

Charitable contributions made as a form of advertising or to attract business from charities in the community may be regarded as business expenses deductible in full rather than as gifts subject to the 75% limitation (50% in 1996 and 20% for taxation years prior to 1996).

Where a taxpayer buys tickets for a fund-raising event involving an element of return in the form of entertainment, the taxpayer may deduct the amount paid minus the greater of the fair market value of the tickets and a reasonable part of the total cost of the event.³¹⁴

Split Gifts Rules

The original definition of "gift" had disqualified as a gift a transfer of property for partial consideration, notwithstanding that there is a clear gift element and donative intent, a result with which the government and the courts were not comfortable. Therefore, on June 26, 2013 (with retroactive effect from December 20, 2002), the Act was amended to permit split gifts. A corporation may now make a gift after December 20, 2002 and receive consideration of a lesser value without wholly disqualifying the gift for deduction.³¹⁵ If the advantage received as partial consideration for, or in gratitude for the gift does not exceed 80% of the fair market value of the gift, the corporation will be allowed a deduction equal to the fair market value of the gift less the advantage received. If the advantage exceeds 80% of the fair market value of the gift, the gift will not necessarily be disqualified if the corporation can establish that the transfer of property was made with a donative intent.³¹⁶

For more information on the new split gifts rules, see ¶3375.

¶3364] Donations that Cannot Be Deducted

The following donations cannot be deducted:

- (1) Donations to individuals.
- (2) Court-ordered transfers of property to charities.
- (3) Gifts of services (for example, donated time, labour).
- (4) Gifts of promises (for example, gift certificates donated by the issuer, hotel accommodation).
- (5) Pledges.
- (6) The value of merchandise where its cost has been charged as an expense of a business.

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³¹⁴ Interp. Bul. IT-110R3.
³¹⁵ Sec. 248(30).

³¹⁶ Sec. 248(32).

(7) Amounts paid for card parties, bingos, and lotteries, even where such activities may be held for the benefit of charity. It is the CRA's view that participants in lotteries, while perhaps influenced in choosing which lottery they will participate in by the identity of the organizing charity, are primarily motivated by the chance to win the significant prizes that are offered. Therefore, in some cases, while there may be an element of donative intent, the amount of the advantage cannot be reasonably quantified. Accordingly, it continues to be the CRA's view, after the coming into force of the new split gifts rules (after December 20, 2002), that no part of the cost of a lottery ticket is a gift which may be receipted for income tax purposes.

(8) The payment of a basic fee for admission to an event or to a program.

(9) The payment of membership fees that convey the right to attend events, receive literature, receive services, or be eligible for entitlements of any material value that exceeds 80% of the value of the payment.

(10) A donation for which the fair market value of the advantage or consideration provided to the donor exceeds 80% of the value of the donation.

(11) A gift in kind for which the fair market value cannot be determined.

(12) Donations provided in exchange for advertising/sponsorship.

(13) Loans of property.

(14) Use of timeshare.

(15) The lease of premises.

(16) Donations subject to a direction by the corporation that they benefit a particular person or family or a non-qualified donee such as a foreign charity.³¹⁷

¶3365] Registered Charities and Canadian Amateur Athletic Organizations

In order to obtain a deduction for donations to these organizations, the organization must be devoted to the specified activity and no part of its income can be available for the personal benefit of any proprietor, member, or shareholder. In addition, the organization must have registered with the CRA. Where there is any doubt as to whether a charity has registered, and the deductibility of the donation is a prime consideration, it would be

See page ii for explanation of footnotes.

³¹⁷ Interp. Bul. IT-110R3.

advisable to discuss this matter with the organization's officials before contributing.

¶3366 Returns, Records and Receipts

Registered charities and Canadian amateur athletic organizations are required to keep records and books of accounts. This includes a duplicate of each receipt for a donation received. The records must contain sufficient information to enable the donations to be verified.³¹⁸ Each receipt must contain a statement that it is an official receipt³¹⁹ for income tax purposes. Donations are deductible only if supported by official receipts.

¶3367 Contents of Receipts

Each donation receipt issued by a registered charity and Canadian amateur athletic organization should indicate the organization's registration number.³²⁰ It is a requirement for donations to foreign universities that they be receipted by serialized receipts showing the name and address of both the donor and the recipient, the place of issue of the receipt, the amount of the donation, the year in which the donation was received, and a signature authorized by the recipient.

¶3368 Crown Gifts

Gifts to the Government of Canada, a Canadian province, or a territory are now subject to the same limits as any other charitable donations (see ¶3361). This means the amount deductible by a corporation in respect of Crown gifts is limited to 75% of the corporation's income, plus, for gifts of capital property, (i) 25% of the taxable capital gain arising from the gift and taken into income in the year and (ii) 25% of the lesser of any recapture of capital cost allowance on the property included in the taxpayer's income in the year and the property's capital cost or proceeds of disposition.³²¹

If, in any one year, the amount in respect of Crown gifts is not deducted (e.g., the corporation's income is too low to absorb it), the corporation may carry forward the undeducted amount to the next five years. The amount of Crown gifts carried forward from a preceding taxation year must be claimed before claiming any gifts made in the current taxation year. This deduction has also been updated to reflect "split gifts" (see ¶3363 above).

Heritage Canada Foundation, a registered charity, has been specially authorized to receive gifts in trust for the federal Crown, so gifts to Heritage Canada are now limited to 75% of the corporation's income for the year.

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³¹⁸ Reg. 3501.

³²⁰ Reg. 3501.

³¹⁹ Reg. 3500.

³²¹ CCH ¶15,754; Sec. 110.1(1)(b); Interp. Bul. IT-297R2.

¶3369 Gifts of Cultural Property to Institutions

A corporation is allowed a deduction for the fair market value of gifts (other than ecological gifts) of cultural property made to institutions designated under the *Cultural Property Export and Import Act*. The gift must be one that the Canadian Cultural Property Export Review Board has determined meets all of the criteria in paragraphs 29(3)(b) and 29(3)(c) of the *Cultural Property Export and Import Act*. The deduction is to be made from income, if any, remaining after claiming deductions for charitable donations (see ¶3361) and gifts to the Crown (see ¶3368). Amounts not deducted in a given taxation year may be carried forward for up to five years.³²² This deduction has also been updated to reflect split gifts (see ¶3363 above).

The fair market value of a gift of cultural property is the fair market value as determined by the Canadian Cultural Property Export Review Board, and such value is deemed to be the fair market value of the cultural property for two years from the date of determination.³²³ A taxpayer may appeal the determination of the fair market value to the Tax Court of Canada. A taxpayer may be assessed beyond the normal assessment period for amounts arising from the redetermination of the fair market value of a cultural property.³²⁴

¶3370 Gifts of Ecologically Sensitive Land

A corporation may deduct the fair market value of a gift of land that has been certified by the Minister of the Environment (or a person designated by that Minister) to be ecologically sensitive, the conservation and protection of which is important to the preservation of Canada's environmental heritage.³²⁵ This deduction has also been updated to reflect split gifts (see ¶3363 above).

Donations of ecologically sensitive land are not subject to the income limits for charitable gifts described in ¶3361. As well, any unused deduction may be carried forward up to five years. The deduction for a donation of ecologically sensitive land is made after deductions for charitable gifts (¶3361), Crown gifts (¶3368), and cultural gifts (¶3369).

Ecologically sensitive land, including a covenant, easement, or servitude must be certified by the Minister of the Environment or a person designated by the Minister. An Environment Canada Information Circular, "Ecological Gifts", sets out a list of certification authorities for various regions of the country, and outlines the national general criteria for ecologically sensitive land.

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³²² CCH ¶15,756; Sec. 110.1(1)(c).

³²⁴ CCH ¶18,367; Sec. 118.1(11).

³²³ CCH ¶18,365; Sec. 118.1(10).

³²⁵ CCH ¶15,756a; Sec. 110.1(1)(d).

Land that qualifies must be under private title; therefore, a corporation cannot donate leased rights of use. If a parcel of land that is donated contains ecologically sensitive land, the entire parcel will be considered to be ecologically sensitive land.

The land must be donated to a registered charity approved by the Minister of the Environment or to one of its provinces or territories, or a "municipality" [or for gifts made after May 8, 2000, a municipal or public body performing a function of government in Canada]. The Minister of the Environment, or a person designated by that minister, has to certify that the land is important to the preservation of Canada's environmental heritage. The Minister will also determine the fair market value (FMV) of the gift.

For a gift of a covenant or an easement, or a real servitude (in Quebec), the FMV of the gift will be the greater of:

- (1) the FMV of the gift otherwise determined; and
- (2) the amount of the reduction of the land's FMV that resulted from the gift.³²⁶

Gifts of ecologically sensitive land to public charities were subject to only 50% of the capital gains tax up to May 2, 2006 and have been completely tax-free since then.³²⁷ This special tax treatment does not apply to gifts to private foundations.

¶13372 Granting of Options to Charities and Other Qualified Donees

If a corporation grants an option to acquire property to a charity (or other qualified donee) after March 21, 2011, no charitable donation deduction will be allowed until such time that the option is exercised so that the property is acquired by the donee. The deduction allowed at that time will be based on the amount by which the fair market value of the property at that particular time exceeds any consideration paid for the property. As a result of split gift rules (see ¶13363), a deduction will generally not be available if the consideration paid by the donee for the property exceeds 80% of its fair market value at the time of acquisition.

In effect, an option granted by a corporation to a qualified donee after March 21, 2011 is not deductible as a charitable donation unless the option is subsequently exercised (at a particular time) so that the property is disposed of to the qualified donee, and either

- (1) 80% of the fair market value of the property at the particular time exceeds the total amount paid by the qualified donee to acquire the option and underlying property; or

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³²⁶ CCH ¶15,770a; Sec. 110.1(5).

³²⁷ CCH ¶6007; Sec. 38(a2).

- (2) the CRA is satisfied that the granting of the option was made with a donative intent.³²⁸

At the time of exercise of the option, the corporation is deemed to have disposed of the property for proceeds equal to its fair market value. It is also entitled, in the year in which the option is exercised, to a charitable donation deduction equal to that fair market value minus the total amount paid by the qualified donee to acquire the option and the underlying property. This deduction is permitted notwithstanding that the disposition of a property as a result of the exercise of the right of an option holder may not be a gift at law.³²⁹

If the option to acquire a corporation's property is subsequently disposed of (at a particular time) by a qualified donee, the corporation is deemed to have disposed of another property for proceeds equal to the lesser of the fair market value of any consideration received by the qualified donee for the option and the fair market value of the property that was the subject of the option. The permitted deduction for the taxation year in which the option was disposed of by the qualified donee is then equal to the proceeds of disposition (as calculated above) minus any consideration paid, if any, by the qualified donee to acquire the option.³³⁰

¶13373 Returned Gifts

After March 21, 2011, a corporation cannot retain tax assistance in the form of a charitable donation deduction in respect of property transferred to a qualified donee if the property is returned. In such a case, no gift is recognized and if the returned property is identical to the transferred property, the returned property is deemed to be the transferred property. If the returned property is not identical, the corporation is deemed to have disposed of the transferred property at the time of its return for consideration that is the returned property. For returned property in excess of \$50, an information return must be filed within 90 days of the return.

These measures address situations where an official donation receipt has been issued by a qualified donee in respect of the transfer of property by a corporation and an identical or substituted property has subsequently been returned to the corporation.³³¹ In such a case and irrespective of whether the transferred property was a gift, the corporation is deemed not to have disposed of the original property at the time of the transfer nor to have made a gift.³³² If the returned property is identical to the original property, the returned property is deemed to be the original property, such that a future disposition of the returned property will have the same result

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³²⁸ Sec. 110.1(10), 110.1(11).

³³¹ Sec. 110.1(14).

³²⁹ Sec. 110.1(12).

³³⁰ Sec. 110.1(13).

³³² Sec. 110.1(15)(a).

as if the property had never been disposed of to the qualified donee.³³³ If the returned property is only substituted property, the original disposition is not recognized but the corporation is considered to have disposed of the original property for consideration that is the returned property, and at the time that the property is returned to the corporation.³³⁴ If the fair market value of the returned property exceeds \$50, the qualified donee who has already issued an official donation receipt at the time of original transfer of property is required to file an information return within 90 days of the subsequent return of that property or substituted property and send a copy to the corporation.³³⁵ The CRA may reassess the return of income of any person to the extent that the reassessment can reasonably be regarded as relating to a return of property from a qualified donee.³³⁶

These new provisions apply to transfers of property made after March 21, 2011, except that an information return required that is filed before the day that is 90 days after August 16, 2011 is deemed to have been filed on time.

[¶3374] Donation of Medicines for the Developing World

After March 18, 2007, a corporation giving medicines from its inventory may claim a special additional deduction equal to the lesser of the cost of those medicines and 50% of the excess of their fair market value over their cost.³³⁷ The special deduction is only available if the gift qualifies as an eligible medical gift. Any amount not claimed in the year the gift is made may be carried forward for up to five years. To be considered eligible, the gift must meet the following conditions:

- (1) It must be made for charitable activities outside Canada.
- (2) Beginning July 1, 2008, it must be donated at least six months prior to the expiration date of the medicine (prior to this change, medicines meeting the requirements of the *Food and Drugs Act* were eligible for this deduction, even if the expiry date of the medicines was imminent). In this regard the six-month period does not modify the World Health Organization Guidelines (the WHO Guidelines) requirement that donated drugs should generally have a shelf-life of 12 months when received by the recipient country.
- (3) After October 2, 2007, it must meet the requirements of the *Food and Drugs Act*, and not be a food, cosmetic, medical device, natural health product, or veterinary drug (if made before October 3, 2007, the gift must be medicine).

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³³³ Sec. 110.1(15)(b).

³³⁴ Sec. 110.1(15)(c).

³³⁵ Sec. 110.1(16).

³³⁶ Sec. 110.1(17).

³³⁷ CCH ¶15,752; Sec. 110.1(1)(a.1).

(4) It must be part of the corporation's inventory.

(5) On or after July 1, 2008, it must be made to a registered charity that, in the opinion of the Minister of International Cooperation (or the Minister responsible for the Canadian International Development Agency (CIDA), if there is no such Minister) meets the conditions prescribed by regulation (gifts made prior to July 1, 2008 must be made to a registered charity that has received a disbursement under an international assistance development program of CIDA).³³⁸

This deduction has also been updated to reflect split gifts (see ¶3363 above). The prescribed conditions a registered charity must meet include the registered charity acting in a manner consistent with the principles and objectives of the WHO Guidelines, having sufficient expertise in delivering medicines, as well as in designing, implementing, and monitoring an international development assistance program (or, if applicable, an international humanitarian assistance program), and delivering the medicine received outside Canada or transferring it to another registered charity that also meets the conditions set out in the regulation. The registered charity is also required to make an application to the Minister for a determination of whether the conditions have been met.³³⁹

[¶3375] Gifts of Capital Property

Rules are provided for determining the amount of the deduction for donations of capital property.³⁴⁰ These rules apply to capital property donated as a charitable gift, a Crown gift, or an ecological gift. They also apply, in the case of a non-resident corporation, to a donation of Canadian real property to a prescribed donee. In the latter case, the donee must provide a satisfactory undertaking that it will hold the property for use in the public interest. To date, the only prescribed donee is the Nature Conservancy, a charity established in the United States. The following two additional conditions must be met for these rules to apply:

- (a) the fair market value of the property must exceed the amount of the advantage in respect of the gift (see ¶3363 above); and
- (b) the making of the gift must be proved by filing receipts containing prescribed information with the Minister.

The corporation is entitled to designate an amount not greater than the fair market value and not less than the advantage amount in respect of the property as its proceeds of disposition and the amount of its gift. The amount that a corporation will want to designate will depend on its particular situation,

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³³⁸ CCH ¶15,770d, ¶15,770g; Sec. 110.1(8), ³⁴⁰ CCH ¶15,765; Sec. 110.1(3); Reg. 3504; Interp. Bul. IT-288R2.

³³⁹ Reg. 3505(1).

60-month period that ends at that time, more than 50% of the fair market value of the share or interest was derived directly or indirectly from one or any combination of

- (i) real or immovable property situated in Canada,
- (ii) Canadian resource properties,
- (iii) timber resource properties, and
- (iv) interests and options in respect of such properties.

Recent legislative amendments have tightened up this definition to ensure that in determining whether the fair market value of the share or interest is derived from such properties, one does not take into account any value derived through a corporation, partnership, or trust the shares or interests in which were not themselves taxable Canadian property.

(5) After March 4, 2010, a share of the capital stock of a corporation that is listed on a designated stock exchange, a share of the capital stock of a mutual fund corporation, or a unit of a mutual fund trust, if at any time during the 60-month period that ends at that time,

- (i) 25% or more of the issued shares of any class of the capital stock of the corporation, or 25% or more of the issued units of the trust, were owned by or belonged to the taxpayer and persons with whom the taxpayer did not deal at arm's length, and
- (ii) more than 50% of the fair market value of the share or unit was derived directly or indirectly from one or any combination of properties described under items (4)(i) to (iv) above.

(6) An option or interest in any of the above properties.

The above-noted capital gains and capital losses do not include any gain or loss from a disposition of a taxable Canadian property that is a "treaty-protected property".¹⁰⁷ This rule ensures that a non-resident's capital loss from the disposition of a treaty-protected property (meaning that, had the property been sold at a gain, it would not have been subject to tax in Canada by virtue of an income tax treaty) does not offset taxable capital gains of the non-resident from other capital properties whose gains are not treaty-protected.

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¹⁰⁷ CCH ¶28,312; Sec. 248(1) "treaty-protected property".

¶15100 Distinguishing between Business Income and Capital Receipts

¶15105 Major Factors Involved

The definitions of capital gain and capital loss in the present Act do not spell out a distinction between a gain or loss that is a capital gain or loss and one that is ordinary business income. It is therefore necessary to look to the ever-evolving body of case law to provide the guidelines in determining whether a gain or loss on the disposition of property is on income or capital account. "Business" is defined¹⁰⁸ as including an adventure in the nature of trade. As a result, a transaction undertaken in isolation from a taxpayer's normal occupation may still be taxed as business income rather than as a capital gain.¹⁰⁹ The question of capital receipt versus business income arises frequently in transactions dealing with real estate¹¹⁰ (see ¶15110) and is decided based on the circumstances of each case.

While it is often difficult to distinguish between a capital gain and business income in particular circumstances, there appear to be certain factors that the Courts have considered in determining whether a taxpayer has realized an investment (capital receipt) or has been carrying on a business (income receipt) when engaging in a particular transaction. The Courts look at the taxpayer's whole course of conduct not only prior to and during the taxation year, but also in the period following it.¹¹¹ In examining the taxpayer's whole course of conduct, the following factors are taken into consideration:

- (1) intention;
- (2) the relation of the transaction or transactions to the taxpayer's regular business;
- (3) the nature of the transaction and the type of asset being disposed of;
- (4) the number and frequency of similar transactions; and
- (5) in the case of corporations, the declared objects of the corporation.

It has been held that in the absence of a specific provision in the Act bringing a receipt into income, a receipt which is on account of capital for accounting purposes will also be a capital receipt for income tax purposes.¹¹²

(1) *Intention*. In examining the taxpayer's course of conduct, the courts, among the different factors considered in the cases at law in which income versus capital gain is involved, always direct their research to the taxpayer's

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¹⁰⁸ CCH ¶28,024; Sec. 248(1) "business"; Interp. Bul. IT-459.

¹¹⁰ Interp. Bul. IT-218R.

¹¹¹ Rosenblat, 55 DTC 1205.

¹⁰⁹ Bakos, 84 DTC 1509, Papley, 84 DTC 1562.

¹¹² Consumers' Gas Co., 87 DTC 5008.

intention. In substance, it is the only factor. All other factors indeed (relation of transaction to taxpayer's business, number and frequency of similar transactions, the length of the period of ownership, the nature of transactions and assets involved, the corporation's object, etc.) are studied inasmuch as they are significant to the taxpayer's main intention and secondary intention.¹¹³

An individual taxpayer and a corporation controlled by the taxpayer were held to be trading in shares since their intention was primarily speculative.¹¹⁴ If an asset is purchased for investment purposes and is later sold out of necessity, then it would appear that the transaction entered into is not an adventure in the nature of trade and the resulting profit would be a capital receipt.¹¹⁵ A distinction may be drawn between an intention to resell that is definite and one that is vague or indefinite. The former may very well be conclusive evidence that the transaction was entered into in a spirit of enterprise, whereas the latter may be quite consistent with the idea of investment. A taxpayer acquired 15 to 20 horses as a hobby and one which turned out to have potential for racing was later sold at a profit. The Court held that at the time of purchase there was no secondary intention of selling for a profit and the profit was therefore a capital gain.¹¹⁶

If property is bought for investment, a profit on its resale might still be considered taxable as income if it was apparent that from the outset there was also a secondary intention to resell at a profit; thus, for example, a taxpayer who bought a timber licence as a hedge against inflation and resold it two years later without working it, was found to have realized an income profit.¹¹⁷ Similarly, where a company acquired a coal mine which remained unproductive for nine years and then resold it, the profit was held to be income.¹¹⁸ Again, if the circumstances surrounding the resale indicate that there was a profit-making scheme, the profit would be considered to be income. Thus, where two associates purchased some land for a shopping centre and apartment house project, transferred the land to two of their own private companies in exchange for shares, and subsequently sold their shares, the profit was held to be taxable as income.¹¹⁹ Similarly, profit from the purchase and sale of several hotels over a nine-year period was income.¹²⁰ Where a dredge was sold and later repurchased and resold, the vendor's intention to make a profit was indicated by the vendor's retention of a purchase option on the original sale.¹²¹ Again, where a company used an option arrangement for putting through its real estate transactions, profits made in exercise of the option were taxable as income.¹²²

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¹¹³ Vardalos, 83 DTC 354.

¹¹⁴ Wolfin et al, 84 DTC 1382.

¹¹⁵ Bell, 89 DTC 165.

¹¹⁶ Armstrong, 85 DTC 5396.

¹¹⁷ Stekl, 59 DTC 1262.

¹¹⁸ Inland Resources Co. Ltd., 64 DTC 5257.

¹¹⁹ Fraser, 64 DTC 5224, De Tora, 65 DTC 5194.

¹²⁰ The King Edward Hotel (Calgary) Ltd., 90 DTC 6468.

¹²¹ Sensibar Dredging Corp. Ltd., 67 DTC 5212.

¹²² Edgeley Farms Ltd., 69 DTC 5228.

However, an intention at the time of acquisition of an investment to sell it in the event that it does not prove profitable does not necessarily make the subsequent sale of the investment an adventure in the nature of trade, although it might if the expectation of profit on resale was one of the factors inducing the taxpayer to make the purchase.¹²³ Where a trader in land acquired a number of apartment properties as an investment and sold them at a profit nine months later, the profit was held to be a capital gain when the taxpayer successfully proved that the apartments had not been acquired for speculative purposes.¹²⁴

The intention of a taxpayer cannot ordinarily be established by a statement of the taxpayer of what the intention was. Such a statement must be supported by other evidence and the intention will be determined after considering the entire course of conduct of the taxpayer.¹²⁵

If the taxpayer's plan for a property is thwarted, for reasons such as the lack of municipal approval, the high realty taxes and cost of servicing the land, illness, or other unexpected problems that occur, the profit will ordinarily be a capital gain.¹²⁶ However, the profit from land bought for a specific purpose and sold after a short period, supposedly because the purpose of the purchase could not be attained, was taxable as income. It was established that the reason for the purchase was abandoned even before the supposed impossibility of achieving it became known and that the land was bought only after a visual inspection.¹²⁷ There are a number of cases in which taxpayers have been held to be taxable on profits from real estate transactions on the grounds that their intention in entering the undertakings was in fact to make profits and that, without even realizing it and judging by what they actually did, they were carrying on a real estate business or had entered into adventures in the nature of trade.¹²⁸ This might be so even though a taxpayer can show that his or her original plan was frustrated; where it is obvious that the taxpayer could or should have known about the obstacles (e.g., zoning), the profit may be taxable as income as being from an adventure in the nature of trade.¹²⁹ The surrounding circumstances will of course be examined. When a taxpayer agreed to sell his interest in land upon being told that the city intended to expropriate it if necessary, the profit was a capital gain.¹³⁰

The original intention may undergo a change; for example, an investor may sell because of the opportunity for a quick profit¹³¹ or merely because the completion of the investment scheme is no longer advantageous or

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¹²³ Crystal Glass Canada Ltd., 89 DTC 5143, Snell Farms Ltd., 90 DTC 6693.

¹²⁴ Hiwako Investments Ltd., 78 DTC 6281.

¹²⁵ Loyens, 83 DTC 535.

¹²⁶ Ratna Arya, 94 DTC 1526, Smith, 87 DTC 595, Jadare Limited et al, 86 DTC 6054, Valleypark Apartments Limited, 81 DTC 245, Acro Developments Co. Ltd., 79 DTC 727.

¹²⁷ Rakosh Engineering & Construction Ltd., 74 DTC 6375, Montpetit, 80 DTC 1273, Kamfeld and Bollint, 80 DTC 1827, Dalfen, 81 DTC 37.

¹²⁸ Lieber, 63 DTC 530, Common Street Holdings, 64 DTC 325.

¹²⁹ Greenberg, 61 DTC 696, Sheffel, 65 DTC 5133.

¹³⁰ Desrochers Development Corp., 87 DTC 5363.

¹³¹ Tandon, 85 DTC 332.

feasible.¹³² This may be the case where the original investment intention is abandoned because of external factors such as increased costs of construction,¹³³ financial difficulties encountered,¹³⁴ the lack of interest by tenants in commercial premises offered for rent,¹³⁵ or when property was reluctantly sold because of threatened competition.¹³⁶ Depending on circumstances and other factors, the change of intention may be construed as indicative of a commercial venture with the resulting profits taxable as income, or it may be viewed as being merely consistent with the original purpose of investing, where the realization of the asset would spell a capital receipt. A taxpayer was held to have changed his intention where in 1976 he unilaterally accepted an unsolicited offer for sale of the land he and his other partners had purchased as an investment in 1974. His other partners repudiated his decision and the land was eventually sold in 1980. The taxpayer's profit was taxed as a capital gain, calculated on the basis of the attempted sale in 1976, and as income thereafter. What happened here is that in 1976 the taxpayer's interest in the land changed use from a capital asset to an income-producing asset.¹³⁷

(2) *Relation of transaction to taxpayer's business.* Where a taxpayer uses the skill and knowledge acquired through experience in trading in a certain line of commodities and later makes a profit on the purchase and sale of such commodities, the courts have held that such profit is taxable as income.¹³⁸ Thus, the profits in wool futures realized by a wool producing manufacturing company were taxable as income,¹³⁹ as were the gains earned by a realtor from mortgage deals.¹⁴⁰ This rule may extend to the taxpayer's spouse/common-law partner.¹⁴¹ Where two taxpayers, at the direction of their investment consultant spouses, made substantial profits from the acquisition and quick resale of speculative mining stock, the profit was held to be income.¹⁴²

The same principle has been applied in the following cases: dealings by an agent for oil companies in oil leases on the agent's own account;¹⁴³ transactions in grain futures by a manager of a company trading in grain;¹⁴⁴ bonuses received in respect of a loan made by a company underwriting mining and oil securities;¹⁴⁵ profits of an investment dealer on its own investments;¹⁴⁶ sale of interest in a large construction contract by a construction company;¹⁴⁷ profits on the resale of lots and land by a coal dealer also carrying on the business of a building contractor;¹⁴⁸ and the sale of a newly built apartment house by the builder.¹⁴⁹ Similarly, where a notary who

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¹³² Green Heron Investments Ltd, 84 DTC 1617.

¹³³ Hanover Management Ltd. et al, 89 DTC 355.

¹³⁴ Plains Investments, 64 DTC 146.

¹³⁵ Grand Marais Development Co. Ltd., 65 DTC 5286.

¹³⁶ No. 467, 57 DTC 537.

¹³⁷ Aldershot Shopping Plaza, 65 DTC 5018.

¹³⁸ Hyman et al, 88 DTC 1352.

¹³⁹ Morrison, 1 DTC 113.

¹⁴⁰ M. Granatstein & Son Ltd, 55 DTC 396.

¹⁴¹ Cerisano, 64 DTC 99.

¹⁴² Wisniewski, 79 DTC 266.

¹⁴³ Darch and Wright, 92 DTC 6366.

¹⁴⁴ No. 331, 56 DTC 143, No. 332, 56 DTC 146.

¹⁴⁵ No. 351, 56 DTC 375.

¹⁴⁶ Stuyvesant-North, 58 DTC 1092.

¹⁴⁷ McMahon and Burns, 58 DTC 1092.

¹⁴⁸ General Construction, 59 DTC 1169.

¹⁴⁹ Gibson, 57 DTC 1119.

¹⁵⁰ Janzen, 64 DTC 756.

was familiar with the process of dealing in land sold a parcel of land which had been held for 19 years, the profits from the sale were held to be income.¹⁵⁰ A corporate taxpayer in the business of lending money received shares, share options, and mortgage bonds as partial consideration for loans. Gains from the dispositions of the securities were taxable as income because the taxpayer dealt with such securities either as a trader or as a regular part of its business.¹⁵¹

The courts have also considered the amount of the taxpayer's time and the amount of attention that the taxpayer gave to a transaction in determining whether or not the profit from the transaction was taxable.¹⁵² Where a professor who, in addition to teaching, wrote and translated textbooks under contracts with the university later sold all rights under the contracts to the university, the professor was held to have received taxable income from an undertaking for profit or a business venture.¹⁵³

Real estate transactions of building contractors, real estate agents, or brokers and taxpayers in similar occupations will usually be taxed as income.¹⁵⁴ Such a taxpayer will have to present a very strong case when claiming a real estate profit to be from an investment.¹⁵⁵

(3) *Nature of transaction and assets involved.* If an asset which could not normally be used for either investment or personal pleasure, either because of the quantity or nature of the asset, is purchased and resold, it is likely that the profit will be of an income rather than a capital nature, although this is not conclusive. In two English decisions,¹⁵⁶ for example, such large quantities of toilet paper and whiskey were purchased that it was obvious the taxpayer could not possibly use them all for personal consumption. Similarly, the profit on a single purchase was held taxable as income where a large organization had to be set up to dispose of the purchased commodity.¹⁵⁷

Normally a sale of fixed capital may be said to result in a capital receipt whereas a sale of circulating capital results in an income receipt. A sale of inventory which was not suited for the purpose for which it was bought was held to result in an income receipt.¹⁵⁸ Sale of oil leases by an exploration and development company resulted in taxable income, since leases, concessions, and other rights were part of the company's stock-in-trade.¹⁵⁹ However, where a family and two companies had been jointly and severally trying unsuccessfully to bring in a producing well on their government leases for about 30 years, and were fortuitous in being able to sell the leases just as they were in imminent danger of losing them, the profit was held to be a

See page ii for explanation of footnotes.

¹⁵⁰ Tardif, 79 DTC 758.

¹⁵¹ Raynot Ltd, 81 DTC 5072.

¹⁵² McDonough, 49 DTC 621.

¹⁵³ LaRue, 63 DTC 553.

¹⁵⁴ Bachuk, 81 DTC 536, P. E. Perron, Ltée, 62 DTC 1268, Blain, 64 DTC 367, Upstream Holdings, Inc., 69 DTC 5358, Consolidated Building Corp., 65 DTC 5211.

¹⁵⁵ Fabl, 65 DTC 5160, Bélisle, 64 DTC 490.

¹⁵⁶ Rutledge, (1929), 14 T.C. 490, Fraser, (1942), 24 T.C. 498.

¹⁵⁷ Martin v. Lowry, [1927] A.C. 512, Gordon, 51 DTC 230, Honeyman, 55 DTC 1094.

¹⁵⁸ No. 123, 53 DTC 407.

¹⁵⁹ Great West Exploration, 57 DTC 444.

realization of a capital asset.¹⁶⁰ A sale of a timber limit was held to result in a capital receipt, where the limit was received from provincial authorities in exchange for freehold timber lands to be used for colonization.¹⁶¹

The manner of disposition of assets, otherwise considered capital, may be important. Thus, taxable income was held to have resulted from sales of mineral and timber rights pertaining to lands a railway company had been granted in 1899. Even though the lands were of a capital nature when received, their character was changed by the manner in which they were later dealt with and used.¹⁶²

With respect to mortgages, profits may be also taxable as income in taxpayers' hands if the mortgages have only a short time to run to their maturity, where they have been purchased at a discount, where the interest rate is much lower than the prevailing rate on first-class second mortgages, or the mortgages are substandard first mortgages, and where they are of a risky nature. The Supreme Court of Canada has held that in instances of this type the taxpayer is regarded as being engaged in the highly speculative business of purchasing mortgages (including agreements for sale and lease-option agreements) at a discount and holding them to maturity in order to realize the maximum amount of profit out of the transactions.¹⁶³ It would therefore seem that nearly all profits realized from transactions involving the purchase of mortgages at a discount or under a bonus arrangement are taxable as income.¹⁶⁴

It is the nature of a transaction, not its singleness or isolation, that must be determined by the courts.¹⁶⁵ Where a taxpayer sought to deduct a trading loss on shares which had been retained as an investment and that had ceased to have any value, the loss on the shares was held to be a capital loss on an investment.¹⁶⁶ In two cases with somewhat similar facts, profits from the sale of shares obtained in exchange for mining claims were on account of capital when the taxpayer engaged a prospector to stake claims for the taxpayer alone¹⁶⁷ but were taxable as income where the taxpayer participated in a syndicate.¹⁶⁸ See ¶5240 regarding an election that a taxpayer can make to have certain securities, described as "Canadian securities," treated as capital property for tax purposes.¹⁶⁹

The former owner of a family business repurchased the shares of the company when it ran into financial difficulties, and acquired with it certain loans owing to shareholders which, at the time, were valued at nil. The former owner turned the business around and collected on the loans. It was held that the gain on the loans was a capital receipt, since gains arising from

See page ii for explanation of footnotes.

¹⁶⁰ Moose Securities Ltd., 63 DTC 182.

¹⁶¹ Gagnon, 58 DTC 562.

¹⁶² The Algoma Central and Hudson Bay Railway Co., 61 DTC 1027.

¹⁶³ Hennick, 64 DTC 307, Wallfish, 64 DTC 5121, Posluns, 64 DTC 5168, Davidson, 65 DTC 109.

¹⁶⁴ Wood, 69 DTC 5073, Ferguson, 70 DTC 1779.

¹⁶⁵ Farris, 70 DTC 6179.

¹⁶⁶ Trotter, 70 DTC 1104.

¹⁶⁷ Foster, 71 DTC 5207.

¹⁶⁸ Kay, 71 DTC 5085.

¹⁶⁹ CCH ¶6387; Sec. 39(4); Interp. Bul. IT-479R.

an entrepreneur's personal efforts were not, for that reason alone, necessarily income.¹⁷⁰

(4) *Number and frequency of similar transactions.* Another factor in determining whether profit derived from a transaction is a capital gain or income is the frequency with which the taxpayer has engaged in such transactions. Where a member of a firm of cotton brokers averaged some fifty transactions a year on the member's own account in cotton futures, the profits were found to be income,¹⁷¹ as were those of a taxpayer involved in the purchase and resale of several restaurant businesses over a period of years.¹⁷²

While a large number of transactions is likely to be indicative of an intention of carrying on a business for profit, the isolated transaction doctrine taken by itself provides a poor ground for an appeal since the term "business" includes an adventure or concern in the nature of trade.¹⁷³

Certain decisions of the Courts and the former Tax Review Board make it abundantly clear that the fact that a transaction is an isolated one does not in itself bring the profit into the capital gain category. In one such case, a profit made by a company director in an isolated transaction not related to the director's employment, involving the sale of four second-hand diesel engines was taxed as income.¹⁷⁴ Similarly, profits realized within a year by a lawyer on three unrelated transactions (deals in pipe, salt prospecting rights, and oil and gas) were held to be taxable as income.¹⁷⁵ Profits realized on the syndication of a stallion were held to be income from an adventure in the nature of trade.¹⁷⁶

(5) *Corporation's objects.* A corporation's objects and powers as set out in its charter create a *prima facie* presumption that acts done within their ambit must also be held to be within the commercial intent of the corporation. This presumption may, however, be rebutted by looking at the corporation's course of conduct and ascertaining what it in fact did during its commercial life rather than what it intended to do as formally stated in its main object clauses. The inclusion in its charter of a power to sell and deal in real estate is not evidence that the corporation was actually engaged in the business of trading in real estate with a view to resale at a profit. What counts is not what the company can do but what it actually does.¹⁷⁷ To borrow the words used by the Supreme Court of Canada, "the question to be decided is not what business or trade the company might have carried on under its memorandum but rather what was in truth the business it did engage in. To determine this it is necessary to examine the facts with care".¹⁷⁸ Thus, even if a corporation's objects were for investment purposes,

See page ii for explanation of footnotes.

¹⁷⁰ Eldinger, 86 DTC 6594.

¹⁷¹ Cooper v. Stubbs, 2 KB. 753.

¹⁷² No. 367, 56 DTC 516.

¹⁷³ CCH ¶28,024; Sec. 248(1) "business"; Interp. Bul. IT-459.

¹⁷⁴ Chuter, 59 DTC 1118.

¹⁷⁵ Turnbull, 57 DTC 1170.

¹⁷⁶ Anderson, 80 DTC 1501.

¹⁷⁷ Rivermead Developments Limited, 93 DTC 5365.

¹⁷⁸ Sutton Lumber & Trading Ltd., 53 DTC 1158.

Thus Mr. B realizes neither a capital gain nor a capital loss. However, he has securities worth \$20,000 at a cost of only \$17,000. On disposition of them he would realize a gain of \$3,000. Thus the actual gain of \$15,000 is split as \$12,000 to Mr. A and \$3,000 to Mr. B.

[¶7470] Distribution of Depreciable Property

If the property distributed to the taxpayer was depreciable property, and if the original capital cost to the trust of the property exceeds the cost at which the taxpayer is deemed to have acquired it, then the capital cost to the taxpayer for purposes of recapture, etc., is the original capital cost to the trust.²⁵² The taxpayer is considered to have claimed as capital cost allowance any excess of the trust's capital cost over the cost at which the taxpayer is deemed to acquire the asset.

Example:

A trust has certain depreciable property, claims capital cost allowance in respect of it and eventually distributes it to the sole capital beneficiary in satisfaction of the beneficiary's capital interest, which was acquired gratuitously.

capital cost to trust _____	\$100,000
undepreciated capital cost _____	80,000
fair market value _____	95,000
deemed cost to beneficiary _____	80,000
deemed capital cost to beneficiary _____	80,000
deemed allowed to beneficiary as capital cost allowance (\$100,000 - \$80,000) _____	20,000
undepreciated capital cost to beneficiary _____	80,000

The beneficiary then sells the property for its fair market value (\$95,000) and realizes recapture of \$15,000.

[¶7475] Proceeds of Disposition of Capital Interest

A taxpayer will be deemed to have disposed of the capital interest in the trust for proceeds equal to the cost at which the property distributed is deemed to have been acquired, minus any "eligible offset". Generally speaking, the eligible offset is the proportionate amount of the trust liabilities assumed by the beneficiary as a condition for the distribution of the trust property.²⁵³

[¶7477] Proceeds of Disposition of Eligible Capital Property

Where eligible capital property is distributed in satisfaction of all or part of the capital interest, the trust is deemed to have received an amount equal to $\frac{1}{3}$ of the cost amount of the property to the trust immediately before that time. The beneficiary is deemed to have acquired the property at $\frac{1}{3}$ of that

See page ii for explanation of footnotes.

²⁵² CCH ¶13,820, ¶29,170; Sec. 107(2)(d); ITAR 20(1.2). ²⁵³ CCH ¶13,820, ¶13,916; Sec. 107(2)(c), 108(1) "eligible offset".

same cost amount, plus adjustments in certain cases. This treatment provides the rollover for eligible capital property, since the trust only includes $\frac{3}{4}$ of the proceeds in the calculation of its cumulative eligible capital (CEC) account.

Additionally, the beneficiary is deemed to have previously deducted $\frac{3}{4}$ of any of the excess of the trust's eligible capital expenditure with respect to the property over the cost at which the beneficiary is deemed to have acquired the asset, so that the beneficiary "steps into the shoes" of the trust with respect to the CEC account.²⁵⁴

Example:

A trust distributes eligible capital property to a beneficiary in satisfaction of the beneficiary's capital interest in the trust.

ECE to trust _____	\$100,000
CEC to trust _____	\$ 60,000
Deemed cost to beneficiary $\frac{1}{3} \times \$60,000 =$	\$80,000
Deemed ECE to beneficiary _____	\$100,000
Amount deemed to have been previously deducted by beneficiary under sec. 20(1)(b) $\frac{3}{4} \times (\$100,000 - \$80,000) = \frac{3}{4} \times \$20,000 =$	\$ 15,000
Deemed CEC to beneficiary $(\frac{3}{4} \times \$100,000) - \$15,000 =$	\$ 60,000

[¶7480] Trusts in Favour of Spouse or Common-Law Partner

Where a post-1971 spousal or common-law partner trust distributes depreciable capital property of a prescribed class, non-depreciable capital property, Canadian or foreign resource property, or land inventory, the trust is deemed to have proceeds of disposition equal to the fair market value of such property.²⁵⁵ As a result, the post-1971 spousal or common-law partner trust will realize any accrued capital gains or losses and inventory profits or losses in respect of the capital property or inventory. Capital gains, recapture, or terminal losses could arise as a result of the application of this rule to depreciable property of a prescribed class. In addition, the deemed proceeds of disposition for the resource properties could result in an income inclusion. The deemed disposition of property at fair market value will apply to a distribution by *alter ego trusts* and *joint spousal or common-law partner trusts*, where the individual (or, in the case of a joint spousal or common-law partner trust, either the individual or the spouse/common-law partner) is alive on the day of the distribution and the distribution is made to a beneficiary other than the individual (or, in the case of a joint spousal or common-law partner trust, the individual or the spouse/common-law partner).

See page ii for explanation of footnotes.

²⁵⁴ CCH ¶13,820; Sec. 107(2)(f). ²⁵⁵ CCH ¶13,150, ¶13,870; Sec. 104(4), 107(4).

The beneficiary to whom the distribution is made is deemed to have acquired the property at a cost equal to its deemed proceeds of disposition to the post-1971 spousal or common-law partner trust. On any later disposition of capital property or land inventory, this base will be used to compute the beneficiary's capital gain or loss or profit or loss. Likewise, this base will be the beneficiary's original cost for purposes of computing capital cost allowance and the amount of any recaptured capital cost allowance on a subsequent disposition of the depreciable property by the beneficiary.

The beneficiary who has paid nothing for the trust interest is deemed to have acquired property for its cost amount. If such a beneficiary had to assume any debt of the trust as a condition of the distribution of the property, the amount of the debt is subtracted in arriving at the deemed proceeds of disposition of the capital interest.

¶7485 Distribution to Non-Resident Beneficiary

Distribution of property by a trust to a non-resident beneficiary (other than as a SIFT trust wind-up event described at ¶6278 and ¶7486) is treated as disposition of property by the trust. As a result, the distribution may give rise to a capital gain. However, the trust may elect to include such gain in its income instead of having the beneficiary include the gain.²⁵⁶ This deemed disposition does not apply to shares of a non-resident-owned investment corporation; real property situated in Canada; Canadian resource property; timber resource property; capital property used in, eligible capital property in respect of, and property described in the inventory of a business carried on in Canada through a permanent establishment in Canada; and certain interests in trusts and deferred income streams.

¶7486 Distribution by SIFT Wind-Up Entity

On the winding-up of a SIFT trust and redemption of its units after July 14, 2008, a SIFT trust may distribute its shares of a Canadian corporation to its unitholders, on a tax-deferred basis. This rollover will also apply where a SIFT trust holds all of the equity interests in a second-tier trust and the second-tier trust distributes shares of a Canadian corporation to the SIFT trust on the winding-up of the second-tier trust. For this rollover to apply, there must be a distribution of all of the trust's property to its unitholders and the distribution must occur within 60 days of the first distribution of property, if any, on the wind-up of the second-tier trust. The only property that can be distributed to former SIFT unitholders under this rollover is shares of a single class of the capital stock of a taxable Canadian corporation.²⁵⁷

The following deemed proceeds of disposition achieve the tax-free rollover. The trust being wound up is deemed to have disposed of the property for proceeds of disposition equal to the adjusted cost base to the trust of the property immediately before the disposition. As to the unitholder, it is deemed

See page ii for explanation of footnotes.

²⁵⁶ CCH ¶13,845, ¶13,847; Sec. 107(2.1), 107(2.11).

²⁵⁷ CCH ¶13,860, ¶13,860g; Sec. 107(3), 107(3.1).

to have disposed of its units for proceeds of disposition equal to the cost amount of the unit immediately before the distribution. If the taxpayer is the only beneficiary of the trust, as would happen where the trust is wholly owned by another trust or corporation, and the taxpayer is a "SIFT wind-up entity" or a taxable Canadian corporation, the taxpayer is deemed to have acquired the trust property at a cost equal to the adjusted cost base to the trust immediately before the disposition. In any other case, such as where the beneficial interests in the trust are held by the public, the property is deemed to be acquired at the cost amount to the taxpayer of the taxpayer's interest as a beneficiary of the trust. Furthermore, if the taxpayer's interest as a beneficiary under the trust was taxable Canadian property, the new property received is deemed to continue to be taxable Canadian property of the taxpayer.

Under the above conversion method of a SIFT trust into a corporation, the trust must first transfer its property to a taxable Canadian corporation. If a liability owed by the trust is, as a consequence of the distribution, assumed by the corporation (i.e., the corporation whose shares are being distributed) and the amount payable on maturity by the corporation is the same as that amount payable by the trust, the trust may transfer this liability to the corporation without any income tax consequences. In such a case, the liability is deemed to have been incurred or issued by the corporation and not the trust.

These SIFT conversion rules apply only to the redemption of units or winding-up of a trust that occurs after July 14, 2009, and before 2013.

¶7487 Distribution of Property with an Accrued Loss

The acquisition of a capital interest in a trust that has property with an accrued loss as a means of transferring losses is discouraged. Where the property is distributed to the beneficiary in satisfaction of that interest, any loss on a subsequent disposition of the property will be denied to the extent that it can be considered to have accrued while owned by the trust and at a time when neither the beneficiary nor a person affiliated with the beneficiary had a capital interest in the trust.²⁵⁸ Without this anti-avoidance rule, a person or partnership acquiring a capital interest in a trust which has a property with an accrued loss could cause the property to be distributed in satisfaction of such interest at its cost amount to the trust and realize a loss on a subsequent disposition.

¶7490 Distributions by Employee Trust or Employee Benefit Plan

Special rules²⁵⁹ apply with respect to the distribution of property by an employee trust or an employee benefit plan to a beneficiary in satisfaction of all or part of the beneficiary's interest in the trust.

In the case of an employee trust, the trust is deemed to have disposed of the property immediately before the distribution for proceeds equal to fair

See page ii for explanation of footnotes.

²⁵⁸ CCH ¶13,882; Sec. 107(6).

²⁵⁹ CCH ¶13,890; Sec. 107.1.

market value. Any gain or loss resulting on the deemed disposition would form part of the amount which the trustee must allocate among the beneficiaries of the trust. The beneficiary is deemed to have acquired the distributed property at a cost equal to its fair market value.

In the case of an employee benefit plan, the trust is deemed to have disposed of the distributed property for proceeds equal to the cost amount of the property to the trust (thus realizing neither a gain nor a loss). The taxpayer is deemed to have acquired the property at a cost equal to the greater of its fair market value at that time and the adjusted cost base of his or her interest in the trust (immediately before that time). It is this fair market value of the property distributed that is the "amount" received by the taxpayer from the plan for the purpose of computing the income inclusion. If the taxpayer would otherwise have a loss on the disposition of his or her interest in the trust, that loss is added to the adjusted cost base of the property received by the beneficiary from the trust.

The taxpayer is deemed to have disposed of his or her interest in the employee trust or employee benefit plan for proceeds equal to its adjusted cost base, thus recognizing no gain or loss on the disposition.

The recognition in an employee trust or employee benefit plan of a gain or loss in respect of property distributed to a beneficiary will apply from 1998 to a health and welfare trust.

Where depreciable property is distributed in satisfaction of the beneficiary's interest, special rules apply where the capital cost of the property to the trust exceeds the deemed cost thereof to the beneficiary. In general, these rules place the beneficiary in the trust's position for claiming capital cost allowance and recognizing recapture or terminal losses. The beneficiary's capital cost is deemed to be the trust's capital cost. The beneficiary is considered to have claimed as capital cost allowance any excess of the trust's capital cost over the cost at which the beneficiary is deemed to acquire the asset. For an example, see ¶7470.

¶7495] Distributions by Retirement Compensation Arrangement

Special rules apply when a trust governed by a retirement compensation arrangement (RCA) distributes property to a beneficiary in satisfaction of all or part of his or her interest in the trust.²⁶⁰ They can be summarized as follows:

(1) The trust is treated as having disposed of the property at its fair market value and, as such, may have to recognize a gain or loss on the distribution.

(2) The trust is deemed to have made a distribution to the beneficiary equal to the fair market value of the property. This may trigger an income inclusion as well as a refund of tax to the custodian of the arrangement under

See page ii for explanation of footnotes.

²⁶⁰ CCH ¶13,892; Sec. 107.2

Part XI.3. It should be noted that the beneficiary who receives the distribution may not be the taxpayer required to include the amount of the distribution in his or her income.

(3) The beneficiary is treated as having acquired the trust property at a cost equal to its fair market value.

(4) The beneficiary will not realize a capital gain or a loss in respect of a disposition or partial disposition of his or her interest in the trust on the distribution. Instead, he or she is deemed to have disposed of his or her interest in the RCA for proceeds of disposition equal to the adjusted cost base of his or her interest.

(5) Where the property distributed is depreciable property, a special rule will apply where the capital cost to the trust of the property exceeds the fair market value of the property. If this is the case, the beneficiary inherits the capital cost to the trust of the property for the purposes only of calculating any recapture of capital cost allowance, and the beneficiary will, on a disposition of the property at a price greater than the fair market value at the time distributed to him or her, be liable to include in income any recovery of capital cost allowance that was previously claimed by the trust.

¶7497] Qualifying Environmental Trusts

Special rules permit the deduction of contributions to trusts maintained for the sole purpose of funding the reclamation of a site in Canada that has been used primarily for, or any combination of, the operation of a mine, the extraction of clay, peat, sand, shale or aggregates (including dimension stone and gravel), or the deposit of waste.²⁶¹

Contributions to (or the purchase of a beneficial interest in) a qualifying environmental trust are deductible in the year made (or bought) and taxable in the year withdrawn (or when the beneficial interest is sold).²⁶² Investment income earned in the trust on the funds on deposit will be taxable both to the trust and the beneficiary (the contributor or purchaser which buys the beneficial interest). The trust itself is taxable under special Part XII.4 at 28%, intended to equal the corporate tax rate, since it is typically an operating corporation that will have the restoration liabilities the trust is intended to fund.²⁶³ The same income taxed in the trust is considered ordinary taxable income of the beneficiary,²⁶⁴ but the beneficiary will receive a refundable tax credit on its income allocation for the tax paid in the trust.²⁶⁵ Thus, if the trust earns \$1,000, it pays \$280 federal tax (similar to the federal corporate rate). The \$280 is a refundable credit to the beneficiary who receives from the trust a \$1,000 income allocation. If the beneficiary has a net income of nil for the year (or a loss), it receives the \$280 tax credit. Provision is made for the trust to flow out

See page ii for explanation of footnotes.

²⁶¹ CCH ¶28,226b; Sec. 248(1) "qualifying environmental trust."

²⁶³ CCH ¶25,950-25,954; Sec. 211.6.

²⁶⁴ CCH ¶43,77b, ¶43,77c; Sec. 12(1)(z1), 12(1)(z2).

²⁶² CCH ¶13,894; Sec. 107.3.

²⁶⁵ CCH ¶19,998; Sec. 127.41(1).

losses as well as income. Income or loss should retain its underlying characteristics.²⁶⁶

For taxation years ending after February 18, 1997, mining reclamation trusts were renamed "qualifying environmental trusts" and the rules were extended to similar trust funds for the reclamation of waste disposal sites and quarries for the extraction of aggregates and similar materials.

[¶7500] Transfers to Bare Trusts, Protective Trusts, and Similar Vehicles

Because bare trusts are essentially agents for their beneficiaries, certain transfers to bare trusts ("qualifying dispositions") are exempt from the normal deemed disposition rules that apply upon a transfer of property to a trust. However, where a Canadian resident transfers property to a non-resident bare trust after December 23, 1998, that transfer will be treated as a disposition and the bare trust will be treated as an ordinary trust.

Where bare trusts are not involved, transfers of property which do not result in any change of beneficial ownership are treated as dispositions subject to explicit rollover rules. Where all or part of a trust interest created under the rollover rules is subsequently disposed of, it is considered to have been disposed of for proceeds of disposition that are not less than an amount based on the fair market value of the net trust assets associated with the interest.²⁶⁷

See page ii for explanation of footnotes.
²⁶⁶ CCH ¶5128p, ¶5128q; Sec. 20(1)(ss), 20(1)(td).
²⁶⁷ CCH ¶13,897; Sec. 107.4.

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