STEP Canada
ADVISING FAMILIES ACROSS GENERATIONS

February 25, 2026

Lindsay Gwyer
Director General, Tax Legislation Division
Tax Policy Branch, Department of Finance
90 Elgin Ottawa, ON
K1A 0G5

Via email: Consultation-Legislation@fin.gc.ca

CC: Robert Duong (Robert.Duong@fin.gc.ca) and Kristina Djogovic-Morgan (kristina.djogovic-morgan@fin.gc.ca)

Dear Ms. Gwyer:

Re: Proposed Amendments to the Trust Deemed Disposition Anti-Avoidance Rule in Subsection 104(5.8)

The STEP Canada Tax Technical Committee respectfully submits this letter in response to the Department of Finance's consultation on the draft legislative proposals released January 29, 2026, which include an amendment to the preamble of subsection 104(5.8) of the *Income Tax Act*, as originally announced in the 2025 federal budget.

The Proposed Amendment to Subsection 104(5.8) and STEP Canada's Concerns About Its Implication

The proposed amendment would revise the preamble to read (emphasis added):

> Where capital property, land included in inventory, Canadian resource property or foreign resource property is transferred**, directly or indirectly in any manner whatever,** at a particular time by a trust (in this subsection referred to as the "transferor trust") to another trust (in this subsection referred to as the "transferee trust") in circumstances in which subsection 107(2) or 107.4(3) or paragraph (f) of the definition disposition in subsection 248(1) applies …

If enacted, this proposal would apply in respect of transfers of property that occur on or after November 4, 2025.

As stated in the Department's Explanatory Notes to the legislative proposal, subsection 104(5.8) is intended to prevent the avoidance of the 21-year deemed disposition rule through trust-to-trust transfers that do not involve dispositions of property at fair market value. The proposed amendment seeks to expand the scope of the provision to address indirect trust-to-trust transfers. The Explanatory Notes further describe an example of the type of indirect transfer being targeted, namely, a tax-deferred distribution by a personal

trust to a corporation that is owned, in whole or in part, by another personal trust. We presume that the Department's intention in using the broad phrase "directly or indirectly in any manner whatever" to address the perceived mischief is to capture scenarios in which a distribution under subsection 107(2) is made to a corporation or other entity that may not be owned directly by another personal trust at the time of the distribution.

Where the conditions in the preamble of subsection 104(5.8) are satisfied, the provision accelerates the timing of the deemed disposition rule that would otherwise apply to the transferee trust. The transferee trust's first deemed disposition day would generally be the earliest of the following:

A. the first day that would have been a deemed disposition day for the transferor trust;

B. the first day that would otherwise be a deemed disposition day for the transferee trust;

C. where the transferor trust is a joint spousal or common-law partner trust and the spouse or common-law partner is alive at the time of transfer, the first day ending at or after the transfer; and

D. where the transferor trust is an alter ego trust or a trust to which paragraph 104(4)(a.4) applies (that is, a self-benefit trust) and the settlor is alive at the time of transfer, the first day ending at or after the transfer.

Paragraphs 104(5.8)(b), (b.1), (b.2), and (b.3) provide exceptions where the transfer is between life interest trusts of the same nature (for example, from one alter ego trust to another alter ego trust), in which case the acceleration rule does not apply.

Concern 1

We are concerned that the extremely broad phrase "directly or indirectly in any manner whatever," combined with the words "in circumstances in which subsection 107(2) … applies," casts the net too widely. While the provision could be interpreted narrowly to mean that the direct or indirect transfer itself must be the transaction to which the referenced provision (for example, subsection 107(2)) applies, it could also potentially be interpreted more broadly to include situations where such a provision applies to a separate transaction within a broader series of transactions that includes the transfer. As a result, many common transactions that are not motivated by an intention to defer the 21-year deemed disposition event in respect of property with accrued gains in a trust may be caught by amended subsection 104(5.8), giving rise to significant uncertainty for taxpayers.

Concern 2

The language of subsection 104(5.8) makes clear that the deemed disposition applies to the transferee trust as a whole. Accordingly, the transferee trust is deemed to dispose of **all** of its capital property, land included in inventory, and resource property on the accelerated deemed disposition date, regardless of the value or proportion of property

transferred directly or indirectly from the transferor trust. This can result in a full realization event for the transferee trust even where only a nominal or incidental amount of property is transferred directly or indirectly from the transferor trust. While we recognize that this is the existing scheme of subsection 104(5.8), this potentially punitive outcome is greatly amplified when the scope of the provision is expanded and there is uncertainty as to when the subsection applies.

Concern 3

Paragraphs 104(5.8)(b), (b.1), (b.2), and (b.3) prevent an acceleration of the deemed disposition event where the transfer occurs between life interest trusts of the same nature. However, given the proposed wording and its potential to capture sequential transfers, there may be scenarios in which a non-life interest trust is considered to have made an indirect transfer, in any manner whatever, to a life interest trust. In such cases, none of the exceptions in paragraphs 104(5.8)(b) to (b.3) would apply, because the transferor trust is not itself a life interest trust. As a result, a life interest trust that would otherwise be subject to a deemed disposition only on the death of the last life interest beneficiary may instead become subject to the 21-year deemed disposition date of the transferor trust. This represents a potentially significant acceleration of the deemed disposition event.

Concern 4

In *St. Michael Trust Corp. v. The Queen* (sub nom. *Garron*), 2010 FCA 309, the Federal Court of Appeal, in the context of section 94 as it then read, considered whether a trust had "acquired property, directly or indirectly in any manner whatever," from a Canadian-resident person. The court observed, at paragraph 80, that these words are meant to "capture every possible means by which the wealth and **income-earning potential** represented by the shares of a Canadian corporation can move to a non-resident trust from a Canadian resident beneficiary of the trust or a person related to that beneficiary." [emphasis added]

We do not believe that this statement should be interpreted to mean that the issuance or purchase of common shares at a nominal amount following a properly valued estate freeze constitutes a direct or indirect transfer of property, even where the words "in any manner whatever" are used. It is important to recognize that the facts in *Garron* were exceptional: the shares subject to the freeze were sold to an arm's-length purchaser for more than ten times the freeze value shortly after the freeze, strongly indicating a significant undervaluation at the time of the transaction. This context was central to the court's analysis and distinguishes *Garron* from typical estate freeze transactions carried out at fair market value.

Nevertheless, we are concerned that the Canada Revenue Agency (CRA) may seek to apply the reasoning in *Garron* more broadly, potentially asserting that even estate freezes implemented at appropriate valuations could constitute a direct or indirect transfer of property "in any manner whatever," where the freeze relates to shares owned by an older trust and new common shares are issued to or purchased by a new trust. The absence of a de minimis threshold in the proposed amendment exacerbates this concern. The CRA

could conceivably challenge transactions on the basis of nominal differences in valuation (for example, asserting that shares should have been valued at $51 million rather than $50 million used for the freeze), and on that basis allege an indirect transfer of property from the old trust to the new trust. Given that the valuation of operating businesses is inherently imprecise and typically expressed as a range, this creates significant uncertainty for taxpayers engaging in legitimate estate planning.

Common Scenarios That May Be Adversely Impacted by the Legislative Proposal

Impacted Scenario 1: Common Estate Planning

Since the announcement of the proposed amendment, we have heard from many STEP Canada members who are concerned that the amended subsection could apply to life interest trust planning undertaken solely for estate and probate planning purposes. The following example illustrates a very common scenario:

- A family trust ("Old Trust") settled on January 1, 2006 owns a capital property ("the Cottage").
- Old Trust distributes the Cottage to an individual, in circumstances where subsection 107(2) applies.
- Subsequently, the individual contributes the Cottage, together with other properties with unrealized gains, to a new trust that is a spousal trust, alter ego trust, self-benefit trust, or joint spousal or common-law partner trust. This subsequent transfer is undertaken solely for estate or probate planning purposes or, in the case of a self-benefit trust, for compliance or governance reasons (such as a politician addressing conflict-of-interest considerations).

Some could argue property of Old Trust is transferred indirectly to the transferee trust in circumstances in which subsection 107(2) applies (on the first leg of the broader series of transactions) and that as such amended subsection 104(5.8) could apply. As a result, the transferee life interest trust would become subject to a deemed disposition of all of its property on January 1, 2027, the 21-year anniversary of Old Trust. This deemed disposition would apply not only to the Cottage but also to other properties with unrealized gains contributed by the individual, even if the Cottage itself has no unrealized gain.

Absent the proposed amendment, the transferee life interest trust would not be subject to a deemed disposition until the death (or last-to-die) of the relevant life interest beneficiary. We submit that this acceleration is not intended. The deferral of a trust's deemed disposition to the death of a capital beneficiary has long been an underlying policy of the Act, and is a core feature of subsection 107(2) and the life interest trust regime more generally.

We also want to point out that even if the Cottage has no unrealized gain, it is common practice for trustees to rely on subsection 107(2) on a capital distribution because (1) the provision applies by default unless the trust elects out of it, and (2) it removes the risk

from the trustee of the CRA subsequently challenging the valuation of the distributed property.

Furthermore, given the coming-into-force provision applicable to the proposed amendment, it is unclear whether the situation is caught where the distribution of the Cottage by Old Trust to the individual occurs prior to November 4, 2025, but the subsequent transfer of the Cottage by that individual to the life interest trust occurs after that date.

Impacted Scenario 2: Other Subsequent Transfers by the Capital Beneficiary

There are many additional examples of common transactions that may be affected by the proposed amendment to subsection 104(5.8) as a result of events occurring **after** a capital beneficiary has received a distribution of property from a trust under subsection 107(2). For example:

- The beneficiary subsequently dies, such that the property becomes property of the beneficiary's graduated rate estate. Because an estate is treated as a trust for the purposes of the Act, some could view this as an indirect transfer, in any manner whatever, of capital property from the original trust to a testamentary trust (the graduated rate estate), in circumstances in which subsection 107(2) applied. As a result, the graduated rate estate may become subject to a deemed disposition of all of its property on the 21-year anniversary of the original trust. We also note that this interpretation could extend further to any testamentary trust to which the estate subsequently distributes the property (or substituted property), given the breadth of the phrase "directly or indirectly in any manner whatever … in circumstances in which … ."

- The beneficiary subsequently dies and the property passes to the beneficiary's estate, which in turn distributes the property to a child of the deceased under subsection 107(2). The child later contributes the property to a new trust. In these circumstances, the new trust may be considered to inherit either the deemed disposition date of the original trust or the 21-year anniversary date of the deceased's estate.

- The beneficiary subsequently sells the property to a third-party purchaser that is a trust. Because property is transferred indirectly from the original trust to another trust, and subsection 107(2) applied on the first leg of the series, the purchaser trust's 21-year deemed disposition date may be accelerated to that of the original trust. As discussed earlier in Concern 2, this acceleration would occur even where the property sold comprises a minimal percentage of the total asset value of the transferee trust.

Impacted Scenario 3: Freeze and Refreeze Transactions

The following example illustrates how freeze and refreeze transactions can be caught due to a minor undervaluation:

- A family trust holds common shares of an operating company valued at $10 million by an independent professional; two months later, the trust implements a freeze using this valuation, taking back $10 million in preferred shares and new common shares. The preferred and common shares are distributed to an individual under subsection 107(2), who then sells the common shares to a new trust for $1. If the CRA determines that the valuation failed to account for two months of retained earnings resulting in a minor undervaluation, existing law would generally tax only the incremental value under the benefit-conferral rules. However, under the proposed amendment to subsection 104(5.8), the CRA could assert that this minor undervaluation constitutes a direct or indirect transfer of property in any manner whatever from the old trust to the new trust (in circumstances to which subsection 107(2) applies), causing the new trust to inherit the old trust's 21-year deemed disposition date—a disproportionately harsh result for an immaterial valuation difference.

Concluding Comment

In summary, the proposed amendments to subsection 104(5.8) are too broad and risk capturing a wide range of ordinary trust and estate planning transactions that are not motivated by an intention to defer a deemed disposition in respect of gains inside a trust beyond the last-to-die of a capital beneficiary and their spouse.

Recommendations: Targeted Application of Subsection 104(5.8) to Prevent Unintended Acceleration of Deemed Dispositions

We understand that the Department of Finance is seeking to address the potential deferral of the deemed disposition event through tax-deferred distributions by a personal trust to an entity that is directly or indirectly owned, in whole or in part, by another personal trust. While the Explanatory Notes indicate that this is intended to be an illustrative example of an indirect trust-to-trust transfer targeted by the proposed amendment, we are not aware of other transactions involving tax-deferred distributions by a trust, indirectly to another trust, that could result in a deferral of the 21-year deemed disposition on gains accrued in the transferor trust.

Moreover, for the reasons outlined above, we are not aware of transactions involving indirect transfers to life interest trusts that give rise to the type of deferral concern the amendment is intended to address.

Accordingly, we respectfully submit that subsection 104(5.8) be more narrowly targeted to capture transactions involving tax-deferred distributions to beneficiaries in which another personal trust has a direct or indirect interest, rather than apply generally to

indirect trust-to-trust transfers. To this end, we recommend the introduction of a new interpretive provision, subsection 104(5.81), to operate in conjunction with subsection 104(5.8), as follows:

Alternative 1: Introduce new subsection 104(5.81)

> **For the purposes of subsection 104(5.8), where a property is distributed by a trust to a taxpayer in circumstances in which subsection 107(2) applies, and another personal trust holds, directly or indirectly, an interest in the taxpayer at the particular time of the distribution, the property shall be deemed to have been transferred at that particular time by the trust to the other trust in circumstances in which subsection 107(2) applies.**

Such a provision would appropriately address the Department's concern regarding the transfer of value on a tax-deferred basis to an entity in which another trust has a direct or indirect interest. At the same time, by tying the application of subsection 104(5.8) to the existence of that interest at the time of the subsection 107(2) distribution, this approach would avoid inadvertently capturing subsequent transfers by the recipient taxpayer to another trust. Under existing legislation, property transferred in those subsequent transactions would be transferred to a trust on a taxable basis at fair market value or, in the case of a tax-deferred transfer to a spousal trust, alter ego trust, self-benefit trust, or joint spousal or common-law partner trust, would remain subject to deemed disposition at fair market value on the death (or last-to-die) of the relevant life interest beneficiary.

If the Department prefers to retain the broad "directly or indirect transfer in any manner whatever" wording currently proposed, we suggest limiting the application of subsection 104(5.8) in the following manner, in order to avoid capturing non-tax motivated estate planning, subsequent trust transfers and situations in which only future growth is transferred:

Alternative 2: Amend subsection 104(5.8)

> Where capital property, land included in inventory, Canadian resource property or foreign resource property is transferred **in specie**, directly or indirectly in any manner whatever, at a particular time by a trust (in this subsection referred to as the "transferor trust") to another trust (in this subsection referred to as the "transferee trust") **other than a transfer to which subsection 73(1) applies, and such transfer involves a distribution** in circumstances in which subsection 107(2) or 107.4(3) or paragraph (f) of the definition "disposition" in subsection 248(1) applies **which results in an increase in the fair market value of the property of the transferee trust at the time of the distribution**, …

If these recommendations are not adopted, we respectfully request that the Department provide clear interpretive guidance in the Explanatory Notes regarding the intended scope of "directly or indirectly in any manner whatever" and "in circumstances in which," to reduce uncertainty for taxpayers and administrators.

Furthermore, we believe that the punitive consequence of subsection 104(5.8) is disproportionately harsh when combined with the proposed expansion of its scope. In this regard, we respectfully request that the Department consider **limiting the effect of subsection 104(5.8) such that any accelerated deemed disposition applies only to the property transferred directly or indirectly to the transferee trust, rather than to all property held by that trust**.

Finally, we respectfully ask the Department to **consider abandoning the proposed amendment to subsection 104(5.8) altogether**. The specific transaction that the amendment appears intended to address is already identified in Notifiable Transaction NT-2023-02, as designated by the Minister. That designation imposes a significant disclosure burden on taxpayers and their advisors, supported by substantial penalties for non-compliance. In addition, the CRA has repeatedly stated that the arrangement described in NT-2023-02 is subject to the general anti-avoidance rule, which now carries a penalty and extended reassessment period. Taken together, these measures already provide a strong deterrent against the transactions described in the Explanatory Notes accompanying the proposed amendment. In our experience, these combined compliance and enforcement measures have been effective, and taxpayers are generally no longer undertaking the types of transactions targeted by the amendment.

We would welcome the opportunity to discuss this matter with you in more detail and respond to any questions you might have,

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

Yours truly,

Richard Niedermayer, KC, TEP
Chair, STEP Canada

Kenneth Keung, CA, CPA, CPA (CO), CFP, MTAX, LLB, TEP
Chair, STEP Canada Tax Technical Committee