TAX FOR THE Owner-Manager

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Evoy Estate: The Meaning of Subsection 104(2) Clarified

In *Evoy Estate v. The Queen* (2016 TCC 263), the issue in dispute was whether the minister had properly treated the appellant (which was one of three testamentary trusts created in the will of the late George Kenneth Evoy [George]) along with two other trusts created pursuant to the will as one individual pursuant to subsection 104(2). That subsection allows the minister to treat multiple trusts as a single trust for the purposes of the Act if

1) substantially all of the property of the various trusts has been received from one person, and
2) the various trusts are conditioned so that the income thereof accrues or will ultimately accrue to the same beneficiary or group or class of beneficiaries.

The facts are relatively straightforward. George died on November 17, 2007 and was survived by his spouse (Pauline) and by his three children (David, Wendy, and Karie) and their respective children. Pursuant to George's will (as amended), George created three separate trusts: one for the appellant (David's trust) and two other trusts ultimately benefiting the two other children (Wendy's trust and Karie's trust). Each of David's trust, Wendy's trust, and Karie's trust was entitled to a block equal to approximately one-third of the testator's shares in a certain corporation. Each of David's trust, Wendy's trust, and Karie's trust was one to which subsection 70(6) applied (that is, each trust was a trust colloquially referred to as a spousal rollover trust).

The terms governing David's trust provided that Pauline was to receive the net income of David's trust during her lifetime. The terms of David's trust further provided that after Pauline's death and until the termination of the trust, David and his children were entitled to all of the net income of the trust. Upon the termination of David's trust, the trust capital would go to David; if David was not alive, it would go to his children in equal shares *per stirpes*. If David left no children, the trust capital would be divided among George's other children in equal shares *per stirpes*, provided that any capital accruing to either Wendy or Karie would be added to Wendy's trust or Karie's trust, as applicable. The terms of Wendy's trust and Karie's trust were identical to the terms of David's trust, but they substituted Wendy and her children and Karie and her children for David and his children, as applicable.

income of David's trust, Wendy's trust, and Karie's trust for the trusts' 2008, 2009, and 2010 taxation years. Pursuant to subsection 104(2), the minister included all of the income of all three testamentary trusts in the income of the appellant in respect of the appellant's 2008, 2009, and 2010 taxation years.

The issue before the TCC was the meaning to be given to the words "conditioned so that the income thereof accrues or will ultimately accrue to the same beneficiary or group or class of beneficiaries" in paragraph 104(2)(b) and, in particular, whether the determination required by that wording is to be made on an annual basis (the position advanced by the minister) or for the entire life of the trusts in question (the position advanced by the appellant).

Paris J cited *Canada Trustco Mortgage Co. v. Canada* (2005 SCC 54), which sets out the approach to interpreting tax statutes and states that "an instrument dominated by explicit provisions dictating specific consequences" invites a largely textual interpretation. He also cited *Canada v. Quinco Financial Inc.* (2014 FCA 108), in which the FCA reiterated the dominance of "the plain meaning of the text of the Act in the process of interpreting provisions of the Act."

The TCC held that that the inclusion of the wording "or will ultimately accrue" supported the conclusion that the paragraph contemplated the consideration of the right to receive the income of the trust over the trust's entire lifetime. The court also held that there was nothing in the text of paragraph 104(2)(b) that would require the reading in of an annual test.

Furthermore, the court found that no power was given to the minister to re-designate a consolidated trust as multiple trusts in the event that the conditions in paragraph 104(2)(b) were not met in a subsequent taxation year. The court noted that if the test in subsection 104(2) were an annual one, it would be impossible for trustees of such trusts to know whether to file on a consolidated or an unconsolidated basis, thereby creating unpredictable results contrary to the admonition of the SCC in *Canada Trustco*.

Paris J then considered the purpose of subsection 104(2), noting that the parties were in agreement that the provision was intended to prevent income splitting among a number of trusts, each with the same beneficiary or group or class of beneficiaries, in order to take advantage of lower marginal rates in respect of the income of each of the trusts. However, the court, agreeing with the appellant, found that the purpose of subsection 104(2) is to prevent income splitting between trusts that are identical over the entire period of the trusts' existence.

The minister also argued, in the alternative, that the three trusts were still conditioned so that the income accrued or would ultimately accrue to the same beneficiary or group of beneficiaries—namely, George's children and grandchildren. In the minister's view, they were part of the same class of beneficiaries because they were all members of the same family.

The TCC rejected this argument and stated that even if the children and grandchildren of George formed a class, (1) each of the applicable trusts had different children and grandchildren of George as residual income beneficiaries, (2) a different part of the class was named in each trust, and (3) there was no crossover of beneficiaries among the children and grandchildren of George in any of the three trusts. Thus, the court held that the trusts were not conditioned so that the income would ultimately accrue to the same group or class of beneficiaries.

The TCC rejected the minister's argument that the condition in paragraph 104(2)(b) was met if the beneficiaries of each trust were members of the same group or class. Paris J said that this rejection was supported by reference to the language of paragraph 104(2)(b), which refers to "the same group or class" and not to "members of the same group or class"—that is, it refers to beneficiaries within each trust, not to a class of beneficiaries distributed among the different trusts forming part of a common group or class.

On the basis of the foregoing, the appeal was allowed. It is now reasonably clear that for the purposes of subsection 104(2) the beneficiaries of each trust must be considered separately and compared when one is considering whether the test in paragraph 104(2)(b) is met. It is also clear that subsection 104(2) is not a test to be applied on an annual basis.

As a result of the 2016 amendments to the Act, which severely curtail the availability of graduated rates to testamentary trusts, the salience of this provision may well be diminished. Nonetheless, the TCC's decision is a welcome clarification of the law.

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