

Checklist: new proposed intergenerational transfer options

As first announced in the 2023 Federal Budget, changes are proposed to the rules enacted in Bill C-208 to ensure that only genuine intergenerational family business sales will qualify for the rule deeming family members to be dealing at arm's length, such that a deemed dividend under subsection 84.1(1) will not apply .

In particular, two new proposed approaches are available for intergenerational business transfers:

- Immediate business transfer (3 year test)
- Gradual business transfer (5 - 10 year test)

The criteria for each transfer approach are very detailed, so CPA Canada has compiled this checklist to facilitate your analysis of the proposed legislation. When all criteria are satisfied, section 84.1 will generally not apply as the parties will be deemed to be dealing with each other at arm's length. As you read through the checklist, conditions that apply to both approaches are shown as a single column.

Disclaimer: This checklist is based on the revised draft legislation released on August 4, 2023, and may be subject to further change. The information contained below is a summary of the draft legislation and should not be relied upon as a substitution for reviewing legislation. Given the complexity of the rules and the inability to align the rules with all potential scenarios, it is prudent to ensure proper due diligence is completed to ensure compliance with the legislation.

CONDITIONS AND SPECIFIC CRITERIA TO CONSIDER	
IMMEDIATE TRANSFERS (3-YEAR TEST)	GRADUAL BUSINESS TRANSFERS (5- TO 10-YEAR TEST)
Conditions that apply before and at the time of disposition	
<input type="checkbox"/> Immediately before the disposition of the subject shares ("disposition time"), the following two conditions must be met: <ul style="list-style-type: none"> <input type="checkbox"/> The vendor, either alone or together with their spouse or common-law partner ("spouse"), controls the subject corporation and no other person or group of persons can legally or factually control the subject corporation. <input type="checkbox"/> The vendor has not sought a previous exception to the application of a deemed dividend under paragraph 84.1(2)(e)¹ with regards to an active business relevant to the determination of whether the subject shares qualify as qualified small business corporation shares (QSBC)² or shares of the capital stock of a qualified family farm or fishing corporation (QFFF)³ (referred to as a "relevant business") 	
<input type="checkbox"/> At the disposition time, the following three conditions must be met: <ul style="list-style-type: none"> <input type="checkbox"/> The vendor must be an individual (other than a trust); <input type="checkbox"/> The purchaser corporation must be controlled by one or more of the vendor's children⁴ who are 18 years of age or older; and <input type="checkbox"/> The subject corporation shares are either: 	

¹ This includes the utilization of paragraph 84.1(2)(e) as enacted under Bill C-208

² As defined in subsection 110.6(1)

³ As defined in subsection 110.6(1)

⁴ The proposed meaning of child of a taxpayer has the same meaning found in subsection 70(10) but is expanded to include a niece or nephew of the taxpayer, a niece or nephew of the taxpayer's spouse and spouses of these individuals.

<input type="checkbox"/> QSBC ⁵ ; or <input type="checkbox"/> QFFF ⁶	
Conditions related to the transfer of economic interests in the business	
<input type="checkbox"/> At all times after the disposition time, the vendor does not – either alone or together with a spouse, own directly or indirectly: <ul style="list-style-type: none"> <input type="checkbox"/> 50% or more of any class of shares, other than shares of a “specified class”⁷ of the subject corporation or the purchaser corporation; or <input type="checkbox"/> 50% or more of any class of equity interest (other than a specified class) in any relevant group entity 	
<input type="checkbox"/> Within 36 months of the disposition time and all times thereafter, the vendor and their spouse does not own, directly or indirectly: <ul style="list-style-type: none"> <input type="checkbox"/> Any shares of the capital stock (other than a specified class) of the subject corporation or of the purchaser corporation; or <input type="checkbox"/> Any equity interest (other than a specified class) in any other person or partnership (“relevant group entity”) 	
<input type="checkbox"/> No additional criteria	<input type="checkbox"/> Within 10 years after the disposition time (“final sale time”) and at all times after, the vendor and their spouse does not own, directly or indirectly, debt or equity interests in any of the subject corporation, the purchaser corporation, and any relevant group entity with a fair market value that exceeds 50% (for QFFFs) and 30% (for QSBCs) of the fair market value of all the interests that they owned before the disposition time
Conditions related to the transfer of control of the business	
<input type="checkbox"/> At all times after the time of sale, the vendor does not – either alone or together with a spouse, legally or factually control : <ul style="list-style-type: none"> <input type="checkbox"/> The subject corporation; <input type="checkbox"/> The purchaser corporation; or, <input type="checkbox"/> Any relevant group entity that carries on a relevant business at the disposition time 	<input type="checkbox"/> At all times after the time of sale, the vendor does not – either alone or together with a spouse, legally control : <ul style="list-style-type: none"> <input type="checkbox"/> The subject corporation; <input type="checkbox"/> The purchaser corporation; or, <input type="checkbox"/> Any relevant group entity that carries on a relevant business at the disposition time

⁵ As defined in subsection 110.6(1)

⁶ As defined in subsection 110.6(1)

⁷ As defined in subsection 256(1.1), generally defined to be fixed value shares that are non-voting, non-convertible and dividends on these shares must be fixed at amount not exceeding a prescribed limit.

<p><input type="checkbox"/> From the disposition time until 36 months after that time:</p> <ul style="list-style-type: none"> <input type="checkbox"/> (1) The child or group of children legally controls the subject corporation and the purchaser corporation;* <input type="checkbox"/> (2) The child, or at least one member of the group of children, is engaged on a regular, continuous and substantial basis⁸ in a relevant business of the subject corporation or a relevant group entity; and 	<p><input type="checkbox"/> From the disposition time until the later of 60 months after the disposition time and the final sale time:</p> <ul style="list-style-type: none"> <input type="checkbox"/> (1) The child or group of children legally controls the subject corporation and the purchaser corporation;* <input type="checkbox"/> (2) The child, or at least one member of the group of children, is engaged on a regular, continuous and substantial basis⁹ in a relevant business of the subject corporation or a relevant group entity; and
<ul style="list-style-type: none"> <input type="checkbox"/> (3) Each relevant business of the subject corporation and any relevant group entity is carried on as an active business 	<ul style="list-style-type: none"> <input type="checkbox"/> (3) Any relevant business of the subject corporation and any relevant group entity is carried on as an active business

* Exceptions:

All three conditions above are deemed to have been met:

- if one or more children, having control, disposed of all shares in the capital stock of the purchaser corporation, subject corporation or all relevant group entities to an arm's length person or group of persons
- if one or more children, having control, disposed of the shares in the capital stock of the purchaser corporation, subject corporation or a relevant group entity to another child or group of children of the taxpayer
- if a child or each of the children, who are actively engaged on a regular, continuous and substantial basis, has died or has, after the disposition of the subject shares, suffered one or more severe and prolonged impairments in physical or mental functions.

Condition (3) above is deemed to have been met:

- if a business of a subject corporation or a relevant group entity has ceased to be carried on due to the disposition of all of the assets that were used to carry on the business in order to satisfy debts owed to creditors of the corporation or of the entity.

⁸ As defined in the Tax On Split Income (TOSI) rules in paragraph 120.4(1.1)(a) i.e. excluded business test

⁹ As defined in the Tax On Split Income (TOSI) rules in paragraph 120.4(1.1)(a) i.e. excluded business test

Conditions requiring the transfer of management of the business to children	
<p>Within 36 months of the time of sale (or greater under reasonable circumstances), the vendor and their spouse takes reasonable steps to:</p> <ul style="list-style-type: none"> <input type="checkbox"/> Transfer management of each relevant business of the subject corporation and any relevant group entity to the child, or at least one member of the group of children, who are actively engaged on a regular, continuous and substantial basis;* and <input type="checkbox"/> Permanently cease to manage each relevant business of the subject corporation and any relevant group entity 	<ul style="list-style-type: none"> <input type="checkbox"/> Within 60 months of the time of sale (or greater under reasonable circumstances), the vendor and their spouse takes reasonable steps to: <ul style="list-style-type: none"> <input type="checkbox"/> Transfer management of each relevant business of the subject corporation and any relevant group entity to the child or at least one member of the group of children, who are actively engaged on a regular, continuous and substantial basis;* and <input type="checkbox"/> Permanently cease to manage each relevant business of the subject corporation and any relevant group entity
<ul style="list-style-type: none"> <input type="checkbox"/> * Exceptions: The conditions above are deemed to have been met: <ul style="list-style-type: none"> <input type="checkbox"/> if one or more children, having control, disposed of all shares in the capital stock of the purchaser corporation, subject corporation or all relevant group entities to an arm's length person or group of persons <input type="checkbox"/> if one or more children, having control, disposed of the shares in the capital stock of the purchaser corporation, subject corporation or a relevant group entity to another child or group of children of the taxpayer <input type="checkbox"/> if a child or each of the children, who are actively engaged on a regular, continuous and substantial basis, has died or has, after the disposition of the subject shares, suffered one or more severe and prolonged impairments in physical or mental functions 	
Election form requirement	
<ul style="list-style-type: none"> <input type="checkbox"/> The vendor and the child, or the vendor and each member of the group of children need to elect in prescribed format to have new proposed paragraph 84.1(2)(e) to apply. This will deem the taxpayer and purchaser corporation to deal with each other at arm's length at the time of the sale of the subject shares. The election must be filed on or before the vendor's filing due date for the taxation year that includes the disposition time. 	