JULY 23, 2021

# Parliament Votes to Facilitate Intergenerational Business Transfers

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Bill C-208, *An Act to amend the Income Tax Act* (*transfer of small business or family farm or fishing corporation*), which aims to amend section 84.1 of the *Income Tax Act* (Act) received royal assent on June 29, 2021. A majority of the House of Commons had voted in May on third reading in favour of private member's Bill C-208. On June 22, 2021, Bill C-208 passed (on division) without amendments by the Senate. Currently and in very general terms, when an individual sells shares of a corporation to a corporation controlled by a family member, section 84.1 of the Act may result in the proceeds from the sale being treated as a dividend, whereas such proceeds would receive more favourable capital gains treatment had the taxpayer sold these shares to an arm's-length party. Bill C-208, will limit the application of section 84.1 of the Act in cases of intergenerational transfers of a business. Since the bill has no coming-into-force provisions, it came into force on the day it received royal assent.

Section 84.1 of the Act is a specific anti-avoidance rule denying capital gains treatment on a wide range of transfers of shares of a corporation by an individual (Taxpayer) to another corporation with which he or she does not deal at arm's length (Purchaser Corporation). The purpose of the rule is to prevent "earning stripping" transactions taking advantage of lower capital gains tax rates. Where the rule applies, the individual is denied capital gains treatment and instead a deemed dividend is triggered, taxable at a higher rate. Importantly, the individual sellers cannot claim their lifetime capital gains exemption where they are disposing of shares of a qualified small business corporation, a family farm or fishing corporation. This means that individuals transferring their business to a corporation controlled by their children are taxed at a higher rate than those who sell their business to an arm's-length third-party. As currently drafted, section 84.1 of the Act thus has the effect of penalizing intergenerational business transfers as compared with arm's-length sales.

Bill C-208 carves out intergenerational transfers from the scope of section 84.1 by deeming the Taxpayer to operate at arm's length with the Purchaser Corporation when the corporation is controlled by one or more children or grandchildren of the Taxpayer who are 18 years of age or older, provided that the Purchaser Corporation does not dispose of the subject shares within 60 months of their purchase.

It is highly unusual for a private member's bill addressing tax matters to pass. The Department of Finance has been studying the issue of intergenerational business transfers for some time. Though Bill C-208 was sponsored by Conservative MP Larry McGuire, all parties have long supported amending section 84.1 to limit its effects on intergenerational business transfers. In fact, similar bills have been introduced in prior parliamentary sessions by Liberal MP Emanuel Dubourg, NDP MP Guy Carron and Bloc Québecois MP Xavier Barsalou-Duval. On third reading in the House of Commons, Bill C-208 received unanimous support from all parties except the Liberal Party (although it was a free vote, 18 Liberal members voted for the bill), citing alleged concerns with the lack of adequate safeguards to ensure that the carve-out is restricted to true intergenerational transfers. In the Senate, Bill C-208 was reviewed and approved by the Standing Senate Committee on Agriculture and Forestry. During third reading in the Senate, some concern was again raised regarding the unintended tax consequences of Bill C-208 – such as tax avoidance opportunities and the expansiveness of the bill. Proposed amendments, such as enabling Finance Canada to add specific regulations, were defeated. And the Senate passed Bill C-208 without amendments. Following the royal assent of Bill C-208, Finance Canada announced that it intended to introduce legislation to clarify that these amendments would apply at the beginning of the next taxation year, starting on January 1, 2022. However, on July 19, Finance Canada backtracked and accepted that Bill C-208 is in force as of June 29, 2021. However, the department announced that draft legislative amendments would be proposed for consultation to rectify any perceived loopholes in the bill that may foster tax avoidance. Once final, these amendments will be introduced and apply as of either November 1, 2021, or the date the final draft legislation is published, whichever is later.

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