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Non-Resident Trusts and Offshore Investment Fund Properties

I. Introduction

Since the early 1980’s the taxation of non-resident trusts (referred to colloquially as “offshore trusts”) has received significant scrutiny from both the Department of Finance (“Finance”) and the Canada Revenue Agency (the “CRA”). This scrutiny has resulted in considerable legislative changes to the provisions in sections 94 and 94.1 of the Income Tax Act\(^2\) (the “Act”), which address the taxation of non-resident trusts and non-resident investment funds. Currently, non-resident trusts are taxed on their Canadian-source income and foreign accrual property income (“FAPI”) under section 94 of the Act. Section 94.1 is intended to prevent taxpayers from avoiding or deferring Canadian tax by investing in offshore investment funds that are resident in low-tax jurisdictions.

Sections 94 and 94.1 are designed to prevent the avoidance or elimination of Canadian federal income tax through the accumulation of investment income in non-resident trusts and offshore investment funds. Both sections have been the subject of extensive proposed amendments that were first announced in the 1999 Federal Budget. Since that announcement, the proposed amendments have been before Parliament on multiple occasions but have not been passed into law.

Prior to the 2010 Federal Budget, the proposed amendments were most recently set out in Bill C-10, which died on September 7, 2008 when the October 14, 2008 federal election was called.\(^3\) These proposed amendments (which are currently outstanding) apply to a wider range of non-resident trusts than existing section 94 and require those trusts to pay tax on their worldwide income (and not just their Canadian-source income and FAPI). In the case of offshore investment funds, it was proposed that existing section 94.1 be replaced by proposed sections 94.1, 94.2, 94.3 and 94.4, which

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1 I would like to acknowledge the assistance provided by Brent Pidborochynski of Thorsteinssons LLP in updating this year’s version of the paper.

2 RSC 1985, c.1 (5th supp.), as amended. Unless otherwise stated herein, all statutory references are to the Income Tax Act and the regulations thereunder (the “Regulations”).

3 Prior to this, the amendments were set out in Bill C-33 which died when Parliament was prorogued on September 4, 2007.
-contained extensive rules governing the tax treatment of foreign investment entities (the “FIE Rules”).

The outstanding rules in Bill C-10 were subsequently criticized by the Advisory Panel on Canada’s System of International Taxation (the “Panel”) in its report to Finance. The Panel concluded that those proposed amendments should be reconsidered in order to reduce overlap and complexity.

The revised proposals in the 2010 Federal Budget are the government’s response to the Panel’s recommendations. With respect to the non-resident trust rules in section 94, the revised rules are based on, and substantially modify, the outstanding rules. Regarding section 94.1, the government announced that it will abandon its proposal to implement the FIE Rules and, instead, the rules in existing section 94.1 will remain in force, subject to relatively minor amendments.

The multiple proposed amendments to section 94 and 94.1 can give rise to some confusion of terminology. For the purposes of this paper, a reference to the “Existing Rules” means the rules in sections 94 and 94.1 that are currently in force, a reference to the “Outstanding Rules” means the amendments that were set out in former Bill C-10, and a reference to the “Revised Rules” means the amendments that were set out in the 2010 Federal Budget.

The Revised Rules have not been drafted and are not currently before Parliament. In the 2010 Federal Budget, the government announced that the Revised Rules will be subject to consultation before being tabled in Parliament. In particular, a panel of tax practitioners will be formed to work with Finance in order to make recommendations regarding the design of the Revised Rules, following which draft legislation will be released for public commentary. The Revised Rules, once enacted, will generally apply to 2007 and subsequent taxation years. However, certain proposals that were not in the Outstanding Rules will only apply to taxation years that end after March 4, 2010.

This paper will describe the Existing Rules, the Outstanding Rules and the Revised Rules regarding non-resident trusts and offshore investment funds. For the time being, these proposed amendments remain the best indication of how offshore investment funds and non-resident trusts will be taxed in the future. Obviously, taxpayers and their advisors will need to review the status of any amendments to sections 94 and 94.1 prior to implementing a transaction that could be affected by those rules.
II. Existing Non-Resident Trust Rules

1. Common Law Test For Residency Of A Trust

A Canadian-resident *inter vivos* or testamentary trust is generally subject to tax on its undistributed taxable income. In contrast, a non-resident *inter vivos* or testamentary trust is generally only subject to Canadian tax on its income earned in Canada (absent the application of section 94). Therefore, the starting point in determining which regime applies is a determination of whether the trust is resident in Canada for the purposes of the Act.

Subject to specific deeming rules in the Act, the legal residence of a trust for Canadian tax purposes is determined by reference to common law principles. Canadian tax practitioners have traditionally been of the view that the residence of a trust is primarily determined by reference to the place where the trustee resides. This principal was stated in *Thibodeau Family Trust v. The Queen*.\(^4\) In that case, the Federal Court-Trial Division was required to determine whether the Thibodeau Family Trust was a resident of Canada or Bermuda for the purposes of the Act. The trust was a discretionary trust that required a majority decision of the trustees on all matters of trustee discretion (two of three trustees were residents of Bermuda). The Court held that because a majority of the trustees were resident in Bermuda, and because the trust document required majority decisions on all matters of trustee discretion, the trust was a resident of Bermuda.

However, in the recent Tax Court of Canada decision of *Garron et al. v. The Queen*,\(^5\) the Court held that the residence of a trust should be determined according to the “central management and control test” used to determine corporate residence.

The *Garron* case involved an estate freeze that included two Barbados trusts. The freeze was carried out in respect of shares of a Canadian resident corporation in the automotive industry, PMPL. Prior to the freeze, the shares of PMPL were held 50% by Dunin and 50% by Garron.\(^6\) As part of the

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5. 2009 DTC 1287 (T.C.C.).
6. Garron’s interest in PMPL was held indirectly through a corporation, GHL, the shares of which were held by Garron, his spouse and the Garron Family Trust.
freeze, trusts were established for the benefit of Garron and his family and Dunin and his family, respectively. The sole trustee of both trusts was St. Michael Trust Corp., a licensed and regulated trust company resident in Barbados. Garron and Dunin froze their respective interests in PMPL by exchanging their common shares for preferred shares of PMPL. New common shares of PMPL were then issued for nominal cash consideration to two Canadian holding corporations that had been incorporated by the Barbados trusts. At the time of the freeze, the common shares of PMPL were valued at approximately $50,000,000.

Two years after the freeze, the Barbados trusts sold the majority of their shares of their respective holding corporations for approximately $532,000,000. The trusts made remittances required under section 116 of the Act in respect of the dispositions, then sought a return of those funds on the basis that the trusts were exempt from Canadian tax pursuant to the Canada-Barbados Income Tax Treaty. The Minister disagreed and assessed the trusts accordingly.

In determining whether the trusts were resident in Canada, the Tax Court of Canada held that the residence of a trust is not determined by reference to the residence of its trustee. Instead, the Court applied the “central management and control test”. In applying this test, the Court found that, from the outset of the transaction, the trustee had agreed to defer to the recommendations of Dunin and Garron. Therefore, the central management and control of both trusts was directed by Dunin and Garron in Canada. It followed that the trusts were resident in Canada and, therefore, that the gains realized on the dispositions of shares were taxable in Canada.

The Garron case is currently under appeal to the Federal Court of Appeal. It remains to be seen whether that Court will agree that the central management and control test is the correct test for determining the residence of a trust under the Act.

2. **Conditions for the Application of the Existing Non-Resident Trust Rules**

Section 94 is an important element of the FAPI regime set out in the Act and operates to tax certain non-resident trusts on their passive income. In this manner, section 94 imposes Canadian tax on

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7 In particular, Article XIV(4) of the Canada-Barbados Income Tax Treaty provides that gains from the alienation of property may only be taxed in the contracting state of which the alienator is resident.
investment income earned outside Canada by certain non-resident trusts. Very generally, the non-resident trust rules in existing section 94 will apply to non-resident trusts where there is both a Canadian-resident beneficiary and a Canadian-resident contributor.

One of the preconditions to the application of existing section 94, which is outlined in paragraph 94(1)(a), is that a trust must have a Canadian resident who is “beneficially interested” in the trust. This precondition will be met where a person resident in Canada is “beneficially interested” in a trust either directly or indirectly through a corporation, trust or controlled foreign affiliate (“CFA”) of the person at any time in the taxation year of the trust. The definition of “beneficially interested” has been amended several times in recent years to try to expand its scope. However, Finance still believes that there is room for abuse and they have eliminated this requirement in the proposed legislation, which is discussed below in detail.

Paragraph 94(1)(b) imposes a second precondition to the application of the existing non-resident trust rules which requires that the trust (or a non-resident corporation that would be a CFA of the trust if the trust was resident in Canada) has acquired property, directly or indirectly, from a person who:

(i) was (or was related to) the Canadian-resident beneficiary referred to in paragraph 94(1)(a), or was an uncle, aunt, nephew or niece of that Canadian-resident beneficiary;

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8 “Beneficially interested” is defined in subsection 248(25) to include a person entitled to any right to income or capital of a trust whether immediate or future, whether absolute or contingent or whether conditional on the exercise of any discretion. Further, pursuant to paragraph 248(25)(b), a person is deemed to be beneficially interested in a trust if the trust acquired property from that person (or any non-arm’s length party or foreign affiliate) and the trust includes a power to appoint new beneficiaries.

9 The following trusts are expressly excluded from this element of the test for a Canadian resident contributor: (i) an inter vivos trust created before 1960 by a person who was a non-resident at that time; (ii) a testamentary trust that arose as a consequence of the death of an individual whose death occurred before 1976; and (iii) a trust governed by a foreign retirement arrangement.

10 Subsection 94(6) deems the trust to have acquired property from any person who has given a guarantee on the trust’s behalf, or from whom it has received any other financial assistance whatever.

11 Pursuant to clause 94(1)(b)(i)(B) the test for a Canadian resident contributor will be met whether the trust acquires property from a person or entity meeting the criteria established in clause 94(1)(b)(i)(A) or from a non-arm’s length trust or corporation that acquired the property from such person or entity.
(ii) was resident in Canada at any time in the previous 18 months (or at any time during the 18 month period preceding the contributor’s death); and

(iii) has been resident in Canada for a period or periods totalling 60 months.\(^{12}\)

Additionally, the requirement in paragraph 94(1)(b) will also be met if the interest in the trust was purchased by a Canadian-resident beneficiary or acquired by way of a gift, inheritance or the exercise of a power of appointment from a person that would have met the Canadian-resident contributor test outlined above. Thus, generally, the test for a Canadian-resident contributor in paragraph 94(1)(b) will be met when a trust acquires property, directly or indirectly, from a Canadian resident or when a Canadian resident purchases an interest in a trust.

Under the existing section 94, a non-resident can establish a non-resident trust for the benefit of a Canadian resident without attracting liability under section 94 (assuming the trust does not otherwise acquire property from a Canadian resident). A Canadian resident can also establish a trust for the benefit of non-residents without section 94 applying. As a result, section 94 currently only applies when a Canadian resident transfers property (either directly or indirectly) to a non-resident trust for the direct or indirect benefit of a Canadian beneficiary.

3. **Application of the Existing Non-Resident Trust Rules**

As discussed above, under the Existing Rules, a non-resident trust will be subject to tax in Canada under section 94 if the trust has a Canadian-resident beneficiary who is related to (or is the uncle, aunt, nephew or niece) of a Canadian resident who has contributed property to the trust. However, the tax payable by the trust will differ depending on whether the trust is a discretionary or non-discretionary trust.

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\(^{12}\) The requirement that the person from whom the trust has acquired property be resident in Canada for 60 months allows immigrating non-residents to avoid Canadian tax on investment income generated from property contributed to a non-resident trust for up to five years. These structures are commonly referred to as “immigration trusts.”
(a) Discretionary Trusts

A discretionary non-resident trust that has a Canadian-resident beneficiary and a Canadian-resident contributor will be subject to the rules outlined in paragraph 94(1)(c). Paragraph 94(1)(c) deems such a trust to be a resident of Canada for the purposes of Part I of the Act and provides that the trust is subject to tax on its Canadian-source income and on its FAPI. The trust’s Canadian-source income is the income on which it would otherwise be subject to Canadian tax as a non-resident calculated in accordance with section 115 of the Act. In addition, a discretionary trust subject to tax under section 94 is required to include all of its FAPI in its income. There is no mechanism to reduce the trust’s tax based on the relative interests of resident and non-resident beneficiaries. However, pursuant to subsections 104(6) and 94(3), to the extent that a portion of the trust’s income or FAPI has been distributed in the year or has become payable to a beneficiary in the year, the trust is entitled to deduct such amount from its income.

The definition of FAPI found in section 95(1) is expanded by paragraph 94(1)(c) for the purposes of calculating the FAPI of a non-resident discretionary trust. Paragraph 94(1)(c) operates to include in FAPI all dividends received by a non-resident trust (including dividends received from a foreign affiliate) and all gains realized by a non-resident trust (including gains on the sale of shares of foreign affiliates engaged in active business). The expansion of the definition of FAPI was introduced to counter a planning opportunity that was previously available to non-resident trusts. Specifically, because a trust has the ability to convert income to capital, if a non-resident trust was not taxed on dividends and gains in the year of receipt, the trust was able to distribute such income or gains by way of a tax-free capital distribution to Canadian beneficiaries in a subsequent year.

Because paragraph 94(1)(c) deems certain non-resident trusts to be persons resident in Canada for the purpose of Part I, non-resident trusts are subject to provisions of the Act that would otherwise only apply to Canadian-resident trusts. Like a Canadian-resident trust, an inter vivos non-resident trust is taxed at the highest marginal rate, whereas a non-resident testamentary trust is taxed at the marginal rates applicable to individuals. Non-resident trusts that are deemed to be resident in

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13 This article is not intended to outline the elements of FAPI. These issues are addressed elsewhere at this conference.
Canada for the purposes of Part I are also subject to the 21-year deemed disposition rule in subsection 104(4).

Subparagraph 94(1)(c)(ii) clarifies that for the purposes of the foreign tax credit available under section 126, a non-resident discretionary trust’s FAPI is deemed to be income from a source in the country other than Canada that the trust would be resident in but for subparagraph 94(1)(c)(i). Any income or profits tax paid by the trust (other than pursuant to section 94) that may reasonably be regarded as having been paid in respect of this income is deemed to be non-business income tax paid by the trust to the government of that country. As a result, such trusts are able to utilize the foreign tax credit available under section 126.

It should be noted that paragraph 94(1)(c) only operates to deem non-resident trusts to be Canadian residents for the purposes of Part I. Therefore, payments to a non-resident discretionary trust are subject to the withholding tax required by Part XIII of the Act. However, provided the income precipitating the withholding under Part XIII is included in the trust’s taxable income, the trust will be entitled to a tax credit in respect of its Part XIII tax.

Under subsection 94(2), Canadian-resident beneficiaries and contributors to a non-resident trust are jointly and severally liable for the unpaid taxes, penalties and interest of the trust. This liability is limited to the total of amounts paid to them by the trust, amounts in respect of which they are entitled to enforce payment and any proceeds of disposition received in respect of an interest in the trust.

A non-resident discretionary trust is also deemed to be a Canadian resident for purposes of sections 233.3 and 233.4. Sections 233.3 and 233.4 impose the reporting obligations in respect of “specified foreign property”. Where a trust is deemed to be a Canadian resident by virtue of section 94 and it owns “specified foreign property” with a cost in excess of $100,000 or holds an interest in a foreign affiliate, the trust will be required to comply with the reporting requirements under sections 233.3 and 233.4 of the Act.
(b) Non-Discretionary Trusts

If existing section 94 applies to a non-discretionary non-resident trust, paragraph 94(1)(d) operates to deem the trust to be a corporation for any beneficiary whose beneficial interest in the trust is not less than 10% of the aggregate fair market value of all beneficial interests in the trust. As a result, any beneficiary holding a beneficial interest that has a fair market value of 10% or more of all of the beneficial interests in the trust will be subject to the FAPI rules as though the trust were a corporation. A beneficiary holding an interest in a non-resident non-discretionary trust that is less than the 10% threshold will not be subject to tax under existing section 94, although existing section 94.1 could apply to such an interest.

III. Proposed Non-Resident Trust Rules

1. Common Law Test For Residency Of A Trust

To address perceived abuses of the non-resident trust rules in existing section 94, Finance has proposed certain amendments to that section. As noted at the beginning of this paper, the draft legislation released as part of the Outstanding Rules in Bill C-10 was never enacted. Further, the government recently announced that it intends to replace the Outstanding Rules with the Revised Rules. Draft legislation for the Revised Rules has not yet been released. However, it is proposed that the draft legislation will be substantially similar to the current draft legislation in the Outstanding Rules, with certain modifications intended to simplify the rules and better target arrangements that are seen as attempting to avoid paying the appropriate amount of Canadian tax.

The Outstanding Rules (and, in turn, the Revised Rules) would significantly broaden the scope of existing section 94. As discussed above, the Existing Rules applied to non-resident trusts where there was both a Canadian-resident beneficiary and a Canadian-resident contributor to the trust. The proposed rules would no longer include a requirement that there be both a Canadian-resident beneficiary and a Canadian-resident contributor to the trust. Instead, the proposed rules focus on taxing non-resident trusts that have received contributions from Canadian residents regardless of whether any Canadian resident is beneficially interested in the trust.
The discussion below will address the: (i) conditions for the application; (ii) the application; and (iii) the liability for tax under the Outstanding Rules. It will also discuss how the scope of these rules will be modified under the Revised Rules.

2. **Conditions for the Application of the Outstanding Non-Resident Trust Rules**

Proposed subsection 94(3) deems certain non-resident trusts to be resident in Canada for the purpose of computing liability for tax under the Act. Proposed subsection 94(3) applies where a non-resident trust (other than an “exempt foreign trust”)\(^{14}\) has either a “resident contributor” or a “resident beneficiary”.

A “resident contributor” is defined in proposed subsection 94(1) to be a “contributor” who is resident in Canada at that time and has been a resident of Canada for periods that total at least five years.\(^{15}\) A “contributor” is an entity\(^{16}\) that has made a “contribution” to the non-resident trust. The meaning of “contribution” is discussed in greater detail below, but very generally includes any transfer or loan (other than an “arm’s length transfer”), directly or indirectly, of property to a trust. Thus, in contrast to the old rules, proposed section 94 will apply where a Canadian-resident person contributes property to a trust exclusively for the benefit of non-resident persons. From a tax policy perspective, it is not clear why the rules have been expanded to apply in this circumstance, since the establishment of a non-resident trust benefiting only non-residents is analogous to giving the property to a non-resident, a situation that would not otherwise attract Canadian tax after the initial gift.

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14 The definition of “exempt foreign trust” in proposed subsection 94(1) includes certain non-resident trusts: (i) benefiting non-resident physically or mentally infirm dependants; (ii) created to benefit non-resident children upon marriage breakdown; (iii) certain trusts established for the benefit of employees; and (iv) certain foreign unit trusts and charitable trusts.

15 The definition of “resident contributor” does not include an individual that has made a “contribution” to a trust established before 1960 by a person that was a non-resident at that time, provided that the individual has not made any “contributions” to the trust after 1959. In addition, the immigration trust exception is preserved because a resident contributor is defined to include a contributor who has been resident in Canada for at least 60 months.

16 An “entity” includes an association, a corporation, a fund, a natural person, a joint venture, an organization, a partnership, a syndicate and a trust.
A “resident beneficiary” is defined as an entity (other than a “specified charity”\(^{17}\) or a “successor beneficiary”\(^{18}\)) that is a Canadian-resident beneficiary of the trust, where at that time there is a “connected contributor” to the trust. A “connected contributor” is defined as an entity that has made a contribution to the trust other than an entity that has only made contributions to the trust at a “non-resident time”.\(^{19}\) In addition, if the entity is an individual (other than a trust) the “connected contributor” must have been resident in Canada for periods totalling five years. Thus, the term “resident beneficiary” is somewhat misleading, as the definition generally requires not only a beneficiary that is resident in Canada, but also a contributor that was a resident of Canada within five years of the time of contribution (either before or after). Therefore, if a non-resident person settles a non-resident trust for the benefit of a Canadian at a non-resident time, proposed section 94 will not apply, provided no additional contributions are made to the trust by residents of Canada.\(^{20}\)

(a) Meaning of “Contribution”

As noted above, proposed section 94 generally requires that a “contribution” be made by an entity that is either currently a resident of Canada or was a resident of Canada within five years of the time of the “contribution”. Thus, the determination of whether an entity has made a “contribution” is a key element in the application of proposed section 94.

In the proposed amendments to subsection 94(1), a particular entity will be considered to have made a “contribution” to a trust where that entity has: (i) made a transfer or loan to the trust; (ii) made a

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\(^{17}\) A “specified charity” includes a registered charity and certain other charities listed in the definition of “total charitable gifts” in subsection 118.1(1). However, a specified charity does not include a charity that at that time or a “specified prior time” was not dealing at arm’s length with certain parties, including the trust, a contributor, or an entity beneficially interested in the trust.

\(^{18}\) The definition of “successor beneficiary” includes a beneficiary whose interest is solely contingent on the subsequent death of an individual that is a contributor, or is related to a contributor.

\(^{19}\) Pursuant to the definition of “non-resident time” in proposed subsection 94(1), a transfer made by an entity within five years of becoming, or ceasing to be, a resident of Canada will not be considered to have been made at a “non-resident time”. Further, the rules will apply with retroactive effect where an entity becomes a Canadian resident within five years of making a contribution and where the entity has been resident for at least 60 months at that time. Therefore, the immigration trust exception is preserved (i.e., there will not be a connected contributor to the trust until the immigrant has been a Canadian resident for 60 months). A special 18-month time period applies to a trust created by, or contributions arising on, the death of an individual. Therefore, a non-resident who dies more than 18 months but less than 60 months after leaving Canada and upon whose death a trust is created, will not be considered to be a “connected contributor” to the trust.

\(^{20}\) This has often been colloquially referred to as a “granny trust” (i.e., a non-resident grandparent settles a trust for the benefit of Canadian resident grandchildren). Under the proposed amendments, a trust created in this manner will still not fall within section 94.
transfer or loan as part of a series of transactions or events that includes a transfer or loan by another entity to the trust where the transfer to the trust by that other entity can reasonably be considered to be in respect of the transfer by the particular entity; or (iii) become obligated to make a transfer or loan as part of a series of transactions or events that includes a transfer or loan by another entity to the trust where the transfer to the trust by that other entity can reasonably be considered to be in respect of the particular entity’s obligation. However, the definition of “contribution” specifically excludes an “arm’s length transfer”. Thus, the definition of “contribution” includes direct and indirect transfers or loans to a trust, other than “arm’s length transfers”.

Proposed subsection 94(2) contains a number of rules which significantly expand the scope of the definition of contribution. For example, where a trust has made a contribution to another trust, paragraph 94(2)(n) deems each contributor to the original trust to have made a contribution to the other trust. Paragraph 94(2)(o) deems a partnership and the members of that partnership (other than limited partners) to have made a contribution to any trust to which the partnership has made a contribution. Paragraph 94(2)(q) deems the acquisition of a “specified fixed interest” in a trust from a third party, or a right to acquire a “specified fixed interest” in a trust, to constitute a contribution directly to the trust.

As noted above, in order to have a “contribution” there must be a “transfer or loan”, directly or indirectly, of property to a trust, other than an “arm’s length transfer”. The meaning of both of these terms is discussed below.

(b) Meaning of “Transfer or Loan”

The terms “transfer” and “loan” are not defined in the proposed legislation. However, proposed subsection 94(2) deems a number of events to constitute a transfer or loan for the purpose of proposed section 94. These deeming rules clarify and significantly broaden the scope of what constitutes a transfer or loan. Proposed subsection 94(2) deems the following to be transfers or loans of property:
(i) a transfer or loan to another entity (other than an “arm’s length transfer”) where the FMV of the trust’s assets increase or the trust’s liabilities decrease as a result of the transfer (paragraph 94(2)(a));

(ii) a transfer or loan of property to another entity (other than an “arm’s length transfer”) if the trust holds property, the value of which is derived from the value of property held by the entity (paragraph 94(2)(c));

(iii) the provision of a guarantee or financial assistance to another entity (paragraph 94(2)(e));

(iv) the provision of certain services after June 22, 2000 (other than “exempt services”) (paragraph 94(2)(f));

(v) the acquisition of shares of a corporation, interests in a trust, partnership or other entity or debt owing by another entity from that corporation, trust, partnership or other entity (paragraph 94(2)(g)(i) to (v));

(vi) the acquisition of rights to acquire or be loaned property after June 22, 2000 (paragraph 94(2)(g)(vi)); and

(vii) an obligation to do an act that would if done otherwise constitute a transfer or loan (paragraph 94(2)(i)).

Proposed paragraph 94(2)(k) applies to bring certain third party transfers within the meaning of transfer or loan. Where an entity has made a transfer or loan to a trust, the transfer or loan is made at the direction (or with the acquiescence) of another entity and it is reasonable to consider that one of the reasons the transfer or loan is made is to minimize the liability of any entity that would have arisen as a result of the application of subsection 94(3), then the contribution is deemed to have been made jointly by the entity and that other entity.
The effect of proposed subsection 94(2) is to broaden the scope of the meaning of transfer or loan, such that the term would appear to include almost any transaction whereby value is created for the benefit of a trust, with the exception of an “arm’s length transfer” (discussed below).

(c) Meaning of “Arm’s Length Transfer”

A transfer or loan to a trust will not be considered to be a “contribution” if it is an “arm’s length transfer” as defined in proposed subsection 94(1).

The definition of “arm’s length transfer” generally includes an arm’s length return on investment and a return of paid up capital. However, a transfer will not be an arm’s length transfer unless it is reasonable to conclude that none of the reasons for the transfer is the acquisition at any time by any entity of an interest as a beneficiary under the trust. In addition, a transfer will generally not be an arm’s length transfer if the payment is a transfer described in proposed paragraph 94(2)(g)\(^{21}\) or the payment is greater than the amount the transferor would have been willing to make if an arm’s length relationship existed between the transferor and transferee.

The definition of “arm’s length transfer” is very narrowly drafted. The requirement that none of the reasons for the transfer is the acquisition at any time by any entity of an interest as a beneficiary in the trust would appear to catch many transactions which are otherwise based on arm’s length terms. For example, where a Canadian resident (the “Lender”) loans money to a non-resident trust benefiting his children, even if arm’s length terms are included in the loan, it may be difficult to conclude that none of the reasons for the loan is the acquisition of an interest in the trust by his children at the time the trust was established. Presumably, one of the reasons the loan is being made is because the non-resident trust benefits the Lender’s children. Thus, an “arm’s length transfer” requires not only arm’s length terms, but also a situation analogous to an arm’s length relationship.

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\(^{21}\) The transfers described in paragraph 94(2)(g) include the acquisition of a share of a corporation from that corporation, an interest in a trust, partnership or other entity from that trust, partnership, or other entity, or the acquisition of debt of an entity from that entity.
3. **Application of the Outstanding Non-Resident Trust Rules**

Under proposed subsection 94(3), a non-resident trust subject to proposed section 94 is deemed to be resident in Canada for the purpose of calculating its liability for tax under the Act. As a result, such a trust will be liable to tax on its worldwide income.

In accordance with proposed section 94, a trust is deemed to be a resident of Canada for the purpose of calculating the trust’s foreign tax credits, the “specified foreign property” reporting rules, the 21-year deemed disposition rule, the deduction in computing income found in subsection 104(6)\(^\text{22}\), and for the purpose of determining its liability for tax under Part XIII of the Act in respect of amounts paid to the trust and by the trust.

With respect to the trust’s Part XIII liability, however, because the deeming rule only applies for the purposes of determining the trust’s liability under Part XIII, and not for the purpose of determining the actual amounts to be withheld, Canadian resident payors are still required to withhold and remit pursuant to Part XIII in respect of amounts paid to a non-resident trust which is deemed to be a resident of Canada by virtue of section 94. The trust is entitled to claim a refund of amounts withheld under Part XIII in its annual return.

(a) **Exceptions from the Deemed Residency**

Proposed subsection 94(4) provides that a trust to which section 94 applies will not be deemed to be a resident of Canada for the purpose of certain provisions in the Act.

The deemed Canadian residency status of a non-resident trust will not apply for the purpose of the rollover provisions in subsection 70(6), subsection 73(1) and paragraph 107.4(1)(c) of the Act. Subsection 70(6) provides a tax-free “rollover” with respect to capital property in respect of a transfer to a trust created on a taxpayer’s death for the benefit of a spouse or common law partner. Subsection 73(1) provides a similar rollover where the taxpayer transfers property to the trust

\(^{22}\) However, see also proposed subsection 104(7.01) which restricts the deduction where the trust has non-resident beneficiaries.
benefiting the taxpayer’s spouse or common-law partner. By virtue of the requirement in subsection 70(6) and subsection 73(1) that the relevant trust be a Canadian resident, it is not possible to transfer assets on a rollover basis to a non-resident trust for the benefit of a spouse or common-law partner despite the fact that the trust may be deemed to be a resident of Canada for other purposes.

Section 107.4 is another rollover provision which applies to certain dispositions where the legal ownership of property changes but its beneficial ownership does not. Paragraph 107.4(1)(c) provides that the rollover does not apply where the transferor of the property to the non-resident trust is a person or partnership resident in Canada or with respect to certain transfers of “taxable Canadian property” to a non-resident. Accordingly, it will not be possible for a Canadian resident to transfer property to a non-resident trust, or to transfer “taxable Canadian property” on a rollover basis to a non-resident trust, even if the trust is deemed to be a Canadian resident for most purposes of the Act.

In addition, the deeming rule in proposed subsection 94(3) which deems certain non-resident trusts to be resident in Canada will not apply for the purpose of determining whether a trust is a “mutual fund trust” or an “exempt foreign trust”. The exception for mutual fund trusts ensures that a non-resident trust cannot qualify as a “mutual fund trust”. The exception for “exempt foreign trusts” prevents any circularity in determining what qualifies as an “exempt foreign trust”.

(b) Becoming or Ceasing to be a Resident of Canada

Proposed paragraph 94(3)(c) and subsections 94(5) and (6) address the taxation of a non-resident trust that is deemed by section 94 to become or cease to be a non-resident trust. The rules generally provide that the provisions in section 128.1 regarding immigration to Canada apply at the beginning of the calendar year in which a non-resident trust is first deemed resident in Canada. The emigration rules in subsection 128.1(4) also apply at the beginning of a calendar year where there is neither a “resident beneficiary” nor a “resident contributor”, provided that there was a “resident beneficiary” or a “resident contributor” in the previous year. The application of subsection 128.1(4) will result in a deemed disposition of the trust’s assets immediately before the trust ceases to be deemed resident in Canada under subsection 94(3).

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23 In addition, by virtue of paragraph 94(4)(f), section 94 will not apply to deem a trust to be resident in Canada for the purpose of the exclusion to the definition of “disposition” in subparagraph (f)(i) of that term in subsection 248(1).
4. **Liability for Tax under the Outstanding Non-Resident Trust Rules**

Under proposed paragraph 94(3)(d), a resident contributor or a resident beneficiary of a trust is jointly, severally, and solidarily liable for the tax payable by the trust. However this liability is limited to an entity’s “recovery limit” if the criteria in proposed subsection 94(7) are met. Subsection 94(7) operates to limit an entity’s liability only if:

(i) the entity is solely liable for tax as a “resident beneficiary” of the trust, or a “resident contributor” that did not contribute more than the greater of $10,000 or 10% of the total contributions made to the trust;

(ii) the trust has filed all information returns required by section 233.2 before that time unless less than $10,000 has been contributed to the trust; and

(iii) it is reasonable to conclude that each transaction which occurred at the direction of or with the acquiescence of the entity was not designed to limit the entity’s exposure under proposed paragraph 94(3)(d).

If these criteria are met, the entity’s liability will be limited to the “recovery limit” as defined in proposed subsection 94(8). The “recovery limit” is generally the total of the amounts received or payable by the trust after 2000 to the entity, amounts received after 2000 upon the disposition of the entity’s interest in the trust, the FMV of the benefits enjoyed after 2000 by the entity from the trust, amounts recoverable from the entity under subsection 94(2) as it read before 2007, and the amount of contributions made by the entity. From this amount, previous recoveries by the CRA are subtracted to determine the entity’s recovery limit. If the conditions in proposed subsection 94(7) are not satisfied, there will be no limit (other than the actual liability of the trust for tax, interest and penalties) to the liability imposed by proposed paragraph 94(3)(d).

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24 Proposed subsection 94(8) provides that in the case of certain shares, interests in a trust, partnership or other entity, or a property that derives its value from any of the foregoing, the amount of the contribution for the purpose of determining the liability under proposed subsection 94(7) is the highest FMV of the property during the three-year period that includes and follows the date of the contribution.
5. The Revised Non-Resident Trust Rules – The 2010 Federal Budget

(a) Scope of the Revised Non-Resident Trust Rules

As discussed above, the Revised Rules are based on the Outstanding Rules with respect to non-resident trusts, but with certain modifications intended to simplify the rules and better target arrangements that are seen as attempting to avoid paying the appropriate amount of Canadian tax.

The Outstanding Rules were designed to apply to a much broader range of non-resident trusts than the Existing Rules (including trusts that have no Canadian beneficiaries). However, in the 2010 Federal Budget, the government announced that it intends to make changes to the scope of the proposed non-resident trust rules in order to ensure that they will not apply to legitimate, non-tax motivated transactions. As such, the Revised Rules will modify the Outstanding Rules by: (i) ensuring that tax-exempt entities will not inadvertently be caught by the proposed rules;\(^\text{25}\) (ii) expanding the exceptions for \textit{bona fide} commercial trusts;\(^\text{26}\) and (iii) ensuring that a conventional loan by a Canadian financial institution is not considered to be a contribution to a non-resident trust.\(^\text{27}\)

(b) Application of the Revised Non-Resident Trust Rules

Under the Outstanding Rules, a non-resident trust that is subject to proposed section 94 is liable to tax on its worldwide income. Under the Revised Rules, however, a deemed resident trust will not be subject to Canadian tax on its worldwide income. Instead, the trust’s property will be divided into a

\(^{25}\) Under the Outstanding Rules, there were concerns that a Canadian tax-exempt entity that invested in a non-resident trust would be jointly and severally liable for the non-resident trust’s tax liability, regardless of its exempt status. Therefore, it is proposed under the Revised Rules that an exemption from the resident contributor test and the resident beneficiary test be provided to persons exempt form tax under section 149 (such as pension funds, Crown corporations and registered charities), provided that the tax-exempt entity is not used as a conduit to make an indirect contribution to a non-resident trust.

\(^{26}\) It is proposed that the exception for commercial trusts in paragraph (h) of the definition of “exempt foreign trust” be expanded in order to ensure that \textit{bona fide} commercial trusts not be deemed to be resident in Canada and that investment in \textit{bona fide} commercial trusts not be deterred.

\(^{27}\) Under the Outstanding Rules, a loan made by a Canadian financial institution to a non-resident trust could potentially be viewed as a contribution to that trust. Therefore, under the Revised Rules, it is proposed that a rule be added to ensure that loans made by a Canadian financial institution to a non-resident trust in the ordinary course of the financial institution’s business will not result in the financial institution being a resident contributor to the trust.
“resident portion” and a “non-resident portion”. The “resident portion” will consist of property acquired by the trust by way of contributions from residents and certain former residents, and any property substituted for such property. The “non-resident portion” will consist of any property that is not part of the resident portion. Any income in respect of the non-resident portion (other than income from Canadian sources upon which non-residents are normally required to pay tax) will be excluded from the non-resident trust’s income for Canadian tax purposes.

Further, a non-resident trust that is subject to proposed section 94 will be entitled to a deduction from its income for: (i) amounts attributed to the trust’s resident contributors (as discussed in more detail below); and (ii) the amount of its income that is payable to its beneficiaries in the year. As a result, the trust will generally only be subject to tax in Canada on its income derived from contributions of certain former resident contributors (i.e. income in respect of the resident portion that is not attributed to a resident contributor).

As stated above, a deemed resident trust’s income from the resident portion will be attributed to its resident contributors in proportion to their contributions and taxed in their hands. This attributed amount will be reduced by the amount of any income actually distributed to the resident contributor or other beneficiaries in the relevant year.

It is proposed that the income of the trust that is not distributed to its beneficiaries in a given year will be added to the resident portion of the trust’s property for the next taxation year. However, as an exception to this rule, any accumulated income that arises in respect of property in the non-resident portion will not form part of the resident portion in the next taxation year, provided that it is kept separate and apart from the property in the resident portion.

The Revised Rules will also contain a series of ordering rules regarding distributions to beneficiaries. Distributions to resident beneficiaries will be deemed to be made first out of the resident portion and distributions to non-resident beneficiaries will be deemed to be made first out of the non-resident portion. Any distributions made to non-resident beneficiaries out of the non-resident portion will not

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28 A resident contributor’s share of the income will be based on the proportion of the fair market value of their contributions to the trust (at the time the contributions were made) to the fair market value of all contributions made to the trust by connected contributors.
be subject to withholding tax under by Part XIII of the Act. However, any distributions made to non-resident beneficiaries out of the resident portion will be subject to withholding under Part XIII.

The Revised Rules will also provide that a non-resident trust that is deemed to be a resident of Canada will be entitled to a foreign tax credit in respect of any income taxes paid to another country that treats the trust as a resident of that country for income tax purposes. In addition, the revised Rules will permit the trust to designate a reasonable portion of its foreign tax credits to the resident contributors to whom the income has been attributed.

(c) Liability to Tax under the Revised Non-Resident Trust Rules

Under the Outstanding Rules, both a resident contributor and a resident beneficiary are jointly, severally, and solidarily liable for the taxes payable by a deemed resident trust. However, as discussed above, under the Revised Rules, a trust’s income from the resident portion will be attributed to its resident contributors and taxed in their hands, based on their respective contributions to the trust. As such, resident contributors would be liable to pay tax on this income, but would not be jointly, severally, and solidarily liable for any tax payable by the trust. Resident beneficiaries, however, will remain jointly, severally, and solidarily liable for the tax payable by the trust in the same manner as under the Outstanding Rules.

The Revised Rules dealing with non-resident trusts will apply for 2007 and subsequent taxation years. However, the rules regarding the attribution of a trust’s income to its resident contributors will apply only to taxation years ending after March 4, 2010. Further, there will be an election allowing a trust to be deemed to be resident for 2001 and later taxation years. It is also proposed that the reassessment period in respect of trusts subject to these rules be extended by three years.

(d) Trusts to which the Revised Non-Resident Trust Rules do not apply

Under the Existing Rules, a non-resident trust that is not deemed to be resident in Canada is treated as being a CFA of any Canadian beneficiary whose beneficial interest in the trust is not less than
10% of the aggregate fair market value of all beneficial interests in the trust. This rule will be expanded under the Revised Rules to apply to any resident beneficiaries who, together with persons not dealing at arm’s length, hold 10% or more of any class of interest in a non-resident trust determined by fair market value. It will also apply to any resident who has contributed “restricted property” (as proposed to be defined) to a non-resident trust.

6. **Summary of Proposed Non-Resident Trust Rules**

Compared to the Existing Rules, the Revised Rules will apply to a broader range of non-resident trusts, including trusts that have no Canadian beneficiaries. The tax imposed in accordance with Revised Rules will also be significantly different than that imposed under the Existing Rules. Under the Revised Rules, the trust’s property would be divided into a “resident portion” and a “non-resident portion”. The trust would only be taxed on the income accumulated in the resident portion, with deductions allowed for income payable to beneficiaries and income attributed to resident contributors.

**IV. Offshore Investment Fund Rules**

1. **Introduction**

Existing section 94.1 is provision that is intended to tax taxpayers in respect of interests in investment funds resident outside Canada. The rules generally apply where a taxpayer has an interest in an “offshore investment fund property”, as defined in subsection 94.1(1), and one of the main reasons for holding the investment is to reduce the tax that would otherwise have been payable if the income had been earned directly. Where the rules apply, a taxpayer is deemed to have received notional income from the investment.

The existing rules in section 94.1 have had little impact and have largely been ignored by taxpayers.

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29 See the earlier discussion of existing paragraph 94(1)(d).
and the CRA. In fact, there is only one reported decision involving the application of section 94.1.\footnote{John S. Walton v. The Queen, 98 DTC 1780 (T.C.C.).} Further, in the 1999 Federal Budget, the government indicated that, in its view, the effectiveness of the provision had weakened over the years. The response was the introduction of the proposed FIE Rules, the latest version of which were included in the Outstanding Rules as part of Bill C-10. As discussed above, these rules were subsequently criticized by the Panel, which recommended that the Outstanding Proposals (including the FIE Rules) be reconsidered. In response, as part of the 2010 Federal Budget, the government announced that it intends to abandon the FIE Rules and that existing section 94.1 will remain in force, subject to certain minor amendments.

2. \textit{Application of the Existing Offshore Investment Fund Rules}

Section 94.1 generally applies where the following conditions are satisfied:

(i) A taxpayer holds an interest in a property that is a share of the capital stock of, an interest in, or a debt of, a non-resident entity;

(ii) That interest may reasonably be considered to derive its value, directly or indirectly, primarily from \textit{portfolio investments} of that or any other non-resident entity in, among other things, interests in one or more corporations, trusts, partnerships, organizations, funds or entities; and

(iii) One of the main reasons for the taxpayer holding or having an interest in the non-resident entity is to derive a benefit from portfolio investments in such a manner that the taxes, if any, on the income, profits and gains from such assets are significantly less that the tax that would have been applicable had the income, profits or gains been earned directly by the taxpayer.

If each of these questions is answered in the affirmative, then section 94.1 will apply and the taxpayer will be subject to an income inclusion from the investment equal to the product obtained when the taxpayer’s “designated cost” of the investment at the end of each month is multiplied by
one-twelfth of the appropriate prescribed interest rate. This notional income is reduced by the amount of taxable income (other than capital gains) actually generated by the offshore investment fund property and included in income by the taxpayer.

The “designated cost” of an offshore investment fund property, as defined in subsection 94.1(2), includes the cost to the taxpayer of the property plus amounts made available by a person to another person whether by way of gift, loan, payment for a share, transfer of property at less than its fair market value or otherwise, in circumstances such that it may reasonable be considered that one of the main reasons for making the additional amount available was to increase the value of the property held by the taxpayer that is not otherwise included in the taxpayer’s cost of the property plus the total of all amounts previously included in the taxpayer’s income in respect of the property by virtue of section 94.1. Further, any such amount that is included in income is also added to the taxpayer’s adjusted cost base of the property pursuant to paragraph 53(1)(m).

In the 2010 Federal Budget, the government proposed that the prescribed interest rate applicable to computing the income inclusion for an interest in an offshore investment fund property be increased to the three-month-average Treasury Bill rate plus 2%.

It is proposed that the measures regarding section 94.1 in the 2010 Federal Budget apply for taxation years that end after March 4, 2010. A taxpayer who had voluntary complied with the FIE Rules in previous years (on the basis that the FIE Rules would be enacted based on the Outstanding Rules) will be entitled to have the relevant years reassessed or deduct (in the current year) any excess amounts that were included in income in the relevant years.

(a) Interest in a Non-Resident Entity

In order for section 94.1 to apply, the taxpayer must hold an interest in a property that is a share of the capital stock of, an interest in, or a debt of, a “non-resident entity” (other than a CFA of a taxpayer\(^{32}\) or a prescribed non-resident entity\(^{33}\) or an interest in or a right or option to acquire such a

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\(^{32}\) Interests in CFA’s are dealt with under the FAPI regime, which is addressed elsewhere at this conference.

\(^{33}\) There are currently no prescribed non-resident entities for the purpose of section 94.1.
share, interest or debt.

The term “non-resident entity” is defined broadly in subsection 94.1(2) to mean “a corporation that is not resident in Canada, a partnership, organization, fund or entity that is not resident or is not situated in Canada or a trust with respect to which the rules in paragraph 94(1)(c) or (d) apply”. The application of this definition appears relatively straightforward for corporations and other foreign entities to which the residence concept can be applied. In the context of trusts, section 94.1, as currently drafted, will only apply to a trust that is subject to the non-resident trust rules in existing paragraphs 94(1)(c) and (d). However, given that the 2010 Federal Budget indicated that the existing non-resident trust rules will be replaced with the Revised Rules, this provision is unlikely to appear in the final version of section 94.1.

(b) Value of a Non-Resident Entity from Portfolio Investments

The second precondition to the application of subsection 94.1 is that a non-resident entity must reasonably be considered to derive its value, directly or indirectly, primarily from portfolio investments of that or any other non-resident entity in:

(i) shares of the capital stock of one or more corporations;

(ii) indebtedness or annuities;

(iii) interests in one or more corporations, trusts, partnerships, organizations, funds or entities;

(iv) commodities;

(v) real estate;

(vi) Canadian or foreign resource properties;

(vii) currency of a country other than Canada;

(viii) rights or options to acquire or dispose of any of the foregoing; or

(ix) any combination of the foregoing.

The term “portfolio investments” is not defined in the Act and its meaning has received no judicial
scrutiny in the context of section 94.1. Therefore, the meaning of the term must be determined based on an examination of the text, context and purpose of section 94.1. In this regard, a term used in a statute and not defined should generally be given the meaning it has among those who are familiar with the term in the context in which it is used in the statute. The subject matter of section 94.1 is offshore investment funds. Accordingly, the meaning of “portfolio investments” should be the meaning that would be applied by people conversant with such funds; generally financiers, investment managers, brokers and accountants. A review of relevant dictionary definitions suggests that “portfolio investments” connote a collection of passive investments that are managed as a group, as opposed to direct investment or control.34

A further observation regarding the meaning of “portfolio investments” is that it should be viewed as a sub-category of “investments”. The word “investment” is typically used in the Act to refer to properties which are capable of yielding income in the nature of interest, dividends, or rent, and which, when disposed of, will result in capital gains or losses. The term “investment” is generally not used to describe a property forming part of an inventory or stock-in-trade which, when disposed of, will give rise to income rather than a capital gain. In other words, “investments” is generally used as a synonym for “capital property”.

The CRA was asked to provide its interpretation of the term “portfolio investments” at the 1986 Revenue Canada Round Table, where it stated that the term, as used in section 94.1 and former subsection 206(1), has “a very broad meaning”.35 Further, at the 1990 Revenue Canada Round Table, the CRA stated that it considered “portfolio investments” not to be limited to passive investments and that it may include property that is used in a business.36


This last statement by the CRA may be intended to mean only that the CRA will consider property to be a “portfolio investments” if it is held for the purpose of earning income from a business as described in the definition of “specified investment business” in subsection 129(4.1) or “investment business” in subsection 95(1). Since such property would be held on capital account, this position would be consistent with the interpretation of portfolio investments described above. However, if the CRA’s position is that portfolio investments can include active business assets that are held on income account, then it is inconsistent with the interpretation attributed to section 94.1 at the time it was announced. In particular, in the supplementary information to the Notice of Ways and Means Motion tabled with the 1984 Federal Budget, Finance indicated that “investments in non-resident entities whose principal business is a bona fide active business will not be affected by these rules”. Further, the interpretation would be difficult to reconcile with an earlier CRA technical interpretation, regarding the meaning of “portfolio investments” in former subsection 206(1), where the CRA stated that “loans made by a Canadian corporation in the course of carrying on the business of lending money would not be considered to be portfolio investments. Again, however, it would be a question of fact whether a corporation is in the business of lending money or simply investing in debt instruments”.

(c) Tax Avoidance Motive

Section 94.1 will not apply unless it can be shown that the taxpayer has met the purpose test outlined in subsection 94.1(1). The purpose test requires that one of the main reasons that the taxpayer acquired an interest in the non-resident entity was to significantly reduce the tax which would have been payable had the taxpayer acquired the portfolio investments directly.

Subsection 94.1(1) indicates that this issue must be examined in light of all the surrounding circumstances including those listed in paragraphs 94.1(1)(c) to (e), which are:

(a) the nature, organization and operation of any non-resident entity and the form of and the terms and conditions governing the taxpayer’s interest in, or connection with, any non-resident entity,
(b) the extent to which any income, profits and gains that may reasonably be considered to be earned or accrued, whether directly or indirectly, for the benefit of any non-resident entity are subject to an income or profits tax that is significantly less than the income tax that would be applicable to such income, profits and gains if they were earned directly by the taxpayer, and

(c) the extent to which the income, profits and gains of any non-resident entity for any fiscal period are distributed in that or the immediately following fiscal period.

The purpose test in section 94.1 requires a comparison of the taxes actually payable in respect of the portfolio investments and the taxes that would have been payable had the taxpayer acquired the portfolio investments directly. Further, the provision states that taxes payable in respect of the portfolio investments must be “significantly” less than the taxes that would have been payable otherwise. It is unclear what is meant by the term “significantly”. However, it appears that if no Canadian tax would have otherwise been payable in the year by the taxpayer if the taxpayer had held the portfolio investments directly (for example, because the taxpayer was in a loss position), then the tax avoidance motive test would not be met.\footnote{This point was made in \textit{Wiener} supra note 30 at page 4.}

Another element of the test is that the tax avoidance motive must be “one of the main reasons” for the taxpayer acquiring the interest in the non-resident entity. As such, the onus is on the taxpayer to demonstrate that \textit{none} of the main reasons for the investment was the reduction of Canadian tax. Although this test appears quite broad, this is one of the traditional shortcomings of section 94.1 (at least from the CRA’s perspective). While the determination is to be made based on all of the surrounding circumstances, it seems likely that many taxpayers with offshore investments have taken the position that such investments are held by them strictly for non-tax reasons (such as access to special fund managers, etc.).
3. **Summary**

The Federal government’s decision to backtrack from the FIE rules constitutes a significant reversal of tax policy. The Federal government has proposed to discuss the amendments with a panel of tax practitioners and there may be additional refinements to the offshore investment fund rules once these consultations have been completed. It will be interesting to see if the Federal government tries to strengthen these rules since it has acknowledged that taxpayers have largely been ignoring them in recent years.
Canadian Bar Association
2010 Tax Law for Lawyers

May 30 – June 4, 2010

NON-RESIDENT TRUSTS
AND
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