

STEP Inside

NEWSLETTER OF THE SOCIETY OF TRUST AND ESTATE PRACTITIONERS (CANADA)

STEP Canada's 27th Annual National Conference



THANK YOU SPONSORS



QSBC SHARES AND THE 24-MONTH HOLDING PERIOD REQUIREMENT

KATHERINE RATCLIFFE, JD, TEP
Linmac LLP; Member, STEP Calgary

The STEP Canada 2025 National Conference session “Practitioners’ Update: Canadian Tax Law” canvassed

recent changes and proposed amendments to, and new commentary from the Canada Revenue Agency (CRA) on, Canadian tax law of importance to trust and estate practitioners. The update included a summary of a March 2025 technical interpretation on the treatment of corporate shares disposed of by a personal trust.

In CRA document no. 2016-0662951E5 (March 28, 2025; in French), the CRA responded to a request for comment on the 24-month holding period requirement set out in paragraph (b) of the definition of “qualified small business corporation share” (“QSBC share”) in subsection 110.6(1) of the *Income Tax Act*.¹ The particular issue was whether the fact that a personal trust has been in existence for less than 24 months when it disposes of shares of a corporation prevents the shares from qualifying as QSBC shares.

In the hypothetical situation presented to the CRA, an individual (“Mr. X”) settled a personal trust (“the trust”). The sole beneficiaries of the trust were his children. After settling the trust, Mr. X transferred to it certain shares of a corporation (“the shares”), which he had held for more than two years prior to the transfer. Six months later, the trust sold the shares to an unrelated buyer. For the purposes of the hypothetical, it was assumed that all other requirements for each of the shares to be a QSBC share were met at that time. The CRA was asked whether paragraph (b) of the QSBC share definition, which generally requires that the shares not be owned by anyone other than the trust or a person related to the trust throughout the 24 months immediately preceding the disposition (“the holding period requirement”), would be met in this case.

¹ *Income Tax Act* (Canada), RSC 1985, c.1 (5th Supp.), as amended (“the Act”).

The CRA referred to subparagraph 110.6(14)(c)(ii) of the Act, which generally provides that, for the purposes of the QSBC share definition, a personal trust is deemed, in respect of shares of a corporation, to be related to the person from whom the trust acquired the shares if, at the time the trust disposed of the shares, all of its beneficiaries² (other than registered charities) were related to that person. In the hypothetical, Mr. X held the shares for two years before they were transferred to the trust, so the holding period requirement would be met by the trust if the trust and Mr. X were related. That should be the case, by virtue of subparagraph 110.6(14)(c)(ii), since the only beneficiaries of the trust when it disposed of the shares were Mr. X's children, who are related to him for the purposes of the Act.³ Accordingly, each of the shares should qualify as a QSBC share, such that the lifetime capital gains exemption could be claimed against capital gains realized on the disposition of the shares, provided that such capital gains became payable to one or more beneficiaries of the trust in the year of disposition and the appropriate designations were made in the trust's tax return for that year.⁴ The CRA confirmed that this result would not be affected by the fact that the trust had been in existence for less than 24 months at the time of disposition.

Interestingly, an individual is not considered to be related to himself or herself for the purposes of subparagraph 110.6(14)(c)(ii). Accordingly, it appears that if Mr. X were a beneficiary

of the trust, subparagraph 110.6(14)(c)(ii) could not apply. In that case, subparagraph 110.6(14)(c)(i), which generally provides that a personal trust is deemed to be related to a person for any period throughout which the person was a beneficiary of the trust, could apply to deem Mr. X to be related to the trust for the purposes of the QSBC share definition. Unfortunately, CRA document no. 2016-0662951E5 does not address this alternative fact pattern. Arguably, the holding period requirement could still be met, based on a generous interpretation of subparagraph 110.6(14)(c)(i) as a relieving measure. However, the CRA might apply a stricter interpretation of subparagraph 110.6(14)(c)(i) and insist that the trust would have to hold the shares for at least 24 months prior to their disposition to qualify as QSBC shares.

2 In CRA document no. 2002-0164995 (May 7, 2003), the CRA interpreted the reference to "all beneficiaries" in subparagraph 110.6(14)(c)(ii) to include only those persons named as beneficiaries at the time of disposition of the shares by the trust, noting that the broad definition of "beneficially interested" in subsection 248(25) of the Act does not apply, and confirming that a narrower interpretation is appropriate because subparagraph 110.6(14)(c)(ii) is a relieving measure. The CRA has not indicated whether its views on this point have changed in light of the Federal Court of Appeal's obiter comments in *Canada v. Propep Inc.* (2009 FCA 274), which the CRA has referenced in other contexts to extend the definition of "beneficially interested" to all uses of the term "beneficiary" in the Act. This is arguably incorrect, but readers should nevertheless be aware of this potential risk.

3 See paragraphs 251(2)(a) and 251(6)(a) of the Act.

4 See subsections 110.6(2.1), 104(13), 104(21), and 104(21.2) of the Act.