A QUARTERLY PUBLICATION OF THE TAX SPECIALIST GROUP (TSG)

Introduction

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With this edition of Tax Perspectives, we welcome two new members to our group: Daye & Co. - Edmonton, and Ralph H. Green and Associates – Saint John, New Brunswick. This extends our coverage to nine firms in seven cities coast-to-coast across Canada. We will continue to build our network and expand our international group of associates as well.

Inside this issue, you will find the usual assortment of articles on Canadian tax matters. You will also find a summary of the recent U.S. tax cuts, and an article on U.S.-Canadian cross-border tax planning.

SUMMER 2003

VOLUME 3 • NUMBER 2

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Sale of a Business – Structuring Non-Compete Arrangements

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A recent decision of the Federal Court of Appeal, *Manrell v. The Queen*, 2003 FCA 128, March 11, 2003, has confirmed that when a business is being sold, it may be possible to arrange the sale so that a portion of the sale proceeds may escape taxation. This is good news for shareholders who are contemplating the sale of the shares of a company, where they have been active participants in the affairs of the company.

In 1995, Manrell entered into an agreement to sell the shares of three different corporations involved in manufacturing businesses. As part of the Share Purchase Agreement with the purchaser, Manrell was required to enter into a Non-Competition Agreement. Manrell received $3,927,078 for his shares and $979,575 for entering into the Non-Competition Agreement.

When Manrell filed his tax return, he reported the Non-Compete payment as proceeds giving rise to a capital gain. After receiving his notices of assessment, Manrell changed his position, on the basis of the decision of the Tax Court in *Fortino*, which had held that Non-Compete payments should be non-taxable amounts.

In considering the Manrell matter, the Federal Court of Appeal held that the taxpayer had not disposed of property; consequently, there was no resulting capital gain to be taxed and the position of the Tax Court was reversed.

The findings of the Federal Court of Appeal in *Manrell* lead us to consider what tax planning opportunities may arise from that decision. Only time will tell the extent to which this decision may be relied upon in structuring various business transactions, but the following possibilities, and cautions, come to mind:

- When a business is being sold, it is generally more beneficial for the vendor to sell shares rather than assets. The capital gains exemption had previously created this bias; now, the possibility of attaching a non-taxable “Non-Compete Agreement” to the share sale arrangement becomes an important planning consideration as it may provide an additional source of tax-free proceeds.

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U.S. Tax Cuts

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Culminating a process that began with the mid-term elections, the President signed into law the Jobs and Growth Tax Relief Reconciliation Act of 2003 on May 28, 2003. The legislation provides $350 billion of tax relief and $20 billion of aid to state governments.

The following are the major provisions of the Act:

Reduction in Tax Bracket Rates

The Act reduces the top federal tax bracket for individuals from 38.6% to 35% and decreases the interim brackets by 2%. Under prior law, these revisions were scheduled to be implemented over several years. The Act accelerates the effective date of the lower rates to January 1, 2003.

Capital Gains

The maximum long-term capital gains tax rate is reduced to 15% for most taxpayers and 5% for those taxpayers whose tax does not exceed the 15% bracket (income up to $47,450). Long-term capital gains were previously subject to a maximum tax of 20% for most higher income taxpayers.

Dividends

The rate of income tax on dividends is reduced from the normal marginal rate (up to 38.6%) to the rate of tax imposed on capital gains, 15% or 5%.

The reduced rate for dividends applies to both regular tax and alternative minimum tax. To be eligible for the reduced rates, the dividend must be paid on a share of stock held for more than 60 days before the ex-dividend date.

The reduced rate will apply to dividends from foreign corporations eligible for the benefits of a comprehensive income tax treaty with the U.S., provided that the Treasury Department determines that the treaty is satisfactory, and provided further that the treaty includes an exchange of information program. The treaty between the U.S. and Barbados is expressly unsatisfactory in light of the corporate inversion transactions that have used Barbados as the place to reincorporate. Dividends from a foreign corporation will qualify provided: (i) the foreign corporation is eligible for treaty benefits for substantially all of its income in the taxable year in which the dividend is paid, or (ii) the foreign corporation's stock is readily tradable on an established securities market in the U.S.

The tax cuts widen the gap between Canada and the U.S.

This takes direct aim at foreign corporations using tax havens and may have far-reaching implications.

Dividends received from a foreign corporation that was a foreign investment company (Code §1246(b)), a passive foreign investment company (Code §1297), or a foreign personal holding company (Code §552) do not qualify.

If a dividend from a foreign corporation qualifies for the reduced rate, 57% of the dividend income will be characterized as U.S. source income to reflect the difference in tax rates between the dividends (15%) and ordinary income (35%). This will have implications in claiming a foreign tax credit.

Alternative Minimum Tax

The Act increases the AMT exemption amount for married taxpayers filing a joint return and surviving spouses to $58,000, and for unmarried taxpayers to $40,250 for taxable years beginning in 2003 and 2004.

The alternative minimum tax is designed to ensure that all persons pay tax notwithstanding the deductions and other tax benefits to which they are entitled. If the income tax is less than the tentative alternative minimum tax, the taxpayer owes the difference as alternative minimum tax. The alternative minimum tax was designed to counter tax strategies of the wealthy. However, its scope has now begun to cover a substantial number of middle class taxpayers.

For an individual, the tentative minimum tax is 26% of the first $175,000 ($87,500 in the case of a married individual filing a separate return) of alternative minimum taxable income in excess of an exemption and 28% of the balance. The maximum tax rate on net capital gains is 20%. The tax cuts will make more people subject to the AMT.

Other Comments

The tax cuts widen the gap between the rates in Canada and those in the U.S., subject to state tax considerations. This is now especially pronounced on dividends. Also, keep in mind that the top tax bracket is not reached in the U.S. until family income exceeds around Cdn $500,000, five times the Canadian top bracket.

Notable by their absence from the Act, but likely to be resurrected, are provisions that were adopted in the Senate, including:

- Mark-to-Market rules for expatriating citizens and long-term residents;
- Provisions to discourage corporate inversions;

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U.S. Tax Cuts continued from page 2

- Determination of basis for amounts paid from foreign pension plans;
- Repeal of the foreign earned income exclusion for citizens or residents living abroad;
- Minimum holding periods for foreign tax credits with respect to withholding taxes on income other than dividends;
- Clarification of the economic substance doctrine, the U.S. equivalent of GAAR;
- Enhanced penalties for understatements of tax arising from transactions lacking economic substance;
- A response to the WTO decision regarding foreign sales corporations and the extraterritorial income exclusion;
- A limitation on the scope of foreign rabbi trusts;
- Anti-tax shelter provisions such as the adoption of an exception to confidentiality privileges relating to taxpayer communications and mandatory disclosure of reportable transactions by material advisors;
- Enhanced penalty provisions for failure to report interests in foreign financial accounts;
- Expanded authority to disallow tax benefits under Code §269;
- Modification of controlled foreign corporation/passive foreign investment company coordination rules;
- Modification of treatment of closely-held REIT's; and
- Denial of tax deductions for punitive damages.

In light of all the provisions that were proposed but not acted upon, the tax legislative agenda may be extremely active in the third and fourth quarters of this year.

Sale of a Business continued from page 1

- If a business sale is being structured as an "asset sale", it will be difficult to argue that any "Non-Compete" payments should not be subject to tax, as such amounts are likely to be regarded as being part of the bundle of intangible assets which are being sold as part of the total sale package. While an argument can be made that it is the individual shareholder who is giving up his right to compete, not the corporation which is selling its assets, CCRA may be quicker to challenge the non-taxability of non-compete payments in asset sale transactions.
- Taxpayers entering into Non-Compete Agreements at the time of selling shares are more likely to be successful arguing that the Non-Compete payments are not taxable if they have been actively involved with the business. Shareholders who have not been active will have a difficult time arguing that their Non-Compete undertakings have any real value.

Allocation of sale proceeds must be reasonable

- The allocation of the total sale proceeds between share proceeds and Non-Compete proceeds must be reasonable in the circumstances.
- The Non-Compete Agreement should set out as many undertakings by the vendor as possible. Consider delineating such items as: data, know-how, customer relationships, trade secrets, promises not to recruit employees, as well as promises not to compete directly or indirectly, by way of loan, investment or in any other manner.
- Where shareholders are parties to a Unanimous Shareholders' Agreement, which specifies that all shareholders receive the same price per share, the active shareholders may get additional proceeds by way of Non-Competition proceeds, whereas non-active shareholders would not get such proceeds. Any attempt to equalize the proceeds on a per-share basis would likely weaken any argument that some of the proceeds are anything other than share sale proceeds.
- Some may argue that it may be possible to extend the rationale in *Manrell* to situations where a key employee possessing special knowledge, customer relationships, etc., is departing and enters into a Non-Compete Agreement with his employer. Unfortunately, the provisions of paragraph 6(3)(e) of the Income Tax Act may serve to deem such amounts to be employment income that would be fully taxable. Accordingly, considerable care must be exercised when trying to apply the rationale in *Manrell* to such situations.
- The GST consequences attached to the non-compete arrangements are not clear as different commentators have expressed differing views on this question. Hopefully, some clarity will be added to the GST question by way of a CCRA ruling or other pronouncement.

The findings in the *Manrell* case provide us with an important tax planning opportunity when structuring sale transactions. The early indications are that the Crown will not seek leave to appeal this decision to the Supreme Court of Canada. This may simply signify that the Minister of Finance will introduce amendments that will be designed to block the favourable findings in Manrell. As a result, the tax planning opportunities confirmed by Manrell may be short-lived.

REDUCED STANDBY CHARGE FOR AUTOMOBILES WELCOMED

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Where an employer provides an automobile to an employee, a personal benefit is assessed based on two-thirds of the lease cost or 24% of the capital cost of the vehicle. This is over and above a benefit for paying for the employee's gasoline, insurance and repairs.

Prior to 2003, the standby charge would only be reduced if personal use was less than 10%. The new rules for the calculation of the standby charge, introduced in the recent federal budget, will reduce standby charges for employer-provided automobiles for a significant number of taxpayers.

Commencing in 2003, the standby charge will be reduced if both:

- personal use of the automobile is less than 1,667 kilometres per month (increased from 1,000 kilometers per month); and
- the automobile is used "primarily," (i.e., more than 50%) for business purposes.

The employer must require the employee to use the car to carry out employment duties, and this should be evidenced in a written employment contract.

When all the tests are met, the standby charge is reduced by business travel. Thus, if an employee has greater than 50% business use, the reduction will be available.

Example 1

An employee uses an automobile costing the employer $35,000. The standby charge, before the reduction for low personal use, is $8,400 (24% of the original cost of the car). The car was available for 12 months and was driven 10,000 personal kilometers and 30,000 business kilometers. The standby charge for 2003 will be $2,100, 25% of what would previously have resulted.

Example 2

A sports car is leased for $2,000/month, or $24,000 a year. The standby charge would have been $16,000 (two-thirds of the lease cost). Assume the car was driven 12,000 personal kilometers and 36,000 business kilometers. The standby charge would now be $4,000.

Example 3

The sports car above is leased by the employee directly, and an allowance of $2,000 per month is paid to the employee. The allowance is a taxable benefit and is included in income. The employee may deduct the lease payments, subject to pro-ration based on personal use, and a ceiling on deduction of around $9,600. This will result in a benefit of about $16,800 ($24,000 less $9,600). Clearly, employer leasing is far better, except that the employer is now stuck with not being able to deduct the full lease payments.

Keep a good business log of your mileage

Comments on the New Rules

The changes will mean that more employees with employer-provided automobiles will qualify for the reduction for low personal use. Now it is more important than ever to keep personal driving to a minimum by:

- Planning trips to maximize business mileage;
- Using an alternative vehicle for personal mileage. For example in two-car families, use the personal car for personal use rather than the company car, whenever possible; and
- Making business calls on the way to or from work to convert personal kilometers to business kilometers.

Other factors such as selecting a vehicle that does not meet the definition of an automobile may also reduce the benefit associated with an employer owned vehicle. Typically a ½ ton truck with one bench seat may qualify for this treatment.

The easiest way to reduce your standby charge and keep the taxman at bay is to keep a good business log of your mileage. Without hard evidence, CCRA are typically not very receptive to reducing the standby charge even if it is obvious that you should qualify. While it is not legislated that you keep a log, it is good business practice.

The reduced standby charge has another side benefit. In lieu of calculating the actual taxable benefit for employer-paid gasoline, insurance, maintenance, etc., a benefit of 50% of the standby charge may be used instead. Under the new reduced standby charge, this may be far lower than in the past, and may prove beneficial.

Cars depreciate quickly. Some say that a new car drops in value by 20% when driven out of the dealer's parking lot. The standby charge for a vehicle owned by the employer is based on its original cost. If it is transferred to a related company after, say, one year, a new and much reduced cost will then apply for purposes of the standby charge calculation.

CAR EXPENSES – SOME THINGS TO ARGUE ABOUT

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The Canada Customs and Revenue Agency (CCRA) takes the position that the trip from home to the office and back is personal, not business travel. This is important for how much may be claimed for car expenses and the reduced standby charge. But is this policy correct?

How and what constitutes personal travel has never been clear. Is usage based on time, mileage, or a combination? Either way, the results will be the same if personal travel and business travel have the same characteristics. But, if you are stuck in traffic during the week, and go out of town by highway to the cottage on most weekends, time usage may produce a very different result to that of mileage.

Decades ago, when the original policy concerning business versus personal usage was devised, there were no such things as car phones, personal computers, satellite navigation systems, voice activation, emails, or the internet. But things have changed.

Consider the scenario below, which may occur some time in the near future.

Tom is a business executive who uses his car for his employment-related duties. Most mornings, he gets into his car and, before leaving, checks his emails, which are sent to him over the internet through a satellite link to the car's built-in P.C. He responds to one urgent email by voice activation before driving off. On the way, Tom is notified that he has two more emails, one of which is urgent. He pulls over for a moment to read that email. He dictates a quick memo to his secretary, and transmits it through his wireless internet connection. Tom returns one phone call on his voice-activated phone and routes two voice mails around the office.

Tom's navigation unit shows his appointments for the day, the quickest routing from one location to another, and how busy the major highways are. He then listens to a daily briefing from his company, sent over the internet in a voice-digitized format.

Tom's car logs every journey on its PC, recording the time and the mileage. Tom indicates on each occasion whether the trip is business or personal.

Tom has an appointment with CCRA the following day in which he proposes to argue that his business usage of the car is 86%, and that his travel from home to the office and back is business travel. He proposes a calculation basis that uses an average of time spent and distance traveled. If Tom is unsuccessful, he will take the matter to court. (He is no longer prepared to accept that his trip from home to office is personal.)

Along with the car came $8,000 of computer hardware and software. Tom leases the car and has deducted the lease payments for this equipment in full.

IN BRIEF

A Summary of Certain Recent Developments

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Professional Incorporation

On October 30, 2002, the Ontario Business Corporations Act ("OBCA") was amended to allow certain professionals to incorporate their practices. It stated that professional corporations can carry on "activities related to or ancillary to the practice of the profession, including the *temporary* investment of surplus funds earned by the corporation." The recent amendments deleted the word "temporary," effective upon the Bill's receiving royal assent. This amendment would seem to alleviate concerns that the after-tax funds earned in a professional corporation would have to be removed.

Interest Expense on Income Trust Units

In general, interest expense is deductible if a loan is used for an eligible purpose. Interest continues to be deductible after the asset is no longer owned, if the loan is reduced for any proceeds or deemed proceeds on disposition of the asset, or if the funds are reinvested. A recent Technical Interpretation states that where a capital distribution has been received from an income trust, the capital distribution must reduce the amount of the loan upon which the interest is to be deducted. Therefore, careful monitoring will be required for those situations where borrowings have been incurred in order to buy income trust units. A similar principle should apply to all mutual fund investments, one would think.

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IMMIGRANT TRUSTS

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Under Canadian income tax laws, new immigrants to Canada are able to shelter income from Canadian tax for a period of up to 60 months through an immigrant trust.

An immigrant trust is an international trust established by a person who has immigrated to Canada, and who has not previously been resident in Canada for 60 months during his lifetime. The immigrant may establish the trust, either before or after becoming a resident of Canada, with a contribution of property to the trust. However, if the trust is established after he becomes a resident, the 60-month tax exempt period is reduced by the number of months in which he was Canadian resident. In addition, if the property contributed to the trust has appreciated in value, then the immigrant will be subject to capital gains tax in Canada on the appreciation when the property is transferred to the trust.

The beneficiaries of an immigrant trust are typically the immigrant and family members who have moved to Canada.

The tax consequences on a contribution of property to an immigrant trust in the immigrant's country of origin should be kept in mind in the design of the trust. For example, persons moving to Canada from the U.K. may remain subject to U.K. inheritance tax for five years. If not carefully structured, this tax, at 20%, can be a very unwelcome surprise.

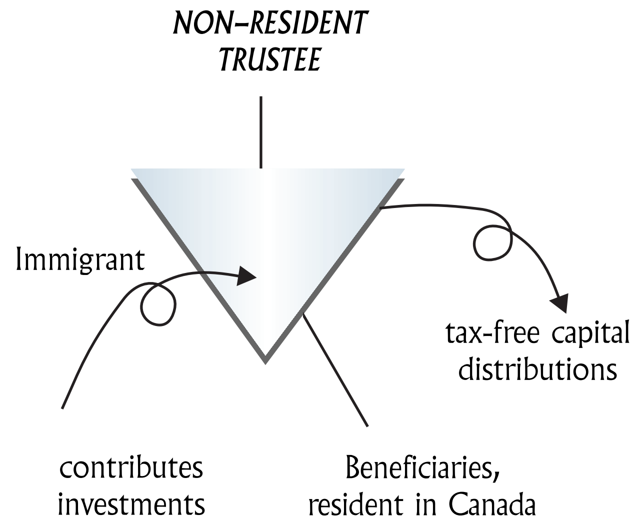
Income accumulates on a tax-free basis in the trust, which becomes part of trust capital

An immigrant trust is typically established in a tax favourable jurisdiction, and therefore no tax is payable on the income or capital gains earned by the trust. In this way, income accumulates on a tax-free basis in the trust, which becomes part of trust capital under trust law principles. Capital can be paid to beneficiaries tax-free, and therefore the accumulating income once capitalized, will not be subject to Canadian tax, even if distributed to Canadian resident persons.

Although the immigrant trust was designed to last for five years, it can be useful to keep the trust beyond this timeframe. If a beneficiary later ceases to be Canadian resident, the departure tax rules could be avoided for property held by the immigrant trust. It may also be possible to distribute income to non-residents and thereby prevent Canadian tax in the trust once it loses its exemption.

Following the expiration of the 60-month tax-exempt period, the immigrant trust is deemed to be Canadian resident. These rules provide that the exemption period ends at the beginning of the calendar year in which the settlor completes the 60th month of his Canadian residency. Therefore, without proper tax planning, the actual exemption period could be less than 60 months.

Planning is available to ensure that immigrants benefit from the entire 60-month tax-exempt period. For example, by changing the residence of the immigrant trust to Canada, the trust would be deemed to have a year-end immediately before the date on which the trust became Canadian. The preceding period would be tax-exempt. In addition, there is a step up in the cost base of the trust assets at that time, and thus the appreciation in the underlying value of the trust assets is not subject to Canadian tax. Alternatively, the immigrant trust could be wound up immediately before the end of the 60th month. The trust assets could be distributed on a tax-free basis to the beneficiaries as capital distributions. As stated earlier, capital distributions are not taxable to Canadian residents.



As many as 200,000 people immigrate to Canada each year. Of those, a sizeable number have over $1 million in investable assets (the threshold to make this planning feasible). Many do not take advantage of the opportunity.

This planning can also be applied to executives who come to Canada to live, but earn a component of their salary from outside Canada. This foreign salary can sometimes be structured to be income of the trust, making it free of Canadian tax.

U.S.-CANADIAN CROSS-BORDER PLANNING

Nova Scotia Unlimited Liability Companies (Part 2)

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As you may recall from my article in the Spring 2002 edition of *Tax Perspectives*, a Nova Scotia unlimited liability company (NSULC) is a Nova Scotia company whose shareholders elect to have unlimited liability for corporate debts. One may wonder why on earth anyone would make such an election. The answer is that this election causes the NSULC to be treated as a flow-through entity for US tax purposes, such that a US shareholder of an NSULC reports its share of the NSULC's income and expenses directly on its US tax return. For Canadian tax purposes, an NSULC is treated just like any other Canadian corporation. This hybrid treatment provides a host of tax planning opportunities for US taxpayers owning Canadian businesses or investments.

My previous article focused on two of the most obvious benefits for US shareholders of NSULC's. First, the NSULC enables US taxpayers to avoid double taxation – by permitting, on the shareholder's US return, a foreign tax credit for the underlying Canadian corporate income tax paid by the NSULC. Second, where the NSULC has losses, these may be deductible on the US return of its shareholder. This article will highlight some other tax advantages that NSULC's can provide, as follows:

- **Interest paid by Canadian company to US shareholder:** A loan to a wholly-owned NSULC from its US shareholder would be disregarded for US tax purposes. If properly structured, interest paid by the NSULC would be deductible by the NSULC for Canadian tax purposes but would not constitute income to the shareholder for US tax purposes. This may achieve a significant reduction in the overall tax rate. Planning such an arrangement must take into account the Canadian thin capitalization rules, which generally limit the deductibility of interest where the total debt to related non-residents exceeds twice the company's equity, and the 10% withholding tax that would apply to interest payments.
- **Acquisition of a Canadian corporation by a US purchaser:** In acquisition negotiations, the vendor and purchaser typically have conflicting interests regarding whether to sell shares or assets – because the vendor's tax on the sale will be lower if he sells shares, but the purchaser will want to buy assets to obtain an increase in the cost of the assets for tax purposes. However, conversion of the corporation to an NSULC may ameliorate this conflict, by allowing the vendor to sell shares while creating a bump to the cost of the corporate assets for US (but not Canadian) tax purposes. Proper structuring of such an acquisition may also include a loan to the NSULC creating interest as described above.
- **Avoidance of double taxation on transfer pricing adjustments:** The amount charged for goods and services between related parties must meet the arm's length standard for both US and Canadian tax purposes. However, determination of an arm's length charge is often difficult or impossible, leaving taxpayers vulnerable to transfer pricing adjustments by the IRS or CCRA. In a US parent – Canadian subsidiary scenario, such a transfer pricing adjustment exposes the US parent to double taxation unless the subsidiary is an NSULC.

  This can be illustrated by a simple example. Assume the US parent provides management services to the Canadian subsidiary, for which it charges a fee. Where the subsidiary is an ordinary Canadian corporation, the fee will create income to the parent company for US tax purposes. If CCRA were to reduce the amount of the fee that is deductible to the subsidiary, double taxation would arise unless the parent company can obtain a corollary reduction in its income inclusion (by consent of the IRS or recourse to the competent authority provisions of the Canada-US Tax Treaty). However, where the subsidiary is an NSULC, all transactions between it and the parent would be disregarded for US tax purposes; thus, the parent would not have an income inclusion for the fee charged to the NSULC, and a reduction in the deduction allowed to the NSULC by CCRA would not create double taxation.
- **Cross-border estate freeze:** Perhaps the most common estate planning device is an estate freeze, in which parents transfer appreciating assets to a freeze company so that future appreciation inures to their children. Where children live in the US however, an estate freeze will generally create disastrous US tax consequences to the children unless the freeze company is an NSULC. That is because, if the freeze company is an ordinary corporation, it will generally be a foreign personal holding company for US tax purposes, which then creates two big problems for the children living in the US: first, they will have to include in income annually their pro rata share of the income of the freeze company, and second, the common shares they own in the freeze company will not receive a step-up in tax basis for US purposes on the death of the parents. If the freeze company is an NSULC, foreign personal holding company characterization is avoided.

As you can see from the above examples, the NSULC has many uses in US-Canadian cross-border tax planning. In implementing an NSULC, the importance of proper planning cannot be overemphasized. The truism in tax planning – that the devil is in the details – is particularly critical where two tax jurisdictions are involved.

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Split Donation Receipts

The December 20, 2002 Technical Bill introduced new provisions that allow charities and political parties to issue tax receipts to donors for the difference between the value of their gift and any consideration received in return. These new rules apply to individual and corporate gifts and political donations made after December 20, 2002. The provisions deal with the calculation of how much the donation is and how to calculate the benefit conferred on the donor.

In Income Tax Technical News No. 26, the CCRA has given guidelines as whether an eligible gift exists and the value of the benefit to the donor. The eligible gift is generally the difference between the amount given to attend the event and the advantage given to the donor. The CCRA states that no advantage is conferred to the donor unless the benefit exceeds the lesser of 10% of the ticket price and $75. In making this calculation, the value of the activity, such as the meal at a fund-raising event, is excluded. Examples of benefits are such things as key chains or t-shirts that are given out at a golf tournament, souvenirs or gifts. Within these guidelines, no reduction need be made when issuing the donation receipt.

The guidelines also include details on how the split receipt policy applies to charitable annuities, donations of mortgaged property, charity auctions, lotteries, concerts, shows, sporting events, golf tournaments and membership fees. The guidelines are available for review on our website at www.taxspecialistgroup.ca

R&D Filing Crackdown

The CCRA announced in its December 2002 newsletter of the Toronto Centre CCRA & Professionals Consultation Group that, as of January 15, 2003, claims for SR&ED that are not complete by the filing deadline will be rejected. This means that it is not sufficient to file some of the SR&ED information on time and amend it later. Instead, it must be complete. In the past, many claimants have filed within the 18-month period, but have received 30-day letters subsequently asking for the missing information. In the future, CCRA will not issue a 30-day letter for those claimants that are past the 18-month deadline for filing. Therefore, to be safe, all claimants should file their tax returns within, say, 16 months, so that if a 30-day letter is issued, there is still time to get information to CCRA on time

Poison Pills on Foreign Spin-Offs

Foreign spin-offs can be tax-free in Canada, pursuant to section 86.1, provided a number of steps and tests have been met. However, the CCRA had previously stated that only common shares could be issued in order for a foreign spin-off to qualify as tax-free. When asked about poison pills rights that are sometimes received along with common shares, the CCRA stated that "it is prepared to accept that, generally, section 86.1 can apply in situations involving such rights, provided that the rights were established for bona fide commercial reasons and not to obtain a tax benefit, and provided that the rights established under the plan did not have any significant value independent of the shares being spun off at the time of the spin off." Therefore, in those spin-offs where the taxpayers also receive a right under a poison pill plan, it would now qualify as a tax-free spin-off. The CCRA also stated that it will accept late-filed elections under subsection 86.1 for those foreign spin-offs that may have been disallowed in the past.

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Tax Perspectives is published quarterly by the Tax Specialist Group (TSG).
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