CHAPTER ONE
AN INTRODUCTION TO CANADIAN INCOME TAX LAW

Chapter one introduces you to the income tax system, including how tax law is enacted by government. It also reviews the primary and secondary sources of tax law and additional government publications that are relevant to the administration of the tax system. The following five exercises are designed to allow you to practice basic research with respect to resources available on public websites. Exercise six is intended to help you consider the rational and process the government would follow for making changes to tax law, and the answer goes beyond the material contained in Chapter One for the purposes of illustration.

REVIEW QUESTIONS

1. Search the Canada Revenue Agency website to find an IT Bulletin on the criteria for determining whether an individual is a resident of Canada, and whether an individual has become a non-resident of Canada. In addition to the IT Bulletin, what other information or publications are available on the website?
2. Find a copy of the investment income schedule for an individual tax return (the individual tax return is called a "T1").
3. Find subsections 104(1) and (2) dealing with the basic rules for taxation of trusts as individuals and the right of CRA to treat multiple trusts as one trust.
4. Look up the reported decision in the Eurig case mentioned in Chapter One.
5. With what countries does Canada have an income tax treaty?
6. Consider the following scenario:

   You are a senior advisor in the Department of Finance in the tax policy branch. It appears that a particular section of the Income Tax Act is being interpreted to permit all employees to claim personal automobile expenses against their employment income. This is in part because of some ambiguous wording in the ITA, and in part because of a recent Tax Court case interpreting the legislation in an unintended manner. The issue has become political, because only employees who drive to work for a distance of less than 20 kilometres each day can take advantage of this apparent loophole. This makes the advantage" unfair" to those who drive more than 20 kilometres to commute, and discourages the use of public transit. In addition, the practice of making this deduction has become extremely popular and several articles have appeared in the print media suggesting methods of taking maximum advantage of this deduction, including methods to inflate automobile expenses for this purpose.

   Prepare a memo for the government suggesting:

   a) The reasons for taking actions to remedy this situation. Assume that the deduction of these expenses is contrary to fiscal and tax policy since personal expenses, which

include transportation, are not supposed to be deductible from employment income. Assume also that tax policy dictates fairness to all employees, and that public transit is to be supported.

b) what actions CRA could take
c) what actions the Department of Finance could take
d) the pros and cons of the actions by CRA or Finance along with the recommended course of action.
e) Assume an amendment to the Act is recommended. Describe the process the proposed amendment to the Act would take in order to be enacted.
f) Same as (e), but discuss the effective date and transitional rules, if any, that might be appropriate for any amendment.

SUGGESTED ANSWERS TO QUESTIONS

1. IT-221R3 *Determination of an Individual's Residence Status* is the IT Bulletin referred to. CRA's website can be located by including "CRA" in almost any search engine and the general link is at www.cra-arc.gc.ca. The IT Bulletin can be located by using the search function in any number of ways. Publications can be searched by type of publication, or the site can be searched for general information.

Entering "resident" gives a number of options, 5 being "Non-residents of Canada". This links to an information page ("NRC") and the link to IT-221R3 are located at the bottom of the page. There is also a form, Form NR74 *Determination of Residency Status (Entering Canada)* referenced on NRC, but this is not for persons leaving Canada. To find that, you can click on "Return to Individuals – International and Non-resident Taxes" at the top of the NRC and look for the link to "Leaving Canada (emigrants)." Following this link, you will also see another link to IT-221R3 and a link to Form NR74 *Determination of Residency Status (Entering Canada).*

2. On the CRA website from the home page click "Forms and publications." You could click on "Tax Packages" then click on the relevant year, and then click on the relevant province. Look at the options on the provincial change – you will see Schedule 4 "Statement of Investment Income.

3. While federal statutes are on the Department of Justice website, the navigation capability is not suitable for a statute as large as the Income Tax Act. Enter CanLII into any search engine to reach the CanLII website. Click on "Federal" and enter "income tax act" in "2" under "statute name". The current act will appear as a link under results. You can then click through the table of contents to see subdivision k – "Trusts and their Beneficiaries [104. – 108.]" and click there to open up the listing of all the subsections in section 104. You will see a listing of subsections (1) to (31) and you can access any of these subsections by clicking on the listing.

4. Open the CanLII website on your browser and type "Eurig" in the "full text" box. The three decisions of the Ontario Superior Court of Justice, Ontario Court of Appeal and the Supreme Court of Canada will appear as the first three items.

5. In the CRA website search box type "tax treaty". The first result will be "Tax treaties." This will lead you to a page on Tax treaties. Under "Topics about Tax treaties" there is a link to

the Finance Canada Web Site for "Treaty countries." This will lead you to the Finance Canada website page on tax treaties. On the page you will see:

STATUS OF TAX TREATIES

- I. In force
- II. Signed but not yet in force
- III. Under negotiation/re-negotiation

If you click on the "In force" link you will be connected to the following page that lists all the countries with which Canada has a current tax treaty:

http://www.fin.gc.ca/treaties-conventions/treatystatus_-eng.asp#status

You may also view IC76-12R6 *Applicable rate of part XIII tax on amounts paid or credited to persons in countries with which Canada has a tax convention* which lists the relevant withholding rates of non resident tax on amounts paid or credited to non-residents. This will give you a general idea of the countries with which there is a tax treaty but the Finance Canada website will provide more up-to-date information about particular treaty status. Nevertheless this IC is very helpful as a general rule in determining if there is a treaty, and if so the rate of withholding on particular payments of income to non-residents of Canada. This IC may be looked up directly if you know the number by using a publications search, or using a topic search "rates of non resident tax" and limiting the search to CRA publications will bring it up in the list of search results.

6.

a) Reasons for taking action:

- To prevent loss of revenue
- To make sure all employees are treated equitably
- To support public transit
- To remedy ambiguity relating to the application of the Act.

b) CRA through the Department of Justice could appeal the Tax Court case and Finance could wait for the results of such an appeal.

c) Minister of Finance could introduce an amendment to the Act to make it clear that these expenses are not deductible by employees.

d) There are many disadvantages to an appeal: These include delay and loss of revenue in the meantime. If the appeal is against the taxpayer, the only way to recover revenue from employees filing in accordance with the Tax Court decision is to assess these returns and hold any taxpayer objections or appeals in abeyance until the case is finally resolved. This involves significant administrative costs given the large number of taxpayers potentially involved. In addition, if there really is ambiguity in the statute any further appeal may be resolved in favour of the taxpayer resulting in loss of revenue throughout the appeal period. An appeal would take time to resolve, particularly if the case continued under appeal through

the courts from the Federal Court of Appeal all the way to the Supreme Court of Canada. An amendment would be faster, and would provide a certain outcome, and protect revenues.

e) This could be done by notice of ways and means following an upcoming budget, or even in a technical bill without being subject to the budget process since there is no real change in tax policy relating to the amendment – it simply addresses an ambiguity that has turned into an inappropriate loophole. The amendment would have to pass several readings in the house (Parliament) and the Senate and would then have to receive Royal Assent before becoming law.

The effective date could be upon Royal Assent, or upon the budget date or the date of release of the technical bill. While the amendment could be retroactive, this is rarely done with tax amendments and only in extraordinary circumstances. It could be effective for the current taxation year, since no returns for the current taxation year would have been filed or assessed. If this was perceived to be unfair, because expenses were incurred in the current year on the understanding that they would be deductible, some kind of grandfathering might be possible, but for policy reasons this would probably not be appropriate. For taxpayers who took the deduction of expenses for prior years, or incurred such expenses before the budget date or introduction of the technical bill, the government could announce its intention to appeal the Tax Court decision and let the outcome of that case determine the status of pre-amendment expenses. This is the most likely scenario, assuming that Finance considers the Tax Court decision to be wrong in law and promoting inappropriate behaviour and contrary to tax policy that personal expenses are not deductible from employment income.

CHAPTER TWO

BASIC TAXATION AND SOURCES OF REVENUE OF INDIVIDUALS

REVIEW QUESTIONS

1. Indicate whether the following receipts are income from property or income from a business and explain why.

Alana owns an apartment building and earns rental income from her tenants.
Alana makes custom drapes as sells them to her tenants.
Alan buys some bonds issued by Morning Glory Motels Corporation. They pay an interest rate of 5% per annum.
Alan is an inventor as well as an investor. He earns royalties from his patent on the ThingerMaBob Machine.
Alan carries on a dental practice. He purchased the practice and all equipment from a retiring dentist.
Alan falls on hard times and must sell the patent rights to the ThingerMaBob invention. He sells the rights for 500,000.

2. Mr. Sorenson was born in Nova Scotia and lived and worked there all his life. When he was ready to retire, he decided to leave Nova Scotia to reside in Bermuda. He sold the family home in Nova Scotia and leased one in Bermuda instead. He and his wife lived in Bermuda for a number of years. However, Mr. Sorenson's wife missed her friends and family in Canada and so persuaded her husband to buy an expensive home in Nova Scotia, which Mr. Sorenson and his wife live in for four months of the year.

Discuss briefly whether Mr. Sorenson and his wife now reside in Canada for tax purposes. List the relevant factors in determining whether Mr. Sorenson and his wife reside in Canada for tax purposes and some of the questions you might ask to help determine how CRA or the courts might determine residence for tax purposes.

Assume the Sorenson's were both born in the US and never resided in Canada prior to their purchase of the Nova Scotia property which they use purely as a summer vacation home

3. Georgiana is resident in Canada, but all her income is earned on investments abroad. Will she have to report this income on her Canadian tax return?

4. True or False: The following expenses are deductible:

a) interest on funds borrowed to acquire interest-bearing securities
b) interest on the mortgage that financed the purchase of a principal residence
c) investment counselling fees
d) interest incurred to contribute to a Tax Free Savings Account
e) interest at 5% to purchase preferred shares yielding fixed dividends of 2%

5. True or False: The following are current (as opposed to capital) expenses for the owner of an apartment building.

a) Repairs to plumbing in one rental unit
b) Replacement of pipes in an entire building
c) Regular maintenance of a lawn
d) Paving a parking lot
e) Replacing burnt out light bulbs in hallways
f) Snow removal
g) Preparation of income statement from the rental property for the purpose of income tax returns
h) Replacing all appliances in the units.

6. Identify which of the following will produce income from employment (as opposed to income from a business):

Lester works 35 hours a week in the shipping department of a store owned by a retail chain and is paid on an hourly basis.

Jacob freelances as a graphic designer and web developer for small businesses across Canada. He works from home on a contract basis with his clients.

Jennifer retired as a broadcast journalist from CXN TV 2 years ago but she still makes cameo appearances on CXN and several other media outlets for a negotiated fee for each appearance.

Allison is an associate lawyer specializing in wills and estates. She shares office space with a boutique commercial law firm and pays rent to the firm on a monthly basis. The firm refers clients to Allison, but she also has clients of her own.

Fred is an expert tailor. He has renovated his home to include a separate entrance to a luxury showroom where his customers chose fabrics and design, and where measurements and fittings are made. He also sews made to measure suits in his home work studio for a small number of high-end men's clothier outlets in his home city including that of his brother-in-law.

Fred is an expert tailor. He earns a flat fee for each made-to measure suit he makes for his brother in-law who owns a tailor shop. His brother in-law supplies all the fabric and equipment and Fred does his work in a small cutting and sewing room in the basement of the shop. Fred is

required to be on the premises during business hours to be available for customers who need to be measured and for fittings.

7. How do non-capital losses from previous years affect the calculation of tax payable by an individual? What if an individual has no net income for a particular taxation year?

8. Once taxable income is calculated how is the amount of tax payable by an individual calculated before any tax credits? Are the provincial tax rates for individuals applied to taxable income as calculated using the ITA or to federal tax payable? Assume the question addresses provinces other than Quebec.

9. Jerry is an elderly retiree who lives below the poverty line on a small pension. He receives so little income that, after the basic personal credit has been applied, his tax payable is zero. A charity promoting a worthy cause calls Jerry annually asking for donations. Jerry feels unable to turn them away, and has contributed $200 to charity this year. Can Jerry take advantage of the charitable donations credit?

10. What is the purpose of the dividend gross-up and credit mechanism? Does it achieve its purpose?

SUGGESTED ANSWERS TO QUESTIONS

1. See the Appendix to Chapter One and 2.2.1 and 2.2.2.3
Rental income is generally considered income from property.
Manufacturing goods for resale is considered a business activity, and the drapes are inventory.
Interest income from bonds or other financial instruments or securities are generally income from property.
Royalties are income from property (the patent is the property, in this case).
Income from the dental practice is business income since the income is generated from the professional services provided by Alan, not by any property.
Proceeds from the sale of a patent are treated as a capital receipt rather than as income from property because the patent is capital property – i.e. it generates royalty income

2. See 2.1.4 and the criteria set out in IT-221R3. There is not a clear answer as to whether the Sorenson family became non-residents of Canada. The most important factor is their prior period of residence in Canada. The facts are very loosely based on *Thomson v. Canada*, [1946] S.C.R. 209. In general, it is difficult for an individual who once resided in Canada to show that

he or she is no longer resident for tax purposes. While it may have been clear that the Sorenson family became non-residents when they first left Canada, the fact that they subsequently purchased a residence in Canada that is available through the year and use the home for four months every year will cast doubt over their intention to become non-residents and sever all ties from Canada. The individual should be prepared to show that he or she is filing tax returns in the foreign jurisdiction.

Relevant factors are:

- ⇒ close family and social ties to Canada
- ⇒ historical citizenship and presence in Canada
- ⇒ the fact that Mr. Sorenson owns a house in Canada and only leases a house in Bermuda
- ⇒ the fact that Mr. Sorenson only lives in Canada for four months of the year

Questions you might ask:

- ⇒ how many years did they live in Bermuda without purchasing the property in Nova Scotia, and how much did they visit Canada during this period
- ⇒ whether he has relinquished his Canadian citizenship
- ⇒ whether he pays taxes in Bermuda (or on property in any other jurisdiction)
- ⇒ whether he has obtained citizenship in Bermuda, or whether he still maintains a valid Canadian passport
- ⇒ whether he maintains ties to social or religious organizations in Canada, or whether he has formed new ties in Bermuda
- ⇒ whether he still qualifies for provincial medical insurance in Nova Scotia
- ⇒ whether he still has a valid driver's licence in Nova Scotia
- ⇒ whether he maintains a membership in a union or professional organization
- ⇒ whether he still has dependants, e.g. young children or elderly parents, in Canada

In another fact situation, it might be relevant whether the individual has a spouse or common law partner residing in Canada or Bermuda.

Had the Sorenson family never resided in Canada prior to purchasing the Nova Scotia residence they would not be considered residents of Canada. The purchase of a vacation property and part-time use of that property is not sufficient to cause them to lose their residential ties to the US and establish residency in Canada.

3. Yes. Canadian residents are taxed on worldwide income – see 2.1.4. Any investment income must be reported in her Canadian income tax return regardless of the country of origin. If she pays tax in the foreign jurisdiction, she may be eligible for a foreign tax credit to reduce her tax payable in Canada on foreign source income. Canada may also have tax treaties with the

countries where Georgiana earns this income, which may reduce the amount of tax she pays in the other jurisdictions.

4. See 2.2.1.3 and 2.2.3:

a) true
b) false
c) true
d) false
e) false (

5. See 2.2.1.9:

a) true
b) false
c) true
d) false
e) true
f) true
g) true
h) false

NOTE: Neither b) nor d) is incurred for the purpose of earning income: the mortgage interest is a personal expense, and the income from TFSA's is not taxable. In e) interest expenses in excess of the grossed up dividend on preferred shares will not be deductible under CRA's administrative policy although technically the entire amount may not be deductible.

6. Items a) and f) produce income from employment.

Note: Refer to section 2.2.2.2, which lists the tests for income from employment vs. income from business. When characterizing such income, ask: who controls the work (e.g. where and when it occurs), whether the individual owns her own tools, who bears the risk of profit or loss (if the individual bears the risk, he or she is likely earning business income), and whether the individual's work is integral or ancillary to the work of the organization.

7. See 2.3.1 and 2.4 Unused non-capital losses from any of the 20 prior taxation years may be deducted from taxable income. Since the rates of tax payable are applied to taxable income, a reduction in taxable income results directly in a reduction of tax payable at the relative marginal tax rate of an individual. Taxable income is calculated *after* net income for tax purposes (which reflects only the current year's gains and losses). Net income for the year must be calculated before deductions from taxable income, such as non-capital loss carry-overs, can be applied to

arrive at taxable income. If there is no net income, the non-capital loss from prior years may be available to be carried forward to a future year, subject to the 20 year expiry for carry forwards.

8. See 2.1.4 and 2.4. Federal tax is calculated applying the graduated federal rates of tax to taxable income as calculated under the Act. Depending on the province of residence on December 31 of the relevant taxation year, the relevant provincial tax is calculated separately. For residents of Quebec a separate return and separate calculation of taxable income is required.

Note: Under the current federal provincial tax collection agreement, provincial tax is calculated as a percentage of taxable income as calculated under the federal Act. This is not the case in Quebec, which has its own system for computing taxable income.

9. No. The charitable donations credit, like most other personal credits, is non-refundable. This means that when an individual has no tax payable to soak up the credit, the individual does not benefit from the credit. If the credit were refundable, Jerry would be able to advantage of the credit as a direct receipt. See 2.4.2.

Note: However, Jerry may carry forward any unused donations and claim them on his return in any one of the five following taxation years. If there is sufficient income in those years he may be able to generate a credit and offset tax payable.

10. The purpose is to have the individual pay his or her individual tax rate on the before-tax value of the income and then to refund to the individual the corporate tax paid. In theory, this should eliminate double tax on dividend income. In practice, the individual may be over- or under-compensated for corporate tax paid. See 2.2.1.4.

CHAPTER THREE
TAXATION OF CAPITAL GAINS

REVIEW QUESTIONS

1. True or False: Each of the following types of capital property qualifies for the capital gains exemption

   a. Shares of a Canadian Controlled Private Corporation, qualified farm property and qualified fishing property

   b. Shares of a Small Business Corporation, qualified farm property and qualified forestry property

   c. Shares of a qualified Small Business Corporation, capital property transferred to a qualified spousal or common-law partner trust and a principal residence, or

   d. Shares of a qualified Small Business Corporation, qualified family farm property and qualified fishing property

2. Discuss the following scenarios with respect to whether the transactions would produce capital receipts, or income receipts.

   a. Ramseh's very successful restaurant, the Shawarma Palace Eatery, operating as a sole proprietorship, is being sold. Ramseh is selling all the assets of the business including the real property the restaurant is located on, as well as all the equipment and the furniture used in the restaurant.

   b. Jessie is a real estate agent who buys and sells residential real estate on a regular basis. Sometimes she makes improvements, such as an updated kitchen with granite countertops and fresh decorating and "flips" the properties for a quick profit. Other times she rents the properties for a limited time and sells them whenever she thinks the opportunity for sale at a profit is good and she can reinvest her money in another potential money maker.

   c. George is an artisan who makes and sells clay pots. His business is not going well, so he decides to mark down his entire existing inventory of pots and dispose of them at a close of business sale.

   d. A farmer who owns a large farm property north of Toronto sells the entire acreage to a land developer. Her family has owned and farmed this property for generations.

3. Will the receipts in the following scenarios be treated as income receipts or on account of capital? Give your reasoning.

    a. A farmer who owns a large farm property north of Toronto subdivides the property at considerable expense, and starts selling the separate parcels to developers as the land increases in value. Her family has owned and farmed this property for generations.

    b. Anna and Orlando, two wealthy investors, purchase a plot of land near a highway intending to develop it into a shopping mall. They realize their business venture will fail when another shopping mall is developed nearby and their prospective cornerstone tenant – Big Box Bargain Barn - declares bankruptcy. They sell the plot of land for a large gain.

    c. Leanne purchases a cottage property, intending to use it for leisure in the summer. The building on the property is a real fixer-upper and Leanne invests a lot of time and money developing it into a modern, comfortable get-away from city life. After 5 years time, Leanne realizes that she does not have enough spare time to take full advantage of her cottage and she sells the property at a gain.

4. What is the effect of adding the costs of acquisition to the adjusted cost base (ACB) of a property? Why would the taxpayer want to do this?

5. Fatima disposes of capital property in year 1 for proceeds of $200,000 and a capital gain of $125,000. Fatima will receive the proceeds over a 5 year period in equal annual instalments, commencing in the year of sale. Assuming Fatima elects to take maximum advantage of the capital gains reserve:

    a. How much capital gain will be included in her income in each of the 5 years?

    b. In year 3, the purchaser decides to pay the entire balance outstanding. How much of the capital gain should be reported in year 3?

    c. Assume Fatima will receive the proceeds over 10 years in 10 instalments of $20,000. How must she report these proceeds, assuming she elects to take advantage of the capital gains reserve?

6. A resident of the U.S. owns 50% of the voting shares of a private corporation that was incorporated in Canada and is resident in Canada. The other 50% of the voting shares are owned by a Canadian living in Canada. Does the business qualify as a Canadian Controlled Private Corporation? Explain your reasons.

7. A CCPC has 80% of its assets invested in debt instruments in SBCs that pay an interest rate of 5%. Does the CCPC qualify as a SBC?

8. Robin and Linda are a same-sex couple who have lived together since 1995. In 2000 Robin purchased a home for the two of them for $100,000 using money inherited from her uncle. In 2004, when the fair market value of the home was $150,000, Robin gifted the home to Linda. In 2009, after living in the home together since it was purchased, Linda and Robin decide to move and Linda sells the home for $410,000.

   Describe the tax consequences of the purchase, the gift and the sale. Assume that a transfer of a principal residence between spouses or common-law partners deems the transferee to have owned the property for the same period as the transferor and that the property will qualify as a principal residence for any years that it qualified for the transferee.

   Consider how the following additional facts might affect the tax consequences of the sale of the home. Robin and Linda also jointly purchased a country retreat in the Gatineau's in Quebec in 2008 for $300,000. All acquisition costs and mortgage payments are funded by them equally from their own independent resources. In 2010 the property is worth $300,000 but they expect the value to increase in the future.

9. Alexandre is the sole shareholder of his own Small Business Corporation, MogulGold Enterprises. He invested $1,000,000 in the company 10 years ago. This year, Alexandre realized he was not cut out to run MogulGold efficiently, as it had yet to turn a profit. Alexandre sold his shares of the business at loss of $500,000 to another business person, who thinks she can turn MogulGold around. Fortunately, MogulGold is not Alexandre's only source of income. He will also earn $200,000 of employment income in the year.

   a. What will Alexandre's income for tax purposes be? Will there be consequences for other tax years?

   b. Assume Alexandre's interest in MogulGold was in the form of debt instruments which have become uncollectable. MogulGold has become insolvent (instead of being sold off). All other facts are the same. Alexandre comes to you for advice. What should you tell him to do?

10. Natalie is a diet pop fanatic. She gets wind of a rumour on the internet that products containing artificial sweeteners will soon be banned from North American markets. In response, Natalie drives around her hometown of Edmonton and purchases the entire stock of diet pop in every grocery store she can find. Her intention in stockpiling diet pop is (1) to ensure her own security of supply when diet pop is banned; and (2) to sell the diet pop at an enormous profit on the black market for diet soft drinks that will surely emerge after the ban. Natalie is disappointed to discover that the rumour on the internet was a hoax and she arranges to sell her entire stockpile at a discount to a local dollar store.

    a) What are the potential income tax consequences of the sale of the stockpile of pop at a loss?

    b) What additional information might be relevant in determining the tax treatment?

    c) Explain how would you characterize the tax treatment and give reasons.

SUGGESTED ANSWERS TO QUESTIONS

1. True or False

   a. False

   b. False

   c. False

   d. True

2. Transactions on income account or capital account. Items a) and d) will produce capital receipts. In b), because Jessie is in the real estate business, has frequent transactions and a short holding period her sale of real estate will likely be treated on income account. In c), George is selling inventory and any gain or loss will be on income account.

3. Capital versus income receipts

   a. This could be income from a business since it appears the farmer had the intention to resell the land at a profit. Although the land was no doubt capital property when it was being used solely for farming in the past, there has now been a change in intention and any gain in value after the new intention to resell at a profit will likely be treated on income account. (The Act provides for a deemed disposition on change of use in such a situation, but the details are beyond the scope of the course.) If the farmer had not taken pro-active steps to prepare the land for resale at a profit – i.e. the subdivision of the property - the gain would likely be treated on capital account.

   b. The owners intended to develop the land to build retail premises that would be a source of rental income. This stated intention would support the argument that the land is capital property. On the other hand, when investors "flip" vacant land at a profit without developing it, it may be presumed that notwithstanding any expectation of development there is likely a secondary intention to sell the land at a profit and thus a resale of vacant land will be treated as an "adventure or concern in the nature of trade" on income account. These facts are loosely based on those in the landmark decision Regal Heights Ltd. v. M.N.R. [1960] S.C.J. No. 56. The court in that decision found that the gain was income and thus fully taxable. This was based on the fact that the purchase of the land was partly speculative and that the investors could foresee that if the shopping mall venture failed, a profit could likely be realized on re-sale of the land in any case.

   c. The question here is whether the property was intended for personal use (or in some cases to produce income if it had been intended as a rental property) or whether it was a speculative venture by which Leanne expected to turn the property for a profit. In order to determine the taxpayer's intention, the courts will examine the actions of the taxpayer. Where real estate consists of a personal residence that was enjoyed by the taxpayer for personal use, whether as a full time residence or as a

vacation property, it is likely to be treated as capital property. The fact that the property was sold at a profit after five years and turned out to be a good investment will not convert the property into inventory. The improvements were not made to earn a profit, but to increase Leanne's enjoyment of the property. Her reason for selling is relevant as well – her ability to make use the property changed – this was not a case where she was simply holding the property until the most opportune time to make a profit. See Interpretation Bulletin IT-218R, "Profit, Capital Gains and Losses from the Sale of Real Estate, Including Farmland, Inherited Land, and Conversion of Real Estate from Capital Property and Vice Versa," September 16,1986.

4. Increasing the ACB by the costs of acquisition of a property causes the ACB to reflect the true cost to the taxpayer of acquiring the property. When the taxpayer disposes of the property, any capital gains will be reduced by the costs of acquisition and any losses will be increased by the costs of acquisition.

5. The income inclusion under the capital gains reserve rules ensures that at least 20% of the taxable capital gain will be included in each of the year of the sale and the following 4 years on a cumulative basis. However, if 50% of the total amount of the proceeds actually received exceeds this amount, the greater amount will be included in income after taking into account what has already been included in previous years.

    a. Fatima will receive no more than 20% of the proceeds in each year, and as a result need only include 20% of the capital gain in year 1, the year of sale and each of the following four years, years 2, 3, 4 and 5. Thus $25,000 of gain will be reported in each of these years 50% of which will be included in income as a taxable capital gain (50% capital gains inclusion rate).

    b. Because the remainder of the proceeds are received in year 3, no reserve will be available and the balance of any unreported gain must be included in year 3. Since $50,000 of the capital gain will have been reported cumulatively in years 1 and 2, the remaining gain of $75,000 must be reported in year 3, 50% of which will be included in income as a taxable capital gain.

    c. The reserve can be claimed over a maximum of 5 years and at least 20% of the taxable capital gain must be reported in each year. This means that Fatima will have to report $20,000 of taxable capital gains in each of the first 5 years even though she will not receive the full proceeds for 10 years. It is as though Fatima were receiving $40,000 of proceeds for each of the first 5 years for tax purposes.

6. Yes the corporation will qualify as a CCPC. CCPCs do not have to be controlled by Canadians. The definition requires that they not be controlled by non-residents or public corporations or a combination of the two.

7. More information is required to determine if the corporation qualifies as a SBC. An SBC must satisfy the 90% test set out in 3.3.2.3. If the SBC issuing the debt instrument is connected to the CCPC then the debt will be a qualifying asset for the purpose of the 90% test. Assuming the debt is from a connected SBC, the remaining assets of the CCPC must be examined to determine if another 10% of the assets qualify to permit the CCPC to meet the 90% test. In the event the debt issuer is not connected to the CCPC, it will not be a

SBC since the debt instrument will produce income from property and will not be considered an "active business" asset for the purposes of the 90% test.

8. Robin and Linda:

The purchase would result in Robin having an ACB of $100,000.

Most of the rules in the Act relating to married persons (i.e. spouses); including the rules for the spousal rollover and those relating to the principal residence exemptions apply equally to common-law couples. A common-law relationship includes two persons who live together in a conjugal relationship and includes two persons of the same gender. Since Robin and Linda commenced living together in 1995, they would be considered to be in a common-law relationship since 1997.

The gift to Linda in 2004 will be a deemed disposition for tax purposes, but because of the common-law relationship this will be deemed to take place on a rollover basis for proceeds of disposition equal to Robin's ACB of $100,000. Linda will be deemed to have acquired the property for $100,000. This assumes that Robin did not elect out of the spousal rollover when she made the gift. Since they are common-law partners, for the purpose of the principal residence exemption, Linda will be deemed to have owned the property since 1999 and it will qualify as a principal residence to Linda during the years Robin owned it.

When Linda disposes of the property there will be a capital gain of $310,000 (proceeds of disposition minus ACB of 100,000) which, in the absence of the principal residence exemption would be attributed back to Robin under the attribution rules. However, the principal residence exemption will be available. Since Linda and her common-law partner resided in the property the property will qualify as a principal residence throughout the holding period. The exemption may be claimed for each calendar year in which one or either of them owned the property and the exemption can fully offset the gain on the property.

If Robin and Linda also owed the Gatineau property, Linda needs to consider whether the Gatineau property also qualifies for the principal residence exemption, and if it does, whether the exemption for the years 2008, 2009 and 2010 should be preserved for future use on the sale of the Gatineau property. Recreational use property qualifies as a principal residence as long as it is used primarily for personal use, and not some other use.

A married couple and a common-law couple may only use the principal residence exemption on one property between them for any particular taxation year. Since the principal residence exemption is optional, and the election is made on a year by year basis, it may be claimed for only some of the years during which the property is owned resulting in a partial gain on the property.

It is always possible to elect for one year less than the years of ownership, preserving at least one year for use on another property because of the "one plus" in the formula. The holding period for the home is 10 years since it was owned during 10 calendar years, and Linda needs only to designate the home as her principal residence for 9 years in order to fully offset the gain on the sale. She could consider designating all years but 2008, 2009 and 2010 to preserve those three years for future use on the sale

of the Gatineau property. She would have to weigh the value of the potential future saving against the immediate tax savings for the current sale of the home.

Usually it is best to use the exemption on the property that has the highest gain per year. The gain per year on the home was $31,000 and to date there has been no gain on the Gatineau property, so it may be best to use the principal residence exemption on the home for 9 years to fully offset the current gain and preserve at least one year for the other property.

9. Alexandre

   a. A loss on the sale of shares of a Small Business Corporation qualifies as a business investment loss. An allowable business investment loss (ABIL) is 50% of a business investment loss. ABIL's may be deduced against all sources of income not just taxable capital gains.

   b. Alexandre has an ABIL of $250,000 which will completely offset his employment income for the year. He will also have $50,000 remaining to carry back 3 years or forward for 10. If Alexandre uses the losses to offset income for any of the prior 3 years, he will be entitled to a refund of tax. After 10 years, unused losses may be carried forward indefinitely as ordinary net capital losses.

10. Natalie and the diet pop.

If Natalie's activities can be characterised as a business, or an adventure in the nature of trade, then her net loss on the sale of the pop will be deductible from all other sources of income for the year and any additional amount not required to fully offset income from the current year will be characterised as a non-capital loss capable of being carried forward 10 years and back 3 years. In calculating the net loss, Natalie would be able to include all her expenses incurred in the business activity including not only the actual cost of the pop, but also the non-personal portion of her car expenses for purchasing and delivery, storage expenses if any, and the like.

If Natalie's activities are considered to be for personal purposes, and not a business, then her loss on the sale of the pop will be a loss in respect of capital property that is personal use property and as such will not be disallowed in its entirety.

Additional information that might be helpful in determining whether the activity is a business includes:

a) The quantity of pop purchased: the larger the quantity the less likely the intention is for personal use only.

b) The amount of time and effort spent in the activity: were only a few hours spent or did Natalie devote her full time to the activity? Did the activity take place over a few days or a longer period? Did she rent warehouse space or pay others to assist her in purchasing and transporting the pop?

c) The existence of any financing – did Natalie arrange for a loan to finance the purchase of the pop?

d) Similar business ventures or activity: Has Natalie had any similar business ventures in the past? – The existence of similar activities would tend to show an ongoing course of conduct that is a business.

It will be to Natalie's advantage to characterize her activity as a business activity. She can argue that her main intention was to profit from the resale of the pop, that the purchase was a speculative business venture rather than an acquisition of property for personal use, and the nature of the activity demonstrates a business intention rather than personal use – i.e. that she would not have put so much time, money and effort into buying the pop for personal use. She can argue that the quantity of pop purchased outstripped any personal consumption needs, and the greater the quantity she purchased, and the more time and effort devoted to the activity, the stronger this argument will be.

Additional notes on Question 12.

See part 3.1.3 for a discussion of the factors relevant to determining whether a receipt is capital or income.

In the past, CRA has re-assessed such dispositions (when profitable) as income from "an adventure or concern in the nature of trade". Taxpayers have tried to characterize massive gains on one-time re-sales of commodities as capital receipts so that only 50% of the gain would be taxable, since gains on the disposition of personal use property (such as diet pop, if it were truly for personal use) are taxed as capital receipts. If Natalie had earned a substantial gain on the resale of the pop it would be to her advantage to characterize the proceeds as a capital receipt since only half would be included in income.

For more information on the characterization of one-off sales of commodities, see *M.N.R. v. Taylor* [1956] C.T.C. 189, 56 D.T.C. 1125 (Ex. Ct.). *Taylor* is a leading case which dealt with a speculative purchase of a large quantity of lead. The court characterized the gain as income. Also see *Rutledge v. CIR* (1929), 14 TC 490, which dealt with a speculative purchase and sale of toilet paper.

CHAPTER FOUR
TAXATION OF TRUSTS

REVIEW QUESTIONS

1. The three original trustees and all the beneficiaries of the Luxor family trust are resident in Canada. One trustee dies, and the remaining trustees, who have the authority to appoint a successor trustee under the trust agreement, wish to appoint Ben, a resident of Buffalo, New York. One of the other trustees is quite elderly and in poor health and has expressed the desire to retire in another year or so. Ben has been a family friend of the Luxor's for years and has agreed to drive to St. Catherines Ontario, a 50 minute drive from Buffalo, to attend quarterly meetings of trustees. For tax reasons it is imperative that the trust remain a resident of Canada under Canadian domestic law without resorting to any treaty tie-breaking rules. You are the advisor to the trustees. What advice would you give?

2. Can the following items be flowed through a trust by the trustees to a beneficiary of a trust and retain their character? Answer yes or no. Assume all income is paid or payable to beneficiaries. For any items where you have answered "yes", explain what is required to effect the flow through. Where your answer is "no", explain and provide any additional comments that might be relevant.

    a. Capital gains eligible for the capital gains exemption

    b. Allowable business investment losses

    c. Rental income

    d. Dividends from a foreign corporation

    e. Interest expense

    f. Principal residence exemption

    g. Charitable donation

3. Mary died in 1982 leaving one half of her estate in a qualifying spousal trust for the sole benefit of her husband George during his lifetime, and the other half to a family trust that included George and Mary's three children from her first marriage as beneficiaries. George also created the George Family Trust in 1978 just before he and Mary purchased a home together making his son from his first marriage and any of his son's children as the beneficiaries. George died in 2010. In his Will he provided that the entire residue of his estate be used to create a trust for his disabled grandson Bernie, providing that his son pay all income tax and other expenses arising on his death.

   a. Identify the testamentary and *inter vivos* trusts in this fact situation, and indicate the tax rates applicable to each trust explaining your answer.

   b. For each trust describe when the first and second and deemed disposition of all property will take place under the 21 year rule, assuming that this rule applies to the first deemed disposition under the Act.

   c. Had you been given the opportunity to offer tax advice to George or Mary what changes might you have suggested?

4. List four types of trusts that capital property may be transferred to on a rollover basis and briefly describe such trusts. When will the deferral of tax permitted by the rollover end?

5. Compare the tax attributes of a qualifying spousal or common-law partner trust with a joint partner and common-law partner trust. Break your answer down into the following items:

   a. Beneficiary,

   b. Rights to Income,

   c. Settlor,

   d. Tax consequences of transferring capital property to the trust,

   e. Timing of deemed dispositions,

   f. Whether such trusts are *inter vivos* or testamentary. .

6. Normally trust income is taxed in the trust unless it is paid or payable to a beneficiary, in which case it is included in the hands of the beneficiary, and the trust may make a corresponding deduction from income. Describe the two main exceptions to this general rule, and give some examples of when they apply.

7. In what circumstances does the distribution of capital property of a trust in satisfaction of a capital interest in a trust take place on a rollover basis?

8. What are the tax and non tax advantages and disadvantages of creating a trust for minor children?

9. Discuss the dangers of undocumented trust arrangements.

10. A trustee has approached you for advice relating to the wind-up of an estate. The sole remaining assets consist of a number of shares in publically traded corporations, some with gains since the date of death and others have unrealised losses. One of the two beneficiaries is non-residents. The beneficiaries have suggested you simply divide the portfolio in half and transfer half to each beneficiary. To avoid any tax consequences and "red tape" the trustee has suggested that the assets transferred to the non-resident be selected so that the unrealised gains since death are cancelled out by the unrealised losses. Discuss the tax consequences and the advice you would give the trustee.

SUGGESTED ANSWERS TO QUESTIONS

1. Residence of a trust. In the past under the Thibodeau decision, the courts and CRA looked to the residence of the trustees to determine the residence of a trust, and where there is more than one trustee, the residence of the trustee who manages or controls the trust assets will determine the residence of the trust. The residence of the beneficiaries was not relevant. The traditional approach may be called into question at present based on the *Garron* decision of the Tax Court which decided that the central management and control test relevant to corporations may be the appropriate test. The rational for using the residence of the trustees is that under trust law, trustees may not delegate their duties and obligations and this is very different from the way corporations are managed where delegation is permitted. Until some certainty returns to which test is applicable it may be the most prudent course of action to make sure, if possible, that the residence of the trust is in the appropriate jurisdiction according to both tests.

   The Luxor trust may continue to be resident in Canada even with a US trustee providing that trustee does not manage or control the trust assets. If the trust is silent, all trustees will have to make decisions together which will prevent the US trustee from being able to make decisions without the input of the other trustees. However, the succession of

trustees must also be examined. What happens if one or both of the other trustees die or also become non-residents? Is there a requirement that there always be at least two trustees and that one of them be a resident? If not, can the trust be amended to provide such a term, or is there any other way to guarantee that the US trustee will never become the sole trustee? As the advisor it would be appropriate to examine all the potential circumstances and determine if there is a risk that the trust will be left with only non-resident trustees, and if so, the existing trustees must consider how important it is to appoint the US trustee, as compared to the tax consequences if the trust were to become a non-resident of Canada. If the tax consequences are adverse, the trustees may not be acting in the best interests of the beneficiaries if they permit a non-resident to become a successor trustee.

2. Flow through of items from a trust to a beneficiary

   a. Yes. A trust may allocate capital gains to be received by a beneficiary by making a designation which will result in the 50% inclusion rate and the ability to offset such income by allowable capital losses or net capital loss carry forwards by a beneficiary. Where the trust has realised capital gains in respect of the disposition of property qualifying for the capital gains exemption, an additional designation is required to make the capital gains already designated to qualify for the capital gains exemption in the hands of the beneficiary. While the first designation may be in any proportion among beneficiaries that is reasonable, the second designation must be pro-rata according to the designation of capital gains.

   b. No. No losses of any kind may be flowed through a trust to a beneficiary. (There may be attribution of losses in one limited circumstance where subsection 75(2) applies – see Chapter 9).

   c. No. Although rental income can be flowed through to a beneficiary it can only be allocated as ordinary income, as there is no specific designation to characterise the income as rental income. It would be treated as income from a trust in the hands of a beneficiary.

   d. No. While dividends from Canadian corporations can be allocated to beneficiaries and specifically designated as taxable dividends from Canadian corporations, there is no such designation for foreign dividends. However, a trust may designate foreign income to a beneficiary which will deem any foreign tax on such income to be paid by the beneficiary which may in turn entitle the beneficiary to claim any related foreign tax credit.

e. No. Interest expense is generally deductible from income if it was incurred for the purpose of earning income. However only income, not expenses can be allocated to beneficiaries. The interest expense is deductible by the trust in calculating its income from business or property and only the resulting net income from a business or property is allocated to beneficiaries. See for example the "Allocation of income and expenses" schedule for the T-3 tax return at the end of Chapter 5.

f. No. The gain on a principal residence realised by a trust, if flowed through to a beneficiary, cannot be designated as eligible for the principal residence exemption. However, the tax attributes of a principal residence, including eligibility for the principal residence exemption can be flowed through to a beneficiary if the residence that qualifies is transferred to a beneficiary on a tax-deferred basis. For the purposes of the exemption, the beneficiary will be deemed to have owned the property during the trust's period of ownership, and if the property would have qualified as a principal residence during those years if the beneficiary had owned it, it will qualify for the exemption for those years when the beneficiary disposes of the residence. The transfer of the residence to a beneficiary may be the preferred way to utilise the principal residence exemption on a property owned by the trust if there is more than one beneficiary who falls within the definition of a qualified beneficiary for this purpose. Although the trust may claim the principal residence exemption if it sells the property directly, the use of the exemption will extinguish the right of all specified beneficiaries to from using the principal residence exemption for the years it is claimed by the trust.

g. No. Charitable donations do not flow through a trust to a beneficiary. However, charitable gifts made by an estate pursuant to the terms of the Will are deemed to be made by the deceased in the year of death and are available in the final tax return of the deceased.

3. Trusts with Mary and George

    a. Trusts and tax rates:

        i. In Mary's Will two testamentary trusts are created, the spousal trust and the family trust. They are both entitled to the marginal rates of tax, but because George is a beneficiary of both trusts, they are potentially only entitled to one set of marginal rates of tax between them if the Minister exercises discretion to tax them as one trust.

        ii. The trust George created during his lifetime is an *inter vivos* trust and is subject to tax at the highest marginal rate applicable to individuals.

iii. The trust in George's Will is a testamentary trust. However, it may be tainted as a testamentary trust for tax purposes because another person is required to contribute to the expenses of the estate, in which case instead of paying taxes at the marginal rates, it will be deemed to be an *inter vivos* trust for tax purposes and required to pay tax at the highest marginal rate.

b. Deemed dispositions:

i. The spousal trust in Mary's Will will have a deemed disposition in 2010 when George died, and a second deemed disposition (if there is another ongoing trust created after the death of George) in 2031. The family trust in Mary's Will had a deemed disposition in 2003, and will have another if applicable, in 2024.

ii. The George family trust had a deemed disposition in 1999, and will have another in 2020.

iii. The trust in George's Will will have a deemed disposition in 2031 and another in 2052.

c. Advice for Mary or George: Mary could consider excluding George from the family trust in her Will if she wanted the two trusts to each have separate access to the marginal rates. To further gain access to the marginal tax rates, Mary could have created separate trusts for each of her three children. George could have created the trust for his grandson without imposing an obligation on his son to pay estate taxes or expenses thereby making it clear that the trust qualified as a testamentary trust for tax purposes under the Act and was entitled to the marginal tax rates permitting income splitting with the beneficiary.

4. Rollovers on transfers to trusts:

a. A qualifying spousal or common-law partner trust

b. An alter ego trust

c. A joint spousal or common-law partner trust

d. A self benefit trust

e. Deferral will end upon the earlier of

   i. Actual disposition of the property

   ii. Death of the lifetime beneficiary – spouse or common law partner for a and c, and death of settlor for b or d.

5. Comparing a qualifying spousal or common-law partner trust with a joint spousal or common-law partner trust.

   a. Beneficiary – for a QST the only beneficiary must be the spouse (including common-law) during his or her lifetime whereas with a JPT the settlor may also be a beneficiary during his or her lifetime

   b. Rights to Income – all income must be payable to the spouse or common-law partner for a QST whereas for a JPT all income must be payable to the settlor and the spouse or common-law partner.

   c. Settlor – the rollover for a JPT requires that the settlor be age 65 or older whereas there is no such age requirement for a QST. (Bonus – it is also possible for a JPT to be settled by both spouses or common-law partners as long as both are age 65 or older).

   d. Tax consequences of transferring capital property to the trust – same for both - a rollover applies automatically unless the settlor elects not to have the rollover apply – the election is made, or not made, on a property by property basis.

   e. Timing of deemed dispositions - on the death of the beneficiary who is the spouse or common-law partner in the case of a QST there is a deemed disposition of all capital property, whereas with a JPT the deemed disposition is deferred until the later of the death of the settlor and the spouse or common-law partner.

   f. Testamentary or *inter vivos* – a QST may be testamentary or *inter vivos* whereas a JPT is only *inter vivos*.

6. Exceptions to general rule for taxation of income paid or payable to beneficiary

a. Income not paid to a beneficiary may be taxed in the hands of the beneficiary where:

    i. The trustees have made a preferred beneficiary election

    ii. Income accumulating in an Age 40 trust for the benefit of a beneficiary under age 21 may be deferred until the beneficiary is up to age 40

b. Income paid or payable to a beneficiary may not be taxable to the beneficiary where:

    i. The trust makes an election (under 104(13.1) or (13.2)), the income will be taxed in the trust

    ii. The income is taxed in the hands of another person, (usually a related person who has transferred property to the trust), under the attribution rules

    iii. Where income is paid during the executor's year and one or more beneficiaries object to being taxed on the income, it will be taxed in the trust

7. The general rule is that upon distribution of trust property to a beneficiary in satisfaction of a capital interest in the trust, there is a rollover and a deemed disposition for proceeds equal to the ACB of the trust. There are exceptions when this rule does not apply and the deemed disposition takes place at fair market value. The main exceptions are where there is a distribution to a non-resident, the trust was subject to the attribution rule in 75(2) or the trustees make an election out of the rollover. Note: Although there are other circumstances where the distribution of trust property is not given rollover treatment, these are not distributions in satisfaction of a capital interest – these include distributions in satisfaction of an income interest and distributions to a person who not a beneficiary of a QST, AET or JPT during the lifetime of the life tenant (being the settlor or settlor's spouse) which are contrary to the requirements for such trusts in the Act.

8. Trusts for minor children – The tax advantages are primarily the ability to income split capital gains (assuming 75(2) doesn't apply)– i.e. capital gains can be allocated to minor children permitting income splitting and multiplying access to the capital gains exemption. The main tax disadvantage is that property may not be transferred to such trusts on a rollover basis. From a non-tax perspective such trusts permit parents and grandparents to irrevocably set aside funds for the benefit of family members without permitting control or direct access to the beneficiaries until a future time specified by the

settlor in the trust document. One disadvantage is that if the settlor changes his or her mind, the funds cannot be returned – in a sense this is both an advantage and a disadvantage.

9. An undocumented trust, sometimes called an informal trust, is a trust that has no written trust agreement.

    a. The first danger is that the arrangement may not be recognised as a trust. Without documentation, it will be more difficult to establish the legal elements required to establish a trust. In particular there may be difficulty establishing certainty with respect to intention – i.e. certainty of the settlor's intention to create a trust. If the trust is being set up for tax purposes, CRA may challenge the validity of the trust and the tax benefits that were intended to be applicable to the trust may unravel such as they did in the *Antle* decision. CRA may consider that the arrangement is one of agency rather than being a trust. If there is no trust, all income and capital gains will be taxed in the hands of the transferor of property to the trust.

    b. The second danger is that such trusts are typically implemented without legal and tax advice and the settlor and others may not understand the legal or tax consequences of creating a trust. Persons setting up and administering informal trusts are often unaware of the following consequences of the creation of a trust. For example:

        i. The settlor may not take back the property transferred to the trust, and the trustee and the settlor engaging in such an activity are participating in a breach of trust.

        ii. The trustees of a trust have all the legal obligations of trustees whether there is a written trust document or not, including the requirement to:

            1. Prepare and file annual income tax and information returns and pay any income tax owing from the trust property.

            2. Obtain a tax clearance certificate before distributions are made, without which the trustee may be personally liable for any unpaid taxes of the trust.

            3. Comply with provincial law respecting investment of trusts

iii. If the settlor is managing the trust property, all income and capital gains will be attributed to the settlor during his or her lifetime, and any transfer of property, even to a beneficiary, will be a taxable disposition.

iv. The application of the 21 year rule

c. Thirdly, informal trusts have no written terms. This can lead to uncertainty with respect to rights to income or capital, time of distribution, and succession of trustees. Such uncertainty may lead to litigation if there is a dispute with beneficiaries or among the trustees, and make it difficult for the trustee to know whether he or she is fulfilling their obligations under the trust arrangement.

d. Lastly, it may be possible for a beneficiary to require the trust property to be distributed to him or her if his or her interest is vested – for example if the beneficiary is competent (not a minor) and there are no other beneficiaries. This is the effect of the rule in *Saunders v. Vautier*. Premature distribution could be prevented in a written trust by specifically providing for a contingent interest.

10. While distributions on the winding up of a trust to the capital beneficiaries normally take place on a rollover basis, this is not the case for distributions of property to non-residents. The compliance requirements for distributions of property in kind to a non-resident include withholding, Part XII.2 tax, and the requirement for a 116 certificate of compliance. This situation is one in which it would be appropriate for the trustee to consult a tax advisor. Selling all or part of the portfolio and distributing cash may seem less complicated from a tax perspective except that this will trigger tax consequences to the trust that must be considered in the light of the fact that there is also a resident beneficiary who can receive the property in kind without triggering a deemed disposition. In addition, the material in Chapter 4 refers to material in other chapters which give additional details that are relevant to this situation. For example, even a distribution of cash to a non-resident triggers potential tax consequences and compliance requirements – as discussed in Chapter 6.