide for indemnification, the legal representative should at least require the residual beneficiaries to indemnify the legal representative against any income tax liability which may arise to the extent of such beneficiary's proportionate share of the estate and should also consider obtaining an indemnity from the beneficiary of a significant bequest.

While the issuance of a clearance certificate relieves the executor from personal liability, it does not free the estate from its primarily liability.[6] The CRA is permitted to "follow" assets distributed to beneficiaries, to satisfy the estate's tax liability.[7]

If the legal representative is distributing assets of a GST registrant, section 270 of the *Excise Tax Act* requires that a clearance certificate (Form GST 158) be obtained prior to distributing money or property.[8]

It is unclear whether a legal representative who is assessed under section 159 of the Income Tax Act or section 270 of the Excise Tax Act can challenge the underlying assessment of the deceased if the time for the deceased to object or appeal has expired. The CRA appears to accept the recent decisions in *Abrametz v. R.*,[9] and *Gaucher v. R.*,[10] where the Court found that it would be open to the legal representative to challenge the underlying assessment.[11]

Footnotes

* Author and Editor, Ms. Crowe thanks Victoria Hockley, Megan Koper, Laura Shylko and Carla Figliomeni for their contributions in writing this chapter.

1 An application for a clearance certificate is made in Form TX19.

2 The issuance of a clearance certificate only relieves the representative from liability under s. **159**(3) and liability is not discharged where the legal representative is otherwise liable to pay or remit an amount due to other provisions of the legislation.

3 Interpretation 2010-0376441E5 — *Liability of legal representatives.*

4 ITA, s. **159**(3)(b).

5 Information Circular 2010-037886117 — *Assessing a taxpayer's legal representative.*

6 Boger Estate v. Minister of National Revenue (*sub nom. Boger Estate v. R.*), 91 DTC 5506, 1991 CarswellNat 501, 1991 CarswellNat 798, [1991] F.C.J. No. 805, (*sub nom. Boger Estate v. Canada*) [1992] 1 F.C. 152, 46 F.T.R. 241, [1991] 2 C.T.C. 168, 43 E.T.R. 27 (Fed. T.D.), affirmed 1993 CarswellNat 930, [1993] F.C.J. No. 545, 65 F.T.R. 160 (note), [1993] 2 C.T.C. 81, 93 D.T.C. 5276, 155 N.R. 303, 50 E.T.R. 1 (Fed. C.A.).

7 Section 160.

8 The application is Form GST 352.

9 Abrametz v. R., 2009 FCA 70, 2009 CarswellNat 577, 2009 CarswellNat 5465, 2009 G.T.C. 2013 (Eng.), [2009] G.S.T.C. 43 (F.C.A.).

10 Gaucher v. R., 2000 CarswellNat 2656, [2000] F.C.J. No. 1869, 264 N.R. 369, 2000 D.T.C. 6678, [2001] 1 C.T.C. 125 (Fed. C.A.).

11 CRA Document number 2010-0390311E5.

SCHEDULE "B"

Release and Indemnity of Trust Beneficiary

See attached.

THE XXXXXXXXXXX TRUST

Acknowledgment, Release & Indemnity

WHEREAS XXXXXXX (the "**Trust**") was settled by an agreement dated XXXXXX, between XXXXXX, as settlor, and XXXXX ("**XXXXXX**"), as the original trustees (the "**Trust Agreement**");

AND WHEREAS XXXXXX remain the trustees of the Trust (the "**Trustees**");

AND WHEREAS the Trustees have resolved to encroach on capital and distribute all of the property and assets of the Trust, (the "**Distributed Property**") as set out in Schedule "A" attached hereto to the XXXXXX Beneficiaries by trustee resolution dated XXXXXX (the "**Resolution**") and wind up the Trust, a copy of which is attached hereto as Schedule "B", and the Trustees have completed the administration of the Trust;

AND WHEREAS with reference to the Distributed Property, XXXXXX have been distributed or transferred to the undersigned as a XXXXXX Beneficiary;

NOW THEREFORE IN CONSIDERATION OF THE FOREGOING and for other good and valuable consideration, the receipt and sufficiency of which is hereby irrevocably acknowledged, the undersigned, a XXXXXX Beneficiary of the Trust, does hereby:

1. acknowledge that I have been advised of the terms of the Trust and have had opportunity to make inquiry;

2. acknowledge that the portion of the Distributed Property that has been endorsed, distributed and transferred to me from the Trust by the Trustee is under my control either directly or beneficially;

3. approve of all acts taken by the Trustee and any predecessor trustee in connection with the administration of the Trust to the date hereof, including all acts included and described in the attached Resolution;

4. acknowledge that accounts relating to the Trust were not provided by the Trustee and I hereby dispense with the preparation and production of any accounting by or for the Trustee;

5. release, remit, quit claim and forever discharge absolutely the Trustee and any predecessor trustee of the Trust of and from any and all actions, causes of action, liabilities, suits, claims, debts, obligations, dues, accounts, bonds, covenants, contracts, demands indemnities and proceedings whatsoever at law or in equity (collectively **"Claims"**) which the undersigned now has, or hereafter can, shall or may have, for or by reason of or in any way arising out of any cause, matter or thing whatsoever against him either personally or in his capacity as Trustee for all acts and failures to act by him up to the present time in the administration of the Trust, including all acts included and described in the attached Resolution, provided that this release of the Trustee shall not extend to acts of wilful misconduct, fraud or gross negligence of such Trustee;

6. represent and warrant that I have not assigned my interest in the Trust and covenant that I will not assign to any other person or entity any of the Claims

which I am releasing hereby;

7. agree not to make any Claim or initiate any proceedings against any person who, or entity which, in respect of the Claims released hereby, might claim contribution from, or to be indemnified by, the Trustee, any predecessor trustee or the Trust.

8. **[**only to the extent of the aggregate amount or value of property (determined as of the date hereof) that I have received, out of the assets of the Trust,**]** indemnify the Trustee (sometimes referred to in this section as the "**Indemnified Party**") and agree to hold him harmless and to reimburse him for any amounts in respect of any and all claims, actions, and proceedings which may be made against the Trust and/or against him personally or as trustee of the Trust by anyone including the undersigned in any capacity whatsoever and/or by my issue, provided that this indemnity of the Indemnified Party shall not extend to any loss or damage attributable to wilful misconduct, fraud or gross negligence of the Indemnified Party. Without limiting the generality of the foregoing, this indemnity shall extend to any claim for taxes and withholding taxes (including interest and penalties) payable or claimed to be payable by the Trust and for any claims made for the payment of taxes and withholding taxes (including interest and penalties) against the Indemnified Party as trustee of the Trust or in his personal capacity which the Indemnified Party may sustain in any manner in relation to the Trust, including any taxes, penalties or interest which may be levied, assessed or reassessed as a result of the Trustee not obtaining a Certificate of Clearance pursuant to the provisions of the *Income Tax Act* (Canada), R.S.C. 1985, c.1, as amended from time to time, before distributing the capital of the Trust, and for all legal, accounting or other costs incurred forthwith as the same are incurred or expended with respect thereto;

9. acknowledge and declare that this document is intended to cover, and does cover, not only known Claims but also those not now known or anticipated but which may later develop or be discovered, including all the effects and consequences thereof;

10. acknowledge and agree that in the event I or any other person claiming through me, makes any Claim, or commences or threatens to commence any action or proceeding against the Trustee, in his personal or fiduciary capacities, or against any of the heirs, executors, administrators, substitute decision makers, attorneys, guardians, successors and assigns of the Trustee, for or by reason of any cause, matter or thing which is the subject matter of this document, this document may be raised and pleaded as an estoppel to any such Claim;

11. acknowledge that I have been advised by XXXX to obtain independent legal advice with respect to the execution of this Acknowledgment, Release and Indemnity; I have had an opportunity to do so and I have either obtained such independent advice or after due consideration I have chosen not to do so;

12. covenant and agree that the provisions of this Acknowledgment, Release and Indemnity shall inure to the benefit of the Trustees and their heirs, executors, administrators, trustees, successors and assigns, and shall be binding upon me, my issue and my respective heirs, executors, administrators, trustees, successors and assigns.

DATED: XXXXXX.