THE CONTINUING LEGAL EDUCATION
SOCIETY OF BRITISH COLUMBIA

CLE BC

INCOME TAX FUNDAMENTALS FOR THE ESTATE PRACTITIONER
PAPER 1.1

Taxable Dispositions and Deferrals

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TAXABLE DISPOSITIONS AND DEFERRALS

I. Overview

In the course of an estate plan, the spectre of tax dispositions can cast a long shadow over otherwise desirable plans. Likewise, when administering an estate the deemed disposition triggered by death can create havoc for an estate's administration. This paper will (a) outline common circumstances in which a disposition of property may give rise to tax and (b) discuss steps that may be taken to defer the taxes payable to a later date or manage the payment of such taxes. We begin with an overview of what is a taxable disposition under the Income Tax Act, R.S.C. 1985, c. 1 (5th Supp.) (the "Act") and how those dispositions may be avoided, and then describe specific circumstances in which a taxable disposition may occur in the estate context, and outline commonly used strategies for deferring tax on those dispositions.

A. What is a Taxable Disposition?

A disposition of capital property is taxable when the taxpayer receives or is deemed to receive more from disposing of the capital property than he or she spent in acquiring it. A disposition can occur on sale, gift or other transfer. In certain circumstances, the Act deems the taxpayer to dispose of capital property for certain proceeds (often fair market value) – whether or not the property was actually disposed of and whether or not any amount was actually received for it. Care must be taken when planning not to inadvertently trigger such a deemed disposition.

The Act defines "disposition", "capital property" and the amount spent in acquiring the property (the "adjusted cost base") in s. 248. For purposes of this discussion:

- "Adjusted cost base" means the cost to the taxpayer of acquiring capital property;
- "Capital gain" means the positive difference between the fair market value of capital property at the time it is disposed of and the adjusted cost base of the property;
- "Capital loss" means the negative difference between the fair market value of capital property at the time it is disposed of and the adjusted cost base of the property;
- "Capital property" means property which the taxpayer may dispose of for a capital gain;
- "Disposition" includes a transaction entitling a taxpayer to proceeds of a disposition or by which a taxpayer is deemed to receive proceeds of a disposition and includes a transfer to a trust of property.

Currently, 50% percent of the value of capital gains are included in income taxable at the marginal rates of tax.

B. How is Tax on Taxable Dispositions Avoided?

Where a disposition would result in an income inclusion, immediate tax can be avoided if the tax can be deferred to a date later than the disposition, there is an exemption available, the transferor has losses that may offset a gain, or there are credits available to the taxpayer.

Deferrals commonly used in estate planning include:

- Spousal rollovers, whereby property is disposed of by transferring it to a spouse either *inter vivos* or on death and whether outright or by spousal trust.
- Rollovers that are available on transfers to certain trusts, such as alter ego trusts, joint partner trusts, and self-benefit trusts, whereby tax is not payable until the death of certain beneficiaries of those trusts.
- Estate freezes, under which the growth value of an asset is directed to another party so that future gains do not accrue in the hands of the donor, but rather the donee.

These types of deferrals are discussed further below.

Exemptions reduce the taxable income that would occur because of the capital gain on a property, with the result that there is no tax payable. Frequently encountered exemptions from capital gains tax include:

- The principal residence exemption found in s. 40(2)(b) of the Act (or s. 40(2)(c) where land used in a farming business is the principal residence of the taxpayer), which eliminates or reduces the capital gain on the disposition of the taxpayer's principal residence. A trust may sometimes claim the principal residence exemption on a home owned by the trust where it is occupied by a beneficiary. Certain criteria must be met in order for this exemption to apply and care must be taken to review these rules when drafting the trust.

- The $800,000 lifetime capital gains exemption for the sale of qualified small business corporation shares and the $1,000,000 qualified farm or fishing property exemption available under s. 110.6 of the Act.
- Dispositions to "qualified donees" (as defined in s. 149.1(1) "qualified donee" of the Act, and generally including a registered charity, a Canadian municipality, the Crown or the United Nations) of certain types of property, including a gift under s. 38(a.1)(i) of the Act of shares in publicly traded companies.

Subsection 3(b) and 38(a) of the Act permit the taxpayer to apply capital losses against capital gains income in calculating the amount of tax owing by the taxpayer. Losses may be carried back 3 years and carried forward an unlimited number of years: s. 111(1)(b). In the year of death, losses may be carried back 3 years and unused taxable losses from previous years can be applied against income in the year of death: s. 111(2).

Credits may be applied to offset the amount of taxes owing by a taxpayer. For example, the charitable donation credit is available where the taxpayer has made a donation to a "qualified donee" such as a registered charity.

The focus of this paper is deferrals that may be available where a disposition occurs. However, where a disposition occurs or will occur, practitioners should be mindful that exemptions or losses may be available to eliminate the taxes owing rather than deferring taxes to a later date.

II. Taxable Dispositions

A. Taxable Dispositions in Estate Planning

In the context of estate planning, taxable dispositions may occur when property is gifted or sold. Special considerations apply when property is transferred into a trust.

1. Gifts

A transfer of the beneficial interest in property will generally give rise to a taxable disposition. Accordingly, gifts of capital property that have appreciated in value will trigger a capital gain. Clause 69(1)(b) of the Act provides that the taxpayer is deemed to receive proceeds of disposition equal to the fair market value of the property where a taxpayer disposes of that property:

- to a person who was not dealing at arm's length for no proceeds or for proceeds less than the fair market value of the property,
- to any person by way of gift, or
- to a trust because of a disposition of property that does not result in a change of the beneficial ownership of the property.

Clause 69(1)(a) provides that a non-arm's length person receiving the property is deemed to receive it at fair market value, which will act as the new cost base for the property.

"Non-arm's length" is not defined in the Act and is a question of fact. Any person, including a corporation, may be found not to be dealing at arm's length with the taxpayer. Section 251 deems certain categories of relationships to be non-arm's length. "Related persons", as defined in s. 251(2) to (6), are deemed by s. 251(1)(a) not to deal with each other at arm's length. Clause 251(2)(a) provides that related persons include persons connected by a "blood relationship", marriage or common-law partnership or adoption. These relationships are further defined in s. 251(6). "Blood relationship" is where one person is the child or other descendant of the other or is a sibling. Connected by marriage includes persons married to each other or where a person is married to someone who has a blood relationship with the other. Adoption includes both legal and in fact adoptions. Transfers of property to any of these persons will be deemed to be for fair market value and will trigger capital gains tax on any accrued gains on the property, whether or not proceeds of disposition are received by the taxpayer.

Gifts of cash generally will not give rise to a capital gain. There are exceptions for dispositions of foreign currency which may be treated as capital property: see ss. 39(1.1) and (2).

Despite the general rule that gifts of cash will not give rise to capital gains, it is important to remember that if a taxpayer gifts property, either directly or indirectly, to his or her spouse or common-law partners, a minor, or a person who is not dealing at arm's length with the taxpayer, s. 160(1) of the Act makes that recipient of the gift jointly, severally and solidarily liable for unpaid tax of the taxpayer up to the value of the gift. If for example, a parent makes a gift from his or her business to a child and there are unpaid taxes owing by the parent, the CRA may follow the unpaid taxes into the child's hands.

2. Sale

If the taxpayer transfers capital property to a third party for consideration less than the adjusted cost base of the property, then the taxpayer will incur a capital loss. A gain will arise if the transfer is for consideration greater than the value of the capital property. If the transfer is to a non-arm's length entity, however, the transfer will be deemed to be at fair market value under s. 69(1), regardless of the amount of consideration which was received.

3. Transfers to Trusts

The general rule is that there is no disposition of property unless there is a change of beneficial interest under the Act and that a disposition does not include a transfer where there is no change in beneficial ownership (section 248(1)). However, clauses 248(1)(e)(i), (ii) and (iii) further provide that clause 248(1)(e) does not apply where the transfer is from a person or partnership to a trust for the benefit of that person or partnership, from a trust to a beneficiary under the trust, or from one trust maintained for the benefit of one or more beneficiaries under the trust to another trust maintained for the benefit of the same beneficiaries.

Therefore, in most circumstances a transfer of appreciated property to a trust will be a "disposition" and capital gains will be triggered even if the beneficial owner of the property remains the same (subject to the exceptions of a bare trust, an alter ego trust, joint partner or common-law partner trust, and self-benefit trust discussed below). Clause 69(1)(b)(iii) of the Act deems the settlor in these instances to have disposed of the property to the trust for proceeds equal to the fair market value of the trust. Under s. 69(1)(c) of the Act, the trust is deemed to acquire the property for fair market value. Therefore, any accrued gains will be realized by the transferor and the fair market value of the property at the time of the disposition will be the adjusted cost base for the trust.

B. Deemed Disposition on Death

1. Deemed Disposition of Capital Property

A taxpayer is deemed immediately before his or her death to have disposed of each capital property of the taxpayer and to have received proceeds of disposition equal to the fair market value of that property: s. 70(5)(a). Any person that acquires capital property as a consequence of the taxpayer's death is deemed to have acquired it for fair market value: s. 70(5)(b).

The result of these provisions is that all gains accrued in the estate will be realized and taxed on the death of the taxpayer. The cost base of the assets that beneficiaries receive from the estate will in most circumstances be the fair market value of the property, and dispositions from the estate to those beneficiaries will not be taxable.

Generally, the taxation of capital gains arising from the deemed disposition on death is the same as the taxation of capital gains during the lifetime of the deceased. Where the conditions for the spousal rollover under s. 70(6) (discussed below) are met, the tax will be deferred. The principal residence exemption will also be available to offset gains on the deceased's principal residence. As well, s. 111(2) will allow capital losses to be carried back to 3 years prior to the year of death if the capital losses exceed the capital gains realized in the year of death. Helpfully, s. 111(2) also permits net capital losses that arise in the terminal year and any capital loss carry forwards from prior years to be used to offset any income source in the terminal year, and not just income from capital property.

A deceased taxpayer's interest in jointly held property will be deemed to be disposed of immediately before the death of the taxpayer for fair market value. The deceased taxpayer's interest for this purpose is calculated by dividing the total value of the property by the number of owners of the property. While the right of survivorship will result in the joint property passing outside the estate with probate fees being avoided on such property, the estate will nevertheless suffer a tax burden for any accrued capital gains on the property. This result may be unfair to the beneficiaries of the residue of the estate as the tax burden will effectively be borne by the residue, while the benefit will pass to the surviving joint tenant or tenants. In addition, if there are insufficient assets in the estate to meet the gain, then the estate would be rendered insolvent.

2. Deemed Disposition of Certain Other Property

If the deceased held depreciable property, there will be recapture of the capital cost allowance of the property (which represents the amount by which the property has depreciated) that is disposed of on death under s. 70(5)(c) if the undepreciated capital cost of the property exceeds the fair market value of the property. The amount recaptured will be included as ordinary income of the deceased.

If the deceased held non-listed personal use property, then the loss from such property will be nil and not available to offset gains in the estate: s. 40(2)(g)(iii). Losses from listed personal use property (defined in s. 54 "listed personal property", and generally referring to collectible items, such as artwork, jewellery, rare books and stamps) are deductible against losses from other personal use property but not other capital losses: ss. 3(b)(ii) and 41(2).

Unique rules are applicable to RRSPs, RRIFs and TSFAs on death. In the case of an unmatured RRSP, when the annuitant of an RRSP dies, s. 146(8.8) of the Act deems the deceased to receive the fair market value of all property held in the RRSP at death, which amount will be reported in the deceased's income. The beneficiary of the RRSP will not pay tax on the amounts received if it was paid by the deceased's estate. This is the case even if the RRSP was paid directly to the named beneficiary and was not received by the estate. If the estate has insufficient assets to pay the tax, then the recipient will be jointly and severally liable with the estate for taxes that are not paid: s. 160.2.

If the RRSP is paid to a spouse or financially dependent child or grandchild of the annuitant, then the amount received will be considered a "refund of premiums": s. 146(1). This amount can be deducted from the deceased taxpayer's terminal return, and such amount will be included as income in the return of the spouse or dependent: s. 146(8.9). Subsection 60(l) of the Act provides a rollover to the spouse or dependent to transfer the property into an RRSP or qualifying annuity. Similar rollover treatment is available where the property is placed into an RDSP: s. 60.02. The personal representative of the estate and a spouse or financially dependent child or grandchild who is the beneficiary of the estate can jointly elect for similar tax treatment if a designation has not been made and the amount is payable to the personal representative: s. 146(8.1).

In the case of a matured RRSP, the remaining annuity payments will be commuted and included as income in the terminal return of the deceased: ss. 146(2)(c.2) and 146(8.8). There is an exception if the spouse of the deceased is the designated beneficiary of the plan, or is the sole beneficiary of the deceased's estate. In such cases, the spouse will become the successor annuitant of the plan, the annuity payments will not be commuted, and the benefits received will be included in the income of the spouse: ss. 146(1) "benefit", 146(8) and 146(8.8)(b). If no designation has been made but the deceased's legal representative receives the amounts from the plan for the benefit of the spouse, the legal representative and the spouse may elect jointly that the spouse be deemed to be the annuitant of the plan.

As with an unmatured RRSP, under s. 146(8.9), the personal representative may deduct from the income of the estate such portion of the commuted value that has been paid to a spouse or financially dependent child or grandchild, or, if the RRSP is paid to the deceased's estate, elect jointly under s. 146(8.1) with that spouse or financially dependent child or grandchild to deem the commuted value to be received by that individual. He or she may then either pay tax on the amounts received or make use of the rollover provisions described above. (See also RC4177(E) Rev. 15 - Death of an RRSP Annuitant or a PRPP/SPP Member.)

Similar rules as apply to unmatured RRSPs apply to RRIFs. The estate will be deemed to receive an amount equal to the fair market value of the fund on the death of the annuitant: s. 146.3(6). Subsection 146(6.2) permits the personal representative to deduct from the income of the estate the amount received by the deceased's spouse or a dependent child or grandchild of the deceased from the RRIF, and such amounts may be rolled into a qualified plan by that recipient under s. 60(l). The legal representative of the deceased and the spouse or dependent child or grandchild may also jointly elect to shift the tax burden for the amounts paid from the RRIF to the legal representative to that spouse or dependent child or grandchild: ss. 146.3(1) "designated benefit" and 146.3(6.1).

It should be noted that the rules applicable to RRSPs or RRIF do not include a rollover for transfers to a spousal trust (described below). The fair market value of the registered plan gifted into a spousal trust will be included as income in the estate. In most cases, it will therefore not be tax efficient to transfer an RRSP or an RRIF to a spousal trust, though there may be non-tax reasons that make a spousal trust desirable. Such reasons include creditor protection, providing for successive interests in the proceeds of the fund, or independent management of the property.

A TFSA ceases to be an arrangement on the death of the last holder of the TFSA: s. 146.2(5). If the TFSA was trusteed, then the arrangement is deemed to continue until the end of the calendar year after the year in which the TFSA holder dies: s. 146.2(9). The amount held in the TFSA will be received by the estate or any designated beneficiary of the TFSA free of tax (though income tax will apply to the increase in value after the TFSA ceases to be an arrangement). A rollover is effectively available if the spouse of the account holder is designated as a beneficiary – the amounts received in this case will not affect the contribution room of the recipient spouse.

Note that the deemed disposition at death can result in double taxation where the estate holds shares in a corporation. On death, accrued gains in the shares held by the deceased will be taxed. If the assets of the corporation are then sold or disposed of, those assets will also be subject to tax in the corporation. Dividend tax may also apply if funds are paid out to the estate as a shareholder. Strategies to avoid double taxation in these circumstances are beyond the scope of this paper. For a useful summary of some of the strategies available see *BC Estate Planning and Wealth Preservation*, Continuing Legal Education Society of BC, at § 7.53 and following and *Joseph Frankovic et al*., eds., *Canadian Estate Planning Guide* (looseleaf) (North York: CCG Canadian Limited, 1995) at ¶13,400.

III. Deferrals

While it is not possible to completely avoid the tax on gains, this pain can sometimes be deferred.

A. Spousal Rollovers

Spousal rollovers are perhaps the most common tax deferral mechanism used to defer payment of capital gains. A deferral is available for transfers to married or common-law spouses under ss. 70(6) (for testamentary transfers) and s. 73 (for *inter vivos* transfers) of the Act, whether by transfer to a trust or by transfer to the spouse outright. These sections provide for an automatic rollover of the property to the spouse, whereby the transferor will be deemed to receive as proceeds of disposition the adjusted cost base of the property and the spouse will be deemed to acquire the property at the adjusted cost base, with the result that no gain will be triggered. Under s.70(6), the requirements for the testamentary rollover are:

(1) the taxpayer and the spouse were resident in Canada immediately before the taxpayer's death;

(2) the property is transferred or distributed to the spouse or to a trust that was resident in Canada immediately after the time the property vested indefeasibly in the trust; and

(3) in the case of a trust, the spouse is entitled to receive all of the income of the trust that arises before the spouse's death, and no one other than the spouse may receive or otherwise obtain the use of any of the income or capital of the trust before the death of the spouse.

Subsection 73(1.01) contains similar requirements with respect to *inter vivos* dispositions to spouses.

In addition, in the case of a testamentary disposition, the property must vests indefeasibly in the spouse or trust within 36 months after the death of the taxpayer or within such other time as the CRA agrees to in response to a written request made within the initial 36-month period by the taxpayer's legal representative.

If the property is not disposed of by the spouse or trust, the deferral will last until the date of the death of the surviving spouse, at which time the spouse or trust will be deemed to dispose of the trust property for proceeds equal to the fair market value. Spousal trusts permit the settlor to appoint a remainder beneficiary of the trust following the death of the spouse, which remainder should not taint the trust provided that the spouse is entitled to receive all of the income of the trust during his or her lifetime, and no person, except the spouse, may obtain the use of the capital of the trust while the spouse is living. These trusts may therefore be used as a vehicle for providing gifts after the death of the spousal beneficiary.

The spousal rollover provisions provide significant opportunity for income splitting and probate avoidance. However, the automatic rollover may not be beneficial in all instances. For example, where there are opportunities to eliminate, rather than defer, the gain (as, for example, where there are net losses available to the estate that may apply to offset the tax of the transfer, there are significant charitable donation credits available to the estate, or the lifetime capital gains exemption or principal residence exemption may apply), it may be preferable for the taxpayer or, if the taxpayer is deceased, the personal representative of the estate, to elect out of the rollover and have the gain be triggered at fair market value: see ss. 70(6.2) and 73(1).

B. Transfers to Certain Types of Trusts

In addition to spousal trusts, the Act also allows rollovers for transfers to certain types of trusts that benefit the settlor, namely alter ego trusts, joint partner or common-law partner trusts and self-benefit trusts. Notably, a bare trust is not considered a trust for purposes of this analysis (see S.248(1) definition of "trust" and s.104).

1. Alter Ego Trusts and Joint Partner or Common-Law Partner Trusts

Alter ego trusts and joint partner or common-law partner trusts permit settlors over 65 to settle property into trust on a rollover basis. These trusts provide exceptional flexibility, as they allow settlors to continue to benefit from the property settled into the funds during their lifetime, provide a mechanism to plan for incapacity or achieve disability planning goals, avoid creditors, probate or wills variation claims, protect confidentiality and simplify the estate administration process.

Both the terms "alter ego trust" and "joint partner or common-law partner trust" are defined in s. 248(1) of the Act. An "alter ego trust" means "a trust to which paragraph 104(4)(a) would apply if that paragraph were read without reference to subparagraph 104(4)(a)(iii) and clauses 104(4)(a)(iv)(B) and (C)" and a "joint partner or common-law partner trust" means "a trust to which paragraph 104(4)(a) would apply if that paragraph were read without reference to subparagraph 104(4)(a)(iii) and clause 104(4)(a)(iv)(A)". The effect of these exclusions is that an alter ego trust is a trust that:

(1) is an *inter vivos* trust (s. 104(4)(a)(ii.1));

(2) is created after 1999 (s. 104(4)(a)(ii.1));

(3) is settled by a person over the age of 65 (s. 104(4)(iv));

(4) provides that the settlor is entitled to receive all of the income of the trust that arose before the settlor's death: (s. 104(4)(iv)(A));

(5) provides that no person except the settlor could, before the settlor's death, receive or otherwise obtain the use of any of the income or capital of the trust (s. 104(4)(iv)(A)); and

(6) does not elect out of being an alter ego trust (s. 104(4)(a)(ii.1)).

A joint partner trust is a trust that is:

(1) is an *inter vivos* trust (s. 104(4)(a)(ii.1));

(2) is created after 1999 (s. 104(4)(a)(ii.1));

(3) is settled by a person over the age of 65 (s. 104(4)(iv));

(4) provides that the settlor or the settlor's spouse (whether by marriage or common law), in combination with the spouse or the settlor, as the case may be, entitled to receive all of the income of the trust that arose before the later of the death of the settlor and the death of the spouse (s. 104(4)(iv)(B) and (C);

(5) provides no other person could, before the later of those deaths, receive or otherwise obtain the use of any of the income or capital of the trust (s. 104(4)(iv)(B) and (C); and

(6) does not elect out of being a joint partnership trust (s. 104(4)(a)(ii.1)).

Subsections 73(1), (1.01) and (1.02) of the Act permit property to be transferred by the settlor into a trust meeting the above conditions on a rollover basis provided that the transferor and the transferee are resident in Canada. Subsection 73(1) permits the settlor to elect out of the rollover. In the case of an alter ego trust, capital gains taxes will not be triggered until the death of the settlor and, in the case of a joint partnership trust, capital gains taxes will not be triggered until the date of the death of the surviving spouse: s. 104(4)(a). The 21 year deemed disposition will similarly not apply, unless the taxpayer otherwise elects under s. 104(4)(a)(ii.1).

Similar to spousal trusts, although the Act restricts the use of the capital and income of the trust during the lifetime of the settlor, in the case of an alter ego trust, and each of the settlor and the spouse, in the case of a joint partner trust, the Act does not restrict the creation of a remainder interest from those trusts. Therefore, the trusts provide a flexible tool for settlors to provide for testamentary gifts, whether outright or on additional trust terms, on the death of the settlor or the surviving spouse.

Changes to the Act effective 2016 created a potential tax mismatch for alter ego, joint partner and self-benefit trusts. Under new s. 104(13.4), as the tax owed on the deemed disposition of the trust property on the death of the settlor, or the surviving spouse in the case of a joint partner trust, is deemed to occur in the estate of that beneficiary, and not in the trust itself. Accordingly, there may be insufficient assets available in the estate to meet the tax liability arising in the trust. To address these concerns, Explanatory Notes from the Department of Finance released in October 2014 suggest that these amounts will be sought from the trustee before the estate of the deceased beneficiary under the joint and several liability regime in s. 160 of the Act: Department of Finance, *Explanatory Notes Relating to the Income Tax Act, Excise Tax Act, Excise Act, 2001 and Related Legislation* (October 2014) at 108-109. Amendments to the Act announced on January 15, 2016 would, once enacted, eliminate the tax mismatch by effectively reversing the changes and providing that the tax will be payable in the trust.

2. Self-Benefit Trusts

Subsection 73(1.02)(b)(ii) permits an *inter vivos* transfer on a rollover basis to a trust that benefits the settlor provided that there is no change in the beneficial ownership of the property and there is immediately after the transfer no absolute or contingent right of a person under the trust. While unlike the alter ego trust, the settlor of a self-benefit trust need not have attained the age of 65 years in order to settle this type of trust, the settlor cannot designate a remainder beneficiary and accordingly the property must revert to the estate of the settlor on his or her death. The use of the rollover is therefore limited, although the trust may be a useful tool for incapacity planning for persons under 65 with accrued gains on a capital asset: see John Poyser, Larry Frostiak and Grace Chow, *Taxation of Trusts and Estates: A Practitioner's Guide 2014* (Toronto: Carswell, 2013) at 142.

C. Estate Freezes

A common strategy to defer taxation of future capital gains is the estate freeze. One of the purposes of an estate freeze is to transfer the future increase in value of capital property to another individual or individuals so that those gains will not accrue in the hands of the freezor. The effect is that the amount of capital gains on the property that will be paid by the estate of the freezor is capped as of the date of the freeze; future accrued gains will be paid by the individuals receiving the growth.

There are several ways to structure an estate freeze. Frequently, the freeze will be structured by transferring assets with accrued growth to a corporation controlled by the freezor. Transfers to a non-arm's length party are usually considered deemed dispositions for an amount equal to the fair market value of the property transferred: s. 69(1)(b). Where, however, the property transferred is eligible property (which includes "capital property": s. 85(1.1) of the Act), s. 85 of the Act may be utilized to roll the property into a taxable Canadian corporation without incurring capital gains tax if the freezor receives consideration for the property transferred that includes shares of the corporation and the taxpayer and the corporation jointly elect that s. 85 will apply. The transfer can occur for any amount between the adjusted cost base and the fair market value of the property. The shares received by the freezor will often take the form of preferred shares with a redemption value of an amount equal to the fair market value of the property received (if the taxpayer wishes to rollover the amount of the property transferred). Alternatively, a lesser redemption value may be used and with the difference in the fair market value being made up by some other fixed value consideration, as, for example, a promissory note.

The persons receiving the future growth shares of the company will often receive common shares that rank behind the preferred shares in priority on the liquidation of the company up to the amount of the redemption amount of the preferred shares and with restrictions on payment of dividends if it will render the company unable to pay the redemption amount of the preferred shares. The freezor may also wish to retain control over the company, and accordingly the assets transferred, during his or her lifetime. This can be achieved, for example, by removing or restricting voting rights on the growth shares, through the number of votes carried by the preferred shares or the number of preferred shares issued to the freezor, or by issuing the freezor low value shares with super-voting rights. The CRA has confirmed that it will not take into account any premium that could be attributable to such shares, but caution should still be advised in this respect: Income Tax Technical News No. 38, September 22, 2008.

Where shares are being transferred, the freeze may be structured by transferring the shares to a holding company from which the beneficiaries receive the common shares, and the freezor receives growth shares, with the terms described above. Section 85 of the Act may be used in these cases so that the transfer of the shares to the holding company is on a rollover basis. This type of freeze structure is typically referred to as an "external freeze".

Alternatively, the freezor may undertake an "internal freeze" where the shares of the corporation are rearranged into freeze configuration. In an internal freeze, the freezor exchanges his or her growth shares for preferred shares in the corporation on terms similar to those described above, and the growth shares are transferred to the beneficiaries of the freeze. A rollover is available under s. 86 of the Act in these cases if the freezor disposes of all of his shares in a particular class in return for new shares. Unlike the s. 85 rollover, no election is required for the rollover to apply, though the freezor will have a reportable disposition.

See Robert Dunseith, *Estate Freezes: What, Why, When and How* (Legal Education Society of Alberta: Edmonton, 2012), online: www.dcllp.com for further discussion.

Rather than transfer the shares to the persons following the future growth directly, additional flexibility can be achieved by transferring the shares into a discretionary trust for the benefit of the freezor and his or her family. Careful consideration of the personal, corporate and trust attribution rules will be needed in these cases, which ultimately may result in any dividends paid on the shares and capital gains on their disposition being attributable to the settlor or freezor. Commonly, these rules are avoided by ensuring that the growth shares are purchased by the trust with funds received from an interest-bearing loan under the terms of which interest is payable, and is actually paid, within 30 days of the end of each year, ensuring that trust property cannot be distributed to persons who are "designated persons" with respect to the freezor (which includes the freezor's spouse, or a minor child, grandchild or nephew or niece of the freezor) and ensuring that the freezor is not the settlor of the trust if he or she will also be the trustee. In each case, reference should be had to the attribution rules before a freeze is undertaken.

D. Gift of the Right of Survivorship

The Supreme Court of Canada in *Pecore v. Pecore*, 2007 SCC 17 contemplated in *obiter* that a joint tenant of a property might gift his or her right of survivorship to that property while retaining the beneficial interest during his or her lifetime. As there is no change in beneficial ownership, the Court considered that there would appear to be no disposition at the moment of the transfer and accordingly tax would not be payable at that time. Neither the courts nor the CRA have yet to consider how this method of *inter vivos* giving will be taxed, and the *Pecore* case appears to be unique among jurisprudence in treating the right of survivorship as a separate and alienable property right rather than a quality incident to joint tenancy. Accordingly, the efficacy of this form of transfer for deferring tax should be approached cautiously.

IV. Conclusion

The above illustrates that there are a variety of planning opportunities available to practitioners in order to defer capital gains that arise on taxable dispositions. In each circumstance, care should be taken to explore the options for deferral that may be beneficial to the client, as well as opportunities for avoiding the amount of tax owing through applicable exemptions, or reducing the amount of tax owing by applying losses or credits.

It is important to remember in all cases that avoiding tax is only one objective of an estate plan. Ensuring that property is transferred to persons who are capable of managing such property at the time of the transfer, accounting for the dynamics of the client's relationships, maintaining sufficient assets to provide for the client's ongoing needs in various exigencies, pursuing plans that are flexible and can be altered, and implementing plans that are cost-effective to the client are all factors that may influence what planning structure may be appropriate.

See the *BC Estate Planning & Wealth Preservation* practice manual published by the Continuing Legal Education Society of British Columbia for further information with respect to tax deferral strategies.