STEP Canada / Canada Revenue Agency Roundtable (2021)

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The following is the author's summary of the verbal answers given by the Canada Revenue Agency ("CRA") representatives to the following questions (as provided by STEP Canada) at the STEP Canada 23rd National Conference on June 15, 2021; official written answers will be published by the CRA in summer 2021.

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

For those hoping for guidance from the CRA on the new trust reporting requirements that have been proposed with application to taxation years ending on or after December 31, 2021, it was noted that the CRA declined to answer any questions on this subject, as they are unable to comment on proposed legislation.

QUESTION 1. Trust Residency and Departure Tax

If a Canadian resident inter vivos personal trust becomes a non-resident of Canada (because its central management and control has shifted to somewhere outside of Canada), this would cause the provisions of subsection 128.1(4) of the Act to apply. If the trust does not have liquidity to pay its "departure tax", its trustee(s) would likely seek to defer the amount owing by providing security pursuant to the provisions of subsections 220(4.5) – (4.54) (noting that the relief provided for in subsection 220(4.51) does not apply to a trust).

> a) From an administrative perspective, could the CRA provide its general comments on how it deals with security issues with a trust vs an individual?
>
> b) Because a Letter of Credit or a Letter of Guarantee carries a high continuing maintenance cost which results in these being impractical for most taxpayers, would the CRA consider a secured line of credit that it can draw on as adequate security?

ANSWER 1:

a) Per the CRA's Collections and Verification Branch, there is no practical difference between an individual and a trust in this scenario. Adequacy of security is determined based on the security provided and not the nature of the taxpayer.

b) There are several key differences between a letter of credit or guarantee and a line of credit (secured or otherwise). Letters of credit or guarantee are acceptable as security, as they are irrevocable and provide for payment to a single beneficiary (i.e., the CRA). In contrast, lines of credit are typically subject to conditions that make them less appropriate as security; for instance, they can be cancelled, and their terms do not generally allow third parties to draw on the line of credit. The CRA would not normally consider a line of credit to be adequate security. However, there are other acceptable forms of security. Taxpayers who will become non-resident should contact the CRA as soon as possible to discuss their options in this regard (1-877-301-3131 for calls within North America).

QUESTION 2. Interpretation of the Definition of "Arm's Length Transfer"

Section 94 of the Act is a provision designed to prevent the avoidance of tax on income which would otherwise be taxable in Canada, through the use of non-resident trusts. In general, if a Canadian resident contributes property to a non-resident trust (other than an "exempt foreign trust" as defined in subsection 94(1)), the trust is deemed under paragraph 94(3)(a) to be resident in Canada for a number of purposes. In addition, the contributor (other than an "electing contributor") to the trust and certain Canadian-resident beneficiaries of the trust may all become jointly and severally, or solidarily, liable to pay Canadian tax on the income of the trust.

Consider a situation in which a resident of Canada ("Father") makes a loan to a factually non-resident trust ("the Trust") six months after the settlement of the Trust. The terms of the loan, including the interest rate, are consistent with the terms of a demand loan between arm's length parties.

We note that the October 2012 Department of Finance Explanatory Notes state:

> Thus, for example, if any person receives a beneficial interest in a non-resident trust as a result of a particular transfer or loan of property or if it is reasonable to conclude that one of the reasons for the transfer was to facilitate the acquisition of such an interest, the transfer will not be an arm's length transfer.

Would CRA consider Father's loan to the Trust to be an "arm's length transfer" as defined by subsection 94(1), particularly when no trust beneficiary acquires an interest under the Trust as a result of this loan?

Consider the following facts:

- The settlor is, and has always been a non-resident;
- To date, the settlor is the only contributor to the Trust;
- The trustee (who is not the settlor, Father or a beneficiary) is a non-resident;
- The central management and control of the trust rests with, and is exercised by the trustee;
- The only beneficiaries of the Trust are the two children of Father. Both children are resident in Canada, and both were named beneficiaries in the trust deed when the Trust was settled;
- Father has always been resident in Canada; and
- Father and the trustee entered into an enforceable contract regarding the terms and conditions of the loan.

ANSWER 2: Note that the definition of "arm's length transfer" in subsection 94(1) has two paragraphs, but only the interpretation of paragraph (a) is considered for the purposes of this scenario. In the CRA's view, the test under paragraph (a) does not require that the beneficiary must acquire an interest in the trust as a result of the transfer; rather, it is sufficient if the beneficiary's existing or future interest in the trust motivates the transferor to make the transfer.

There must be no connection between the beneficial interest and the purpose of the transfer. In this scenario, although the terms of the loan are similar to the terms that an arm's length lender would accept, it may be that Father is making the loan because of the children's interests as beneficiaries of the trust. Note that paragraph (a) specifically refers to consideration all of the circumstances (i.e., it is a question of fact). In this scenario, the CRA is of the opinion that the loan from Father would likely not constitute an arm's length transfer, because it is highly likely that Father is making the loan because of the children's interests in the trust.

QUESTION 3. Reasonable Return on Promissory Note Issued by Family Trust

A family trust can distribute its income to a beneficiary by making an amount payable in the year to the beneficiary, provided the beneficiary is entitled in the year to enforce payment of it (as per the requirements of subsection 104(24) of the Act). If the amount payable to the beneficiary is in the form of an interest bearing promissory note owing to the beneficiary, the beneficiary will report interest income for each year the promissory note remains outstanding. Assuming the beneficiary is not a minor and has not performed any work, has not contributed any property or assumed any risk with respect to any related business owned directly or indirectly by the trust, would the beneficiary be able to rely on the "reasonable return" exception in either subparagraph (f)(ii) or (g)(ii) of the definition of "excluded amount" in subsection 120.4(1) if the interest rate is equivalent to an interest rate that would have been charged between parties dealing at arm's length with each other?

ANSWER 3: We need to first consider the definitions of "specified individual" and "split income" in subsection 120.4(1) to determine if the tax on split income ("TOSI") rules in section 120.4 of the Act are engaged. (All definitions referred to in this answer are set out in subsection 120.4(1).) In this case, the interest income is likely split income, as paragraph (d) of the definition applies to interest in respect of a debt obligation of a trust. If the interest income is derived from a "related business", then the TOSI will apply unless it is an "excluded amount". The exception in subparagraph (f)(ii) of the definition of "excluded amount" would not apply, as there has been no contribution of arm's length capital by the beneficiary, but the exception in subparagraph (g)(ii) might apply. Whether the interest represents a "reasonable return" is a question of fact. However, the CRA generally will not substitute its judgment for what is a reasonable return where the taxpayers have made a good faith attempt to determine a reasonable return based on the criteria set out in paragraph (b) of that definition.

QUESTION 4. TOSI on Dividends

Tom, Dick and Harry are brothers and Canadian residents. Many years ago they pooled their savings and incorporated TDH Co, a Canadian private corporation. Each owns 1/3 of the issued shares of the corporation. TDH Co owns three rental properties known as T, D and H. Each have equal value. The brothers live primarily on the dividend income of TDH Co and receive around $100,000 per year each. The brothers have never been active in managing TDH Co, which engages an outside arm's length property management company to manage the properties. The initial capital was repaid many years ago.

a) Does the CRA agree that dividends received by Tom, Dick and Harry are subject to TOSI?

b) If a butterfly reorganization was done to split the corporation into 3 equal parts where Tom, via a corporation, owned T, Dick, via a corporation, owned D, and Harry, via a corporation, owned H, would dividends received by Tom, Dick and Harry, as the case may be, thereafter be subject to TOSI?

ANSWER 4: For the purposes of this answer, the CRA has assumed that each of Tom, Dick and Harry are at least 25 years old and hold at least 10% of the issued shares of TDH Co (i.e., representing at least 10% of the voting shares and 10% of the fair market value of all of the issued shares of TDH Co). All definitions referred to in this answer are set out in subsection 120.4(1).

a) If the shares of TDH are "excluded shares", any dividends paid on those shares would be an "excluded amount" not subject to the TOSI. The CRA has previously commented that where the level of activity is insufficient to constitute a business, the excluded shares exception (subparagraph (g)(i) of the definition of "excluded amount") cannot apply. In this case, if the level of activity is sufficient to constitute a business, the excluded shares exception would apply. If not, subparagraph (e)(i) of the definition of "excluded amount" would apply, as the dividends are not derived directly or indirectly from a related business.

b) The analysis would essentially be the same after the reorganization.

QUESTION 5. Income Attribution from Alter Ego Trust

A taxpayer settles an alter ago trust and contributes property to the trust. In general, the income of an alter ego trust attributes to the settlor because subsection 75(2) of the Act applies to the trust.

Are there any exceptions to this (i.e., types of income that would not attribute)? For example, consider the following independent scenarios:

a) The property transferred is an interest in a limited partnership and the trust is allocated business income.

b) The trust realizes a capital gain, reinvests the proceeds and realizes another capital gain.

c) The trust earns income, reinvests the income and earns income on the reinvestment (second generation income).

For each scenario above, could the CRA comment on the possible application of subsection 75(2) to that type of income?

ANSWER 5: Note that subsection 75(2) will generally apply if a trust, that is resident in Canada and that was created in any manner whatever since 1934, holds property on condition (a) that it or property substituted therefor may (i) revert to the person from whom the property or property for which it was substituted was directly or indirectly received (referred to as "the person"), or (ii) pass to persons to be determined by the person at a time subsequent to the creation of the trust, or (b) that, during the existence of the person, the property shall not be disposed of except with the person's consent or in accordance with the person's direction. If any of these conditions are met, any income or loss from the property or from property substituted for the property, and any taxable capital gain or allowable capital loss from the disposition of the property or of property substituted for the property, is attributed to the person while he or she is alive and resident in Canada.

a) Business income or loss will not be attributed to the settlor, as subsection 75(2) does not apply to income or losses from a business. However, the terms of an alter ego trust must require that the settlor is entitled to receive all of the income of the trust during his or her lifetime. Therefore, any business income of the trust will still be included in the settlor's income under subsection 104(13) and will be deemed to be trust income under subsection 108(5). Further, any property income earned by the partnership and allocated to the trust will be attributed to the settlor under subsection 75(2), and if such income is a dividend, subsection 82(2) will deem such dividend to have been received by the settlor such that it will retain its character for the purposes of the Act.

b) Proceeds received on a disposition of property contributed by the settlor would be substituted property. Similarly, investments acquired with such proceeds would be substituted property, meaning any income from such investments would be attributed to the settlor under subsection 75(2). This will continue to apply to future substituted property, no matter how often the substituted property is disposed of and reinvested.

c) Any second generation income or loss would not be attributed to the settlor under subsection 75(2), as it is not earned on property contributed to the trust by the settlor or property substituted therefor. However, as above, the second generation income will be included in the settlor's income under subsection 104(13) and will be deemed to be trust income under subsection 108(5), unless the trust makes a designation to retain the original character of such income (e.g., under subsection 104(19) or (21)).

QUESTION 6. Vested Indefeasibly

A trust in which all interests have vested indefeasibly is excluded from the scope of the 21-year deemed disposition rule in paragraph 104(4)(b) of the Act. This result arises from the definition of "trust" in subsection 108(1) of the Act. It is noted that other conditions apply under paragraph (g) of that definition, such that in order for a trust to qualify for the exclusion, the trust cannot be described in subparagraphs (g)(i) to (vi) of the definition of "trust" - for example, subparagraph (iv) stipulates that not more that 20% of the total value of all interests of a trust that is resident in Canada may be held by non-resident beneficiaries.

> a) Can the CRA provide clarity as to what is required to meet the condition that all interests in the trust have vested indefeasibly?
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> b) How is this disclosed on the trust return for the trust?
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> c) What are the tax implications when a beneficiary resident in Canada holds an interest which has vested indefeasibly, and the beneficiary dies?

ANSWER 6:

a) Refer to the CRA's response to Question 9 of the May 2018 STEP Canada Roundtable (CRA Views 2018-0744111C6); the comments set out therein continue to apply. Whether an interest has vested indefeasibly is a question of fact and law, as is the question of whether the trustee has the power to vest trust interests indefeasibly.

Cancelled Interpretation Bulletin IT-449R provided the statement that "vested indefeasibly refers to the unassailable right to ownership of a particular property" and "…that such right cannot be defeated by any future event, even though that person may not be entitled to the immediate enjoyment of all the benefits arising from that right." For an interest in a trust to vest indefeasibly in a beneficiary of the trust, the situation must be such that that the beneficiary can be ascertained and that there is no condition precedent to the beneficiary holding such trust interest. Further, there must be no condition subsequent, or possible future event or limitation that could revoke, limit or defeat the beneficiary's interest in the trust.

Where none of the exceptions in subparagraphs (g)(i) through (vi) of the definition of "trust" in subsection 108(1) apply and it is clear in law that interests have vested indefeasibly since inception or where a trust gives the trustees the power to indefeasibly vest the interests in the trust and they lawfully do so before the 21st anniversary date specified in subsection 104(4), the 21-year deemed disposition rule will not apply.

b) There is no place on the T3 return to disclose that all trust interests have vested indefeasibly. Trustees may submit a note explaining that all interests have vested indefeasibly and may attach a nil return. The CRA will consider making updates to the T3 Guide if there are standard steps they want trustees to take in this regard.

c) For the purposes of the deemed disposition of the beneficiary's interest in the trust under paragraph 70(5)(a) of the Act, the fair market value of such interest would be determined with reference to subsection 107.4(4) of the Act.

QUESTION 7. Subsection 107(2) and Trust to Trust Transfers

A discretionary family trust, a personal trust resident in Canada, (the "Trust") is settled by Mr. X. The beneficiaries of Trust are the children of Mr. X (the "Beneficiaries"). The trust agreement (the "Trust Agreement") gives the trustees the power to distribute income or capital of the Trust to or for the benefit of the Beneficiaries. The Trust Agreement does not contemplate that a trust created for the benefit of the Beneficiaries could be added as a beneficiary nor does it provide that a trust for the benefit of the Beneficiaries is a beneficiary of Trust.

The trustees of Trust intend to distribute the property of Trust to a newly created trust (the "New Trust") which has been settled for the benefit of the Beneficiaries, on a tax deferred basis pursuant to subsection 107(2) of the Act. None of subsections 107(2.001), and (4) to (5) are applicable to deny the application of subsection 107(2) to any distributions from Trust.

Can the CRA confirm that subsection 107(2) will apply to the transfer of the property from Trust to New Trust?

ANSWER 7: Subsection 107(2) generally applies where property is distributed by a personal trust to a beneficiary in satisfaction of the beneficiary's capital interest in the trust, provided none of the exceptions noted above apply. For the purposes of subsection 107(2), "beneficiary" is defined in subsection 108(1) to include a person "beneficially interested" in a trust, as defined in subsection 248(25). Paragraph (a) of that definition provides that a person or partnership beneficially interested in a particular trust includes any person or partnership that has any right (whether immediate or future, whether absolute or contingent or whether conditional on or subject to the exercise of any discretion by any person or partnership) as a beneficiary under a trust to receive any of the income or capital of the particular trust either directly from the particular trust or indirectly through one or more trusts or partnerships. In other words, a person must have some right as a beneficiary to be considered "beneficially interested" in a trust. Although the term "beneficiary" is not defined for the purposes of subsection 248(25), the CRA considers this term to have its ordinary meaning. In this scenario, the beneficiaries of the Trust do not include another trust. Therefore, subsection 107(2) would not apply, since New Trust is not a beneficiary. However, consideration could be given to the potential application of paragraph (f) of the definition of "disposition" in subsection 248(1) or subsection 107.4(3), neither of which have been specifically addressed here.

QUESTION 8. Income Tax Rulings Directorate – Remissions

The fees charged by the CRA for providing an advance income tax ruling or a supplemental ruling (a Ruling), and a consultation in advance of a Ruling (a Pre-ruling Consultation), are governed by the *Service Fees Act*.[1]

In accordance with section 7 of the *Service Fees Act*, a reduction of a fee (a remission) is required where the CRA considers that a service standard has not been met.

Can the CRA describe how a remission will be determined with respect to the fees charged for Rulings and Pre-ruling Consultations?

ANSWER 8: See Information Circular IC 70-6R11 ("IC 70-6") for detailed information on processes and requirements for advance rulings; the latest version was issued on April 1, 2021. The service standard for an advance income tax ruling is 90 business days commencing with the receipt of all information required from the requestor as outlined in IC 70-6. The service standard for a pre-ruling consultation is within 15 business days from the date the requestor receives confirmation that the pre-ruling consultation request has been accepted as outlined in IC 70-6. It may not always be possible to meet these service standard targets, in which case the directorate will inform the taxpayer in advance and establish an alternate mutually agreed upon service target date. Where the service target date is not met, a remission of the service fee will apply, in accordance with the calculation set out in Appendix "H" of IC 70-6.

QUESTION 9. Safe Income Computation

CRA's Income Tax Technical News No. 37 released in 2008 sets out the CRA's position that non-deductible expenses must be deducted in computing safe income on hand. However, non-

[1] S.C. 2017, c. 20, s. 451.

deductible expenses for purposes of the safe income on hand calculation are not explicitly defined. In addition, the phrase "non-deductible expenses" is not defined within subsection 55(5) of the Act. Accordingly, can the CRA provide a definition of non-deductible expenses for the purposes of section 55?

ANSWER 9: For the purposes of section 55, safe income is income earned or realized after 1971 and before the applicable safe income determination time, and safe income on hand is safe income that can reasonably be considered to contribute to a capital gain on a share. Non-deductible expenses are any expenses incurred or disbursements made that were not deductible in calculating net income for tax purposes. In Income Tax Technical News No. 37, the CRA stated that safe income on hand must be reduced to reflect cash outflows (such as non-deductible expenses), which are not deducted in the computation of the corporation's net income for tax purposes but still have the effect of reducing the amount of disposable after-tax income. Note that this would not include outlays for an acquisition of property or repayment of the principal amount of a loan. Examples of such cash outflows include dividends paid or payable, taxes (including refundable taxes), interest and penalties, charitable donations, and the non-deductible portion of certain expenses (e.g., meals and entertainment expenses). See also CRA Views 2016-0672321C6, which states that contingent payments should also be taken into account.

QUESTION 10. Acquisition of Control

The hypothetical fact situation is described as follows: ACo, BCo and CCo are Canadian-controlled private corporations. All of the issued and outstanding shares of ACo are owned equally by BCo and CCo. BCo and CCo are not related under paragraph 251(2)(c), and deal at arm's length with each other. Neither BCo nor CCo controls ACo. ACo's taxation year ends on December 31 of each year.

At a particular time on November 1, 2020, ACo purchases for cancellation all of its shares owned by BCo for consideration that exceeds the aggregate paid-up capital of those shares, resulting in ACo being deemed to pay a dividend, as computed under subsection 84(3) ("Deemed Dividend") at that time, to BCo. ACo's acquisition of its own shares owned by BCo results in CCo acquiring control of ACo ("the AOC").

CCo's AOC of ACo is a "loss restriction event" (as defined in subsection 251.2(2)). Unless ACo elects for it not to apply, subsection 256(9) will deem CCo to have acquired control of ACo at the beginning of November 1, 2020, and not at the particular time of CCo's AOC of ACo on November 1, 2020, such that paragraph 249(4)(a) will deem ACo to have: (i) a deemed taxation year end immediately before the beginning of November 1, 2020, (i.e., the last moment of time on October 31, 2020), and (ii) a new taxation year commence at the beginning of November 1, 2020.

If an election is made for subsection 256(9) not to apply, paragraph 249(4)(a) will deem ACo to have: (i) a deemed taxation year end immediately before the particular time of the AOC on November 1, 2020; and (ii) a new taxation year commence at the particular time of the AOC on November 1, 2020.

ACo selects December 31, 2020 as the last day of its new taxation year ("New Taxation Year") to coincide with its previous practice.

Assuming that ACo was entitled to receive a dividend refund as computed under paragraph 129(1)(a), with respect to the Deemed Dividend, can the CRA please confirm its position as to whether the dividend refund to ACo is for the taxation year deemed to end by paragraph 249(4)(a), or the New Taxation Year, in the situation both where ACo elects for subsection 256(9) to apply to the AOC and where it does not.

ANSWER 10:

Scenario 1: no election under subsection 256(9); deemed year-end on October 31, 2020.

Scenario 2: election under subsection 256(9); deemed year-end on November 1, 2020.

In either case, the deemed dividend is considered to be paid by ACo in its New Taxation Year.

QUESTION 11. TFSA Over-contribution

A taxpayer moves to Canada in 2021 and opens a TFSA soon afterwards. Because he was previously non-resident, the taxpayer's TFSA contribution room for 2021 is only $6,000. Due to a misunderstanding of the TFSA rules, the taxpayer contributes $18,000 to his TFSA and invests it all in shares of one company. Before he has a chance to withdraw the $12,000 over-contribution, the company goes bankrupt and the value of the TFSA goes to zero.

How can the taxpayer stop the TFSA over-contribution tax or request a waiver of the tax under subsection 207.06(1) if he can no longer withdraw the over-contribution? Does he need to wait two years for new TFSA contribution room to open up?

ANSWER 11: The taxpayer would be subject to the 1% tax under section 207.02 of the Act on the amount of the over-contribution. This tax continues to apply while the excess amount remains in the TFSA. Since the individual is unable to withdraw any amount, subsection 207.06(1) cannot apply to mitigate the tax liability in this case. Therefore, the over-contribution can only be reduced when new contribution room becomes available in future years. Assuming new contribution room of $6,000 per year, the over-contribution will be reduced in 2022 and eliminated in 2023, and the section 207.02 tax will apply in 2021 and 2022; the taxpayer will be unable to make new contributions to the TFSA until 2024.

QUESTION 12. Joint Spousal or Common-law Partner Trust – Contribution of Jointly-held Property

Is it possible for spouses or common-law partners to jointly create a trust which meets the conditions set out in subparagraph 73(1.01)(c)(iii) of the Act with a contribution of property jointly-owned by the spouses or common-law partners? Further, is it possible for one or both spouses or common-law partners to make subsequent contributions to the trust on a tax-deferred basis with property that is owned jointly by the spouses or common law partners, and other property that is owned individually? Assume that both spouses or common-law partners have attained 65 years of age and are resident in Canada at all relevant times. Additionally, would paragraph 104(4)(a) apply in this particular situation?

ANSWER 12: If a trust is created by a contribution of jointly-held property by spouses or common-law partners, it will be considered to have been settled by both individuals for the purposes of subparagraph 73(1.01)(c)(iii) of the Act. Assuming all other conditions in that subparagraph are met, any subsequent transfers to the trust by either spouse or common-law partner would be eligible for the rollover under subsection 73(1). Note that paragraphs 104(4)(a) and 104(13.4)(a) will also apply to the trust to cause a deemed disposition and taxation year-end on the death of the last to die of the spouses or common-law partners.

QUESTION 13. Paragraph 104(13.4)(a) Deemed Taxation Year End for an Alter Ego Trust

Generally speaking, where the settlor of an alter ego trust dies, the trust is deemed to dispose of its capital property[2] at the end of the day of death, and to reacquire the property immediately after that day, pursuant to paragraph 104(4)(a) of the Act. Paragraph 104(13.4)(a) of the Act provides that on a death referred to in paragraph 104(4)(a), (a.1) or (a.4), the taxation year of the trust is deemed to end at the end of the day of death.

Does a deemed year end occur pursuant to 104(13.4)(a) where a trust that would otherwise be an alter ego trust makes an election under subparagraph 104(4)(a)(ii.1) to not have that subparagraph apply?

ANSWER 13: The preamble to subsection 104(13.4) considers the death of an individual referred to in paragraphs 104(4)(a), (a.1) or (a.4) in respect of a trust. Subsection 248(1) defines "alter ego trust" by reference to paragraph 104(4)(a) if that paragraph were read without reference to subparagraph 104(4)(a)(iii) and clauses 104(4)(a)(iv)(B) and (C). Pursuant to subparagraph 104(4)(a)(ii.1), a trust is not subject to paragraph 104(4)(a) if it is a trust the terms of which are described in clause 104(4)(a)(iv)(A) and the trust elects in its T3 return for its first taxation year that subparagraph 104(4)(a)(ii.1) not apply to the trust. In other words, a trust that would otherwise be an alter ego trust can elect out of this status in its first taxation year. If paragraph 104(4)(a) does not apply to the trust as a result of this election, the settlor's death would not be relevant for the purposes of subsection 104(13.4), and paragraph 104(13.4)(a) would not cause a deemed year-end on that date. However, any income arising in the trust prior to the death of the settlor would be taxed in the settlor's terminal T1 return. The subsection 73(1) rollover also would not apply, and the 21-year deemed disposition rule would apply under 104(4)(b). Note that no similar election is available for any other trusts referred to in paragraph 104(4)(a).

QUESTION 14. Extending the "Graduated Rate Estate" Period

Generally speaking, pursuant to subsection 248(1) of the Act, a "graduated rate estate" (GRE) of an individual at any time means the estate that arose on and as a consequence of the individual's death if:

i) that time is not more than 36 months after the death of the individual;

[2] The preamble of subsection 104(4) refers to "each property of the trust (other than exempt property) that was capital property (other than depreciable property) or land included in the inventory of a business of the trust".

ii) the estate is a "testamentary trust";[3]

iii) the individual's social insurance number is provided in estate's T3 Trust Income Tax and Information Return; and

iv) the estate designates itself as a GRE of the individual; and no other estate makes this designation in respect of the same individual.

Therefore, an estate may be a GRE for a maximum period of 36 months beginning from the date of death of the individual.

Consider a situation where an individual is a member of a pension plan which, upon the death of the individual, provides that a lump-sum pension benefit is payable to the estate of the deceased individual. Unfortunately, on occasion, these payments are received after the GRE status of the estate has expired. Consider a further complication whereby the lump-sum amount is received by the estate at the end of its taxation year and the executor is unable to distribute the income to the sole beneficiary before the end of the year. When this is the case, it would appear that the estate is not be able to calculate its tax payable using the graduated tax rates and the estate's income would be subject to the highest marginal tax rate for individuals.

Can the Minister, under circumstances where the late payment of the pension benefits is of no fault of the executor, extend the GRE status of the estate beyond the 36-month period? If not, is there any way the pension income could be taxed in the estate's 36-month GRE period?

ANSWER 14: Paragraph (a) of the definition of "graduated rate estate" in subsection 248(1) of the Act establishes the 36-month period and does not provide the Minister with any authority to extend this period, nor does this authority exist anywhere else in the Act. Pension benefits are included in income for the taxation year in which they are received. Although in this case the estate became eligible for the lump sum in the year of death, it cannot be reported until actually received. If it cannot be distributed in the year of receipt, it will be taxed in the estate. However, if the income is made payable to a beneficiary, it will be taxed in the beneficiary's hands and deductible to the estate. Consider subsection 104(24) of the Act, which requires that the beneficiary must have received payment or be entitled to enforce payment in the year for the income to be considered payable to the beneficiary. This will depend on the relevant terms of the Will and status of the state administration. If the executor determines that the beneficiary was entitled to enforce payment, the executor must issue a T3 slip to the beneficiary. Where certain conditions are met, subsection 104(27) of the Act allows a GRE to flow through pension benefits to a recipient beneficiary. However, this provision cannot be relied upon if the estate is no longer a GRE, and subsection 108(5) will apply to deem the income to be trust income.

QUESTION 15. Information on Trust Registration New Online Process

Can the CRA provide us with additional information about their new service which allows users to apply for a trust account number online?

[3] "testamentary trust" is defined in subsection 108(1) to mean, subject to certain exceptions, a trust that arose on and as a consequence of the death of an individual (including a trust referred to in subsection 248(9.1)).

ANSWER 15: As of February 2021, trustees and representatives can apply for trust account numbers online. The registrant must know the trust type and have a signed copy of the trust instrument and certain information about the trust and trustee. Once the request is submitted, the registrant will receive confirmation of registration and the trust account number. Note that this option is not available for a non-resident trust.