June 15, 2022

Trevor McGowan, Director General
Tax Legislation Division, Department of Finance
90 Elgin St
Ottawa, ON K1A 0G5
SENT VIA EMAIL: intergenerational-transfers-transferts-intergenerationnels@fin.gc.ca

Dear Mr. McGowan:

Re: Budget 2022 consultation on Bill C-208 and section 84.1

On behalf of the Conference for Advanced Life Underwriting (CALU) we are making this submission in response to the consultation announced in Budget 2022 relating to how the existing rules in section 84.1[1] could be strengthened to protect the integrity of the tax system while continuing to facilitate genuine intergenerational business transfers.

CALU has previously provided its comments and recommendations on this important issue in submissions to the Department of Finance (Finance Canada) dated September 29, 2017 (the "original submission") and September 17, 2021 (the "second submission")[2]. We continue to support the primary recommendations made in CALU's second submission and will only briefly comment on several additional issues that were not specifically addressed in that submission.

While we understand that Finance Canada does not intend to modify the existing rules that were introduced with the enactment of Bill C-208 on a retroactive basis, we have also included recommendations on potential amendments to section 84.1 in order to clarify their application to share transfers that have taken place since the enactment of Bill C-208.[3]

About CALU

CALU is the only national professional organization dedicated to advanced planning issues related to life underwriting, tax planning and wealth management. CALU's industry leading members include insurance and financial advisors as well as accounting, tax, legal and actuarial experts. Along with our partner organization, Advocis, we speak for more than 17,000 insurance and financial advisors in every part of Canada to grow and preserve the financial well-being of Canadians and family businesses.

[1] The Income Tax Act, R.S.C. 1985, C.1 (5th Supplement), as amended. Herein the "Act".
[2] We have included a copy of the second submission with this submission.
[3] Royal Assent was provided on June 29, 2021.

Discussion of revisions to section 84.1

As noted, CALU has already provided its recommendations relating to the criteria that might apply to any future amendments to the exception to section 84.1.[4] Based on further input from CALU members, we would like to make the following additional comments and recommendations:

- The exception should provide for situations where the taxpayers (i.e., the parents) may have already commenced the process of selling their shares to the next generation of owners.[5] As a result of prior transfers, at the time of a future transfer, the taxpayers may no longer own a majority of the voting shares in the subject corporation. We believe that the parents should continue to qualify for any exception to section 84.1 relating to a future sale of their remaining shares in the subject corporation.
- Some conditions/requirements for the exception to the section 84.1 equivalent in the Quebec Tax Act[6] (the "Quebec rules") differentiate between the sale of shares of the capital stock of a family farm or fishing corporation, and the sale of qualified small business corporation shares. We believe the conditions for any exception to section 84.1 should apply in a similar manner to all types of shares that are eligible for the exception to section 84.1.
- The exception should also provide for circumstances where the subject shares being transferred are shares of a holding company which does not control the downstream company which operates the active business. This may be the case where the shares of the operating company are owned by different holding companies representing different families or generations of family members.
- There is the ongoing concern that introducing a complex set of prescriptive rules to qualify for the exception to section 84.1, similar to those in the Quebec rules, would both be a significant barrier to small business owners accessing the exception and in turn could result in a number of business owners inadvertently not qualifying for the exception.

Recommendations relating to amendments to Bill C-208 provisions

Discussion of Bill C-208

The exception to section 84.1 contained in the amendments to the Act in Bill C-208 deem the selling shareholder (the "taxpayer") and the purchaser corporation "to be dealing at arm's length" in the following circumstances:

a) The shares being sold (referred to as the "subject shares") are qualified small business corporation shares or shares of the capital stock of a family farm or fishing corporation;
b) The purchaser corporation is controlled by one or more children or grandchildren of the taxpayer who are 18 years of age or older[7]; and
c) The purchaser corporation does not dispose of the subject shares within 60 months of their purchase.[8]

---

[4] As provided for in paragraph 84.1(2)(e) and subsection 84.1(2.3).
[5] The transfer of shares by the taxpayers may have commenced before the enactment of Bill C-208 or in reliance on the exception introduced in Bill C-208.
[6] Sections 517.5.3 – 517.5.11 of the Quebec Taxation Act, C. I-3.
[7] The extended definition of child in subsection 251(1) includes a spouse or common-law partner of a child.
[8] Paragraph 84.1(2)(e).

The exception to section 84.1 is not available where the purchaser corporation disposes of shares in the subject corporation within 60 months from the date of purchase (the "60-month rule"). In these circumstances, except where the disposition was "by reason of death," for the purposes of paragraph 84.1(2)(e), the following rules will apply:

a) The exception to section 84.1 contained in paragraph 84.1(2)(e) is deemed to have never applied;
b) The taxpayer is deemed, for purposes of section 84.1, to have disposed of the subject shares to the person who acquired them from the purchaser corporation; and
c) The 60-month period applicable to the sale under b) above is deemed to have begun when the taxpayer disposed of the subject shares to the purchaser corporation.[9]

An additional provision is intended to reduce the taxpayer's access to the lifetime capital gains exemption (only for the purpose of a sale transaction that falls under the exception to section 84.1) where the subject corporation has taxable capital employed in Canada exceeding $10 million.[10]

The new legislation also requires the taxpayer to provide the CRA with an independent assessment of the fair market value of the subject shares, as well as an affidavit signed by the taxpayer and by a third party attesting to the disposal of the shares.[11]

Recommended changes to the Bill C-208 provisions

Recently, the Canada Revenue Agency (CRA) has provided guidance and technical interpretations relating to various aspects of the new rules enacted by Bill C-208.

With respect to the 60-month rule, the CRA commented on the meaning of "by reason of death" and the tax implications that will arise where the subject corporation shares are transferred within the 60 month period and the "by reason of death" exception is not applicable.[12] The CRA's response indicated that in circumstances where the subsequent transfer of shares of the subject corporation is made by the purchaser corporation to an arm's length person or to the original transferor of the shares,[13] the 60-month rule would not exclude the original transfer from the application of paragraph 84.1(2)(e) and no adverse tax consequences would arise for the taxpayer from the subsequent transfer of shares of the subject corporation. Given this result, and the overall lack of clarity concerning the purpose of this rule, we recommend that the 60-month rule be repealed[14] to give effect to the CRA's interpretation of this provision.

The CRA also confirmed that the provision that appears intended to reduce a taxpayer's access to the lifetime capital gains exemption[15] does not apply for the purposes of section 110.6 and, therefore, does not actually have the impact of reducing a taxpayer's claim for the lifetime capital gains deduction.[16] As this provision does

---

[9] Paragraph 84.1(2.3)(a).
[10] Paragraph 84.1(2.3)(b).
[11] Paragraph 84.1(2.3)(c).
[12] CALU 2022 CRA Roundtable dated May 3, 2022 – Q. 3.1 and 3.2
[13] Meaning the person who transferred the shares to the purchaser corporation.
[14] As of the effective date of Bill C-208.
[15] Paragraph 84.1(2.3)(b).
[16] Supra note 12, Q 3.3.

not have any application as confirmed by the CRA, we would recommend that this provision be repealed effective as of the enactment date of Bill C-208.[17]

Finally, the CRA indicated that the requirement to provide the CRA with an independent assessment of the fair market value of the subject shares, as well as an affidavit signed by the taxpayer and by a third party attesting to the disposal of the shares, must be met to qualify for the exemption from section 84.1.[18] Given this view, and the significant tax implications that can arise for a taxpayer who fails to meet these documentary requirements, we believe it is appropriate to amend section 84.1 to permit for the "late filing" of these documents with a reasonable late filing penalty.

We would recommend that any such amendments to the provisions enacted by Bill C-208 be announced as quickly as possible to provide clarity to business owners who are undertaking, or who have undertaken, share transfers in reliance of these rules.

Conclusions

CALU is supportive of Finance Canada's goal of amending section 84.1 to accommodate genuine intergenerational business transfers while still protecting against potential tax abuse. As noted in this and our prior submissions, it is important that any changes to section 84.1 not create unnecessary restrictions that would impede the successful transfer of small businesses to the next generation of owners and effectively force business owners to sell their shares to arm's length purchasers.

We look forward to continuing our discussions on how these amendments can be implemented to preserve family-owned businesses while minimizing unintended tax consequences.

Yours truly,

Kelly Adams
Chair, Board of Directors

Guy Legault
President & CEO

encl.

cc: Lauchlin MacEachern, Director, Domestic Corporations and Resource, Finance Canada

---

[17] We would also like to restate our recommendation, as set out in our second submission, that we do not believe it is appropriate to claw back or eliminate access to the exemption (or access to the capital gains exemption) based on the "size" of the corporation. As well, we do not feel there should be a limitation based on the amount of the lifetime capital gains exemption being claimed. This could be a significant disincentive to transferring the business within the family and run counter to the purpose of having an exception for intergenerational transfers.

[18] Supra note 12, Q 3.4.

September 17, 2021

Trevor McGowan
Director General, Tax Legislation Division
Department of Finance
90 Elgin St Ottawa, ON K1A 0G5

Dear Mr. McGowan:

Re: Proposed Amendments to Section 84.1 to Permit Intergenerational Transfers

On behalf of the Conference for Advanced Life Underwriting (CALU), we are writing to supplement our submission to the Department of Finance (Finance Canada) dated September 29, 2017 (the "original submission"). In the original submission CALU provided comments and recommendations on how to amend section 84.1 of the Income Tax Act (Canada) (the Act) to better accommodate genuine intergenerational business transfers while still protecting against potential tax abuses. This submission updates the original submission to take into account more recent developments, including the recent enactment of Bill C-208[1] and the subsequent Finance Canada media releases[2], as well as the growing experience with the exception to the Quebec Taxation Act rules that are the equivalent to section 84.1.[3]

CALU is the only national professional organization dedicated to advanced planning issues related to life underwriting, tax planning and wealth management. CALU's industry leading members include insurance and financial advisors as well as accounting, tax, legal and actuarial experts. Through a strategic partnership with Advocis, we advocate on behalf of more than 13,000 advisors in support of fair and competitive public policies to grow and preserve the financial well-being of Canadian families and businesses.

---

[1] Royal Assent was received on June 29, 2021.
[2] In a press release dated July 19, 2021. Finance Canada indicated that it planned to bring forward amendments to Bill C-208 that would safeguard against unintended tax avoidance loopholes such a corporate surplus stripping. Herein referred to as the "press release".
[3] Sections 517.1-517.5.11 of the Quebec Taxation Act, CI-3.

Conference for Advanced Life Underwriting
Suite 600 - 170 Laurier Avenue West
Ottawa, ON K1P 5V5
Tel: 613-505-9632 • www.calu.com

Background

Finance Canada Consultation on Tax Planning Using Private Corporations

In 2017 Finance Canada announced a consultation on tax planning using private corporations.[4] As part of this consultation the government "invited views and ideas on whether, and how, it would be possible to better accommodate genuine intergenerational business transfers in the Income Tax Act while still protecting the fairness of the tax system by ensuring that any such accommodation cannot be used as a means to circumvent other rules in the Income Tax Act."

In the consultation paper, it was suggested that any exception to section 84.1 should include "hallmarks" that would ensure a genuine transfer of a business to the new owners. Such hallmarks would generally include to following criteria or conditions:

- the vendor ceasing on the transfer to have factual and legal control of the transferred business;
- the intent of the new owner to continue the business as a going concern long after its purchase;
- the vendor not having any financial interest in the transferred business; and
- the vendor not participating in the management and operations of the business.

The consultation paper also commented on a similar legislative exception in the United States:

> "For example, the United States has long-standing rules meant to distinguish cases where a parent "terminates" his or her interest in a corporation on the sale of shares to a family member including a corporation controlled by family members. In general terms, the approach of the United States is to rely on rules that establish a bright-line test that is not amenable to factual disputes about the genuineness of an intergenerational transfer of the small business corporation. It does so by simulating a straightforward arm's-length sale in which the vendor has no interest or involvement in the transferred corporation after the sale.
>
> The American approach arguably accommodates genuine intergenerational transfers because it does not prevent a parent/owner of a private corporation from having the corporation employ their children in the years leading up the actual transfer. During this period, the parent can transfer knowledge of the business to the child as well as assist the child in gaining the experience necessary to operate the business as a future owner."

[4] Consultation Paper entitled "Tax Planning Using Private Corporations" (Department of Finance, July 18, 2017). Herein referred to as the "consultation paper".

Conference for Advanced Life Underwriting
Suite 600 - 170 Laurier Avenue West
Ottawa, ON K1P 5V5
Tel: 613-505-9632 • www.calu.com

The Province of Quebec has already introduced an exception to the Quebec Taxation Act rules that are the equivalent to section 84.1.[5] Generally, these measures apply where the following conditions are met:

1. The shares being acquired are qualified small business corporation shares.[6]
2. The taxpayer disposing of the shares must be an individual other than a trust.
3. The taxpayer disposing of the shares (or the taxpayer's spouse) must have played an active role and held a substantial interest in the business (effectively 25% of votes and value) during the 24 months preceding the disposition.
4. The taxpayer disposing of the shares (or the taxpayer's spouse) does not play an active role in the business after the transaction.
5. The taxpayer disposing of the shares (or the taxpayer's spouse) does not exercise du jure control after the transfer of the shares.
6. The taxpayer disposing of the shares (or the taxpayer's spouse) does not hold common shares of the corporation after the transaction. The total fair market value of all the residual financial interests held by the transferor in the transferred business must not be greater than 60% (80% in the case of a farming or fishing business)[7]; and
7. After the sale, at least one person participating as a shareholder in the acquiring corporation plays an active role in carrying on the business.

Discussion of Hallmarks in Other Jurisdictions

We continue to be supportive of Finance's position that the exception to section 84.1 for family business transfers should be based on certain "hallmarks" or "bright-line tests" to ensure there is a genuine transfer of the business to the next generation of owners. However, we believe such hallmarks should not impose conditions or restrictions that would not apply in the case of an arm's length transfer, and that also recognize the realities of family-owned businesses. For example, the U.S requirements that the departing business owner terminate all interests in the business after the transfer of shares is not always a hallmark for an arm's length sale and does not consider the possibility of a forced sale due to the ill-health of the business owner. It is similarly important to permit the departing owner to retain some equity or debt in the transferred business for a period of time to assist their children, who might not qualify for traditional financing, to complete the purchase of the business. In fact, ongoing participation of the departing owner (both working in the business and continuing an ownership interest) in the transferred business, for a limited period of time, is a relatively common condition in arm's-length transactions.

---

[5] Sections 517.1 to 517.3 of the Quebec Taxation Act, C I-3. These measures apply to dispositions taking place after March 18, 2016.

[6] As defined in subsection 110.6(1) of the Act.

[7] There are a number of other terms and conditions applicable to financial interests retained by the transferor of shares.

Conference for Advanced Life Underwriting
Suite 600 - 170 Laurier Avenue West
Ottawa, ON K1P 5V5
Tel: 613-505-9632 • www.calu.com

In our original submission we attached a letter prepared by an expert in the area of arm's length acquisitions and divestitures of Canadian corporations.[8] The relevant portions of this letter are reproduced below relating to the vendor having a continued financial interest and management participation in the transferred business:

Continued Financial Interest

It is not unusual for the vendor of a privately-held Canadian company to retain a financial interest in the transferred business. Notable circumstances where this occurs include:

- the sale to a private equity firm. Such purchasers normally prefer that the vendor retain an equity position in the transferred business to align the interests of the parties. In some cases, the vendor may retain a majority equity position, although their ability to unilaterally control the business is subject to the provisions of a shareholder agreement;
- corporate buyers or individual investors who prefer to acquire a majority equity stake in the business. Such a transaction structure reduces the initial cash outlay for the purchaser and creates an economic incentive for the vendor through the put-call provisions of the retained equity interest; and
- a sale of the business to arm's-length management, who may have limited financial resources and must acquire the shares over time.

In lieu of, or in addition to, retaining an equity interest, many arm's-length transactions involve the vendor retaining a debt obligation against the transferred business. The obligation to the vendor is normally structured as a promissory note (or retractable preferred shares) which is subordinated to other obligations in the business. Such transaction structures (commonly referred to as a "vendor take-back") are frequently used in the acquisition of small and medium-sized private companies where the purchaser (often another small private company or individual) cannot secure sufficient financial resources at the closing date. The promissory note (or series of notes) may extend for several years following the transaction.

Continued Management Participation

It is very common for the vendor to continue participation in the management and operations of the transferred business. In fact, it is unusual for the vendor of a privately-held company to make a "clean break" at the closing date of the transaction. As a condition to the transaction, purchasers normally insist that the vendor enter into a management or consulting agreement to help facilitate the transition, particularly with respect to proprietary know-how, employee morale and customer relationships.

The duration and responsibilities of the vendor under the management or consulting agreement depends on numerous factors, including the nature of the business itself, the vendor's involvement in the business prior to the transaction, the experience and capabilities of the management team, and the vendor's health and personal circumstances. Where the transaction is structured such that a portion of the purchase price is contingent on the future operating results of the business (i.e. an earnout), the vendor normally insists on their continued

---

[8] Howard Johnson, MBA, FCPA, FCA, FCMA, FCBV, CPA, CFA, ASA, CF, C.Dir.

Conference for Advanced Life Underwriting
Suite 600 - 170 Laurier Avenue West
Ottawa, ON K1P 5V5
Tel: 613-505-9632 • www.calu.com

involvement in the business and their ability to manage the business in a way that maximizes the likelihood of achieving the earnout metrics.

Based on discussions with Quebec tax practitioners, we also have similar concerns with the criteria established to qualify for the Quebec exception to their equivalent of section 84.1. For example, the requirement that the transferor not play an active role in the business after the sale, and that the taxpayer (or taxpayer's spouse) not being able to hold any common shares in the corporation after the transaction, seem overly onerous in determining whether there has been a genuine transfer of the business.

With this background and after considering the dynamics and needs of family-owned businesses, we believe any exception to section 84.1 should permit the limited but ongoing participation of the transferor (and/or transferor's spouse) in the business (both from an ownership and management perspective) for a reasonable period of time. Our recommendations outlined below support this approach.

Discussion of Bill C-208

The amendments to section 84.1 contained in Bill C-208 deem the selling shareholder (the "taxpayer") and the purchaser corporation "to be dealing at arm's length" (and therefore not subject to the anti-avoidance rules in section 84.1) in the following circumstances:

a. the shares being sold (referred to as the "subject shares") are qualified small business corporation shares or shares of the capital stock of a family or fishing corporation;
b. the purchaser corporation is controlled by one or more children or grandchildren of the taxpayer who are 18 years of age or older[9]; and
c. the purchaser corporation does not dispose of the subject shares within 60 months of their purchase.[10]

The exception to section 84.1 is not available where the purchaser corporation disposes of shares in the subject corporation within 60 months from the date of purchase. In these circumstances, except where the disposition was "by reason of death," for the purposes of paragraph 84.1(2)(e), the following rules will apply:

a. The exception to section 84.1 contained in paragraph 84.1(2)(e) is deemed to have never applied;
b. The taxpayer is deemed, for purposes of section 84.1, to have disposed of the subject shares to the person who acquired them from the purchaser corporation; and
c. The 60-month period applicable to the sale under b) above is deemed to have begun when the taxpayer disposed of the subject shares to the purchaser corporation.[11]

---

[9] The extended definition of child in subsection 252(1) also includes a spouse or common-law partner of a child.
[10] New paragraph 84.1(2)(e) of the Act
[11] New paragraph 84.1(2.3)(a).

Conference for Advanced Life Underwriting
Suite 600 - 170 Laurier Avenue West
Ottawa, ON K1P 5V5
Tel: 613-505-9632 • www.calu.com

An additional provision is intended to reduce the taxpayer's access to the lifetime capital gains exemption (presumably only for the purpose of a sale transaction that falls under the new exemption to section 84.1) where the subject corporation has taxable capital employed in Canada exceeding $10 million.[12]

The new legislation also requires the taxpayer to provide the CRA with an independent assessment of the fair market value of the subject shares, as well as an affidavit signed by the taxpayer and by a third party attesting to the disposal of the shares, where the taxpayer is relying on the exemption to section 84.1.[13]

As noted above, Finance Canada officials are concerned that Bill C-208 does not contain the necessary hallmarks to ensure that the exception to section 84.1 prevents the opportunity for "surplus stripping", which would otherwise permit the conversion of taxable dividends to capital gains, without a genuine transfer of the business taking place. Finance Canada specifically mentioned the following possible criteria that amendments to Bill C-208 would address:

- the requirement to transfer legal and factual control of the corporation carrying on the business from the parent to their child or grandchild
- the level of ownership in the corporation carrying on the business that the parent can maintain for a reasonable time after the transfer
- the requirements and timeline for the parent to transition their involvement in the business to the next generation
- the level of involvement of the child or grandchild in the business after the transfer.

We agree with many of these concerns and believe that amendments to section 84.1 are warranted to ensure the exception is properly targeted and there is greater clarity relating to the requirements to qualify for the exception and the consequences associated with abusive tax planning.

Suggested "Hallmarks" for an Exception to Section 84.1

Similar to our prior submission, this section outlines a number of hallmarks that could be applied to qualify for the exception to section 84.1 and CALU's recommended approach.

a) Should the Vendor be a certain age to qualify for the exception?

We continue to believe it would be appropriate to establish a minimum age (for example, age 50) before the transferor is entitled to claim the exception from section 84.1. However, the exception should also be available if the transferor provides evidence of a medical condition which would prevent that person from participating in the business for a period of one year or longer.

---

[12] New paragraph 84.1(2.3)(b). The exemption will not be available once the subject corporation's taxable capital in Canada reaches $15 million.
[13] New paragraph 84.1(2.3)(c).

Conference for Advanced Life Underwriting
Suite 600 - 170 Laurier Avenue West
Ottawa, ON K1P 5V5
Tel: 613-505-9632 • www.calu.com

Commentary: Most family business transfers occur as a result of the retirement of the business owner. A minimum age requirement (or a significant health issue) would be one indicator that the transfer is being made for bona fide non-tax purposes.

b) *Can the Taxpayer Retain an Interest in the Subject Corporation?*

Upon the initial sale the taxpayer must dispose of a controlling interest (in excess of 50% of votes and value) of the subject corporation to “qualified individuals” and/or a “qualified purchaser corporation” that meet the conditions discussed below.

Within a three-year period of time the taxpayer must dispose of any remaining **voting** shares in the subject corporation to “qualified individuals” or a “qualified purchaser corporation”. The taxpayer would be permitted to retain debt and non-voting fixed value shares in the subject corporation for a period of up to 10 calendar years after the year of sale.

Commentary: The exception is designed to assist with the retirement and business succession planning for the current owner(s). Therefore, the current owner(s) must give up control of the business to the “next generation” as part of the initial sale transaction to benefit from the exception. However, as is the case with many arm’s-length purchase transactions, it is important that the current business owner(s) be allowed to participate in the operations of the business and retain a minority voting interest for up to a period of three years after the initial transfer of control to assist with a successful transition to the new owners.

c) *Who are Qualified Individuals?*

Qualified individuals would be defined to be any of the taxpayer’s children and grandchildren who are over the age of 17. As well, nephews/nieces and grandnephews/grandnieces of the taxpayer who are over the age of 17 would be qualified individuals.[14]

There should be a further requirement that at least one of the qualified individuals have regularly worked in the business or a related business on the equivalent of a full-time basis for at least a year in any of the five taxation years prior to the sale.

Commentary: The exception from the application of section 84.1 would not include transfers to siblings, grandparents, a spouse (or related entities) or any trust. As well, there is a requirement that at least one of the qualified individuals have worked in the business for the stated period of time prior to the sale transaction.

d) *What is a “Qualified Purchaser Corporation”?*

---

[14] This to avoid the Canada Revenue Agency making a factual determination that a nephew/niece or grandnephew/grandniece is factually not dealing at arm’s length with the taxpayer.

Conference for Advanced Life Underwriting
Suite 600 - 170 Laurier Avenue West
Ottawa, ON K1P 5V5
Tel: 613-505-9632 • www.calu.com

A qualified purchaser corporation would be defined as one where one or more qualified individuals own over 50% of the votes and value of the corporation. In addition, all other shareholders of the qualified purchaser corporation must deal at arm's length with the qualified individuals and the subject corporation, and not be affiliated with the subject corporation.

Commentary: The exception from section 84.1 should apply not only on a direct sale to qualified individuals (to permit hard basis for the full purchase price), but also to a sale to a purchaser corporation controlled by qualified individuals. However, the transferor is not permitted to own shares in the purchaser corporation.

e) *What Restrictions Apply to the Subject Corporation?*

The shares of the subject corporation must be qualified small business corporation shares or shares of the capital stock of a family farm or fishing corporation, as those terms are defined in section 110.6 of the Act.

Commentary: We are recommending that initially the exception would only apply to shares which qualify for the lifetime capital gains exemption. We further recommend that once the exception to section 84.1 has been in place for several years and appears to be operating appropriately, that the exception be expanded to apply to all Canadian-controlled private corporations. This is in recognition of the fact that many family businesses are now expanding into the United States and other international locations, with the result that the shares in such corporations may no longer meet the definition of qualified small business corporation shares. We don't believe that business owners and family members should be penalized through the potential application of section 84.1 for successfully expanding their businesses internationally.

f) *Does a Qualified Individual Have to Work in the Acquired Business After the Sale?*

Where a qualified individual purchases the shares in the subject corporation directly, that person must play an active role in the business for at least three years after the sale transaction through a senior management and/or board of director position with the subject corporation. Where the purchase is through a qualified purchaser corporation, a qualified individual must plan an active role in the business for at least three years after the sale transaction through a senior management and/or board of director position with the subject corporation or purchaser corporation.

Commentary: To qualify for the exception at least one qualified individual must participate in the business through a senior management or board of director role with either the subject corporation or the qualified purchaser corporation for at least three years after the sale transaction. An exception should be provided where the qualified individual cannot perform such duties during that three-year period due to ill health or death.

g) *What is the Extent of the Exception?*

The exception would apply to the full amount of the gain realized on the disposition of the shares of the subject corporation.

Conference for Advanced Life Underwriting
Suite 600 - 170 Laurier Avenue West
Ottawa, ON K1P 5V5
Tel: 613-505-9632 • www.calu.com

Commentary: We do not believe it is appropriate to "claw back" or eliminate access to the exemption (or access to the capital gains exemption) based on the "size" of the corporation. As well, we do not feel there should be a limitation based on the amount of the lifetime capital gains exemption being claimed. This could be a significant disincentive to transferring the business within the family and run counter to the purpose of having an exception for intergenerational transfers.

h) What Type of Consideration Does the Exception Apply to?

The exception would apply only to cash proceeds or prescribed debt received on the sale of the subject shares. Where debt is involved, the loan must have reasonable terms for repayment.

Commentary: The exemption would not be available on that portion of the proceeds that represent shares in the purchaser corporation or any related corporation.

i) Does the Exception Require an Independent Valuation/Affidavit?

There should not be a requirement for an independent valuation of the shares being sold, as contained in Bill C-208. We also don't believe the taxpayer should be required to file an affidavit relating to the transaction. Instead, we recommend that claiming the exception would need to be reported in the taxpayer's return in the year of disposition.

Commentary: The requirement to have an independent valuation and/or affidavit creates an additional layer of cost, complexity, and time that we do not feel is required. Instead, the Canada Revenue Agency (CRA) would receive notice that the exception to section 84.1 is being claimed (through the filing of an election with the corporate tax return for the year of the transaction), placing the CRA in the position where it can review the transaction to ensure that all requirements are satisfied, and that the sale transaction has taken place for fair market value.

j) Can the Taxpayer also Claim a Capital Gains Reserve?

The capital gain arising on the sale of the shares should be treated like any other capital gain and a reserve can be claimed where the proceeds of disposition of the property are payable after the end of the year as set out in the Act.[15]

Commentary: Where the exception to section 84.1 applies, the normal rules applicable to the determination of capital gains and the reporting of such gains would apply.

k) Would There be a Specific Anti-Avoidance Rule?

---

[15] Subparagraph 40(1)(a)(iii) and subsection 40(1.1) of the Act.

Conference for Advanced Life Underwriting
Suite 600 - 170 Laurier Avenue West
Ottawa, ON K1P 5V5
Tel: 613-505-9632 • www.calu.com

We would support the inclusion of anti-avoidance rules (similar to Bill C-208) that would “reverse” the benefits of the exception from section 84.1 if there are arrangements or transactions that were designed with the intent that the transferor would directly or indirectly retain or acquire control of the subject or purchaser corporation within a specified timeframe. However, exceptions should be provided if control is acquired as a result of the death of disability of a purchaser who was a qualified individual.

Commentary: The timing of the reversal of the tax benefits, penalties and interest as well as the extension of assessment time periods would need to be considered. However, if one of the possible triggering events for the application of the anti-avoidance rule is the subsequent sale of the shares to a third party, we believe any reversal of the tax benefits should only take effect in that particular taxation year and not the taxation year in which the exception to section 84.1 was claimed.

Conclusions

CALU supports the Government’s plan to amend section 84.1 of the Act to better accommodate genuine intergenerational business transfers while still protecting against potential tax abuse. As discussed in CALU’s original submission, family-owned businesses are the backbone of the Canadian economy and the local communities in which they operate. It is therefore extremely important for the government to remove the tax inequities which currently arise from the application of section 84.1 to bona fides intergenerational business transfers. We hope the recommendations made in this submission will be helpful in your consideration of how to implement these changes.

We look forward to having further dialogues with the Government and Finance Canada on how these changes can be implemented to preserve family-owned businesses while minimizing unintended tax consequences.

Yours truly,

Barry Pascal
Chair, Board of Directors

Guy Legault
President & CEO

cc: Shawn Porter, Associate Assistant Deputy Minister (Legislation)

Conference for Advanced Life Underwriting
Suite 600 - 170 Laurier Avenue West
Ottawa, ON K1P 5V5
Tel: 613-505-9632 • www.calu.com