THE GLOBE AND MAIL

CESTNICK

TAX MATTERS

How to avoid an awkward surprise – an unexpected tax assessment

SPECIAL TO THE GLOBE AND MAIL
PUBLISHED JUNE 30, 2022

The right kind of surprise can be pleasant. I think of the Tooting Library in London, England, which received in the mail a book, A Confederate General From Big Sur, that had been checked out in 1974 and was overdue by 48 years. The borrower, now living in British Columbia, was spared the maximum fine (which would have worked out to about $13). The library was surprised – and pleased – to have the book back.

But not all surprises are pleasant – like an unexpected assessment under Section 160 of our tax law, for instance. Section 160 can make you liable for someone else's taxes if you're not careful. Let me share a few real-life stories to shed light on how this works.

The Law

Section 160 is a tax collection tool that prevents folks who owe taxes from hiding or giving away their assets to avoid the tax collector. If someone transfers property – assets of any kind, really – to another person at a time when the transferor owes taxes, the taxman can chase the recipient (the transferee) for the taxes owing, up to the value of the property transferred. In technical language, our tax law says that "the transferee and transferor are jointly and severally, or solidarily, liable" for the taxes owing.

If the recipient actually pays full value for the property being transferred, then Section 160 won't apply. And for Section 160 to leave a recipient liable, that person has to be one of the following at the time of the transfer: (1) The spouse or common-law partner of the transferor, (2) a person who was under age 18, or (3) a person who was not dealing at arm's length with the transferor (a child, sibling, or even a family trust or corporation, for example).

The Stories

Receiving dividends from a corporation. A decision was handed down by the Federal Court of Appeal on April 14 of this year in the case of Kufsky v. Canada (2022 DTC 5046) that left someone saddled with an unexpected tax bill. The taxpayer, Ms. K, was a shareholder of M Inc., which had unpaid tax debts totalling $68,616. The company then paid Ms. K dividends of $85,000 at the time it owed taxes. The taxman applied Section 160 and assessed Ms. K personally because the dividends paid to her counted as a “transfer” of property. She was on the hook for the full tax bill because the dividends paid were higher than the tax bill owing by M Inc. Ms. K lost her battle in court – which is the usual outcome for most Section 160 cases.

Placing a home in another’s name. In the case De Sanctis-Pedro v. R (2010 DTC 1102), Mr. D, the father of two adult children, owed $69,000 to the taxman. At that time, he sold his home, netted $27,824 of cash proceeds, and bought a condominium which he lived in with his children. He invested the $27,824 in the new condo. But Mr. D also put the condo in the name of the kids – not his own name. The CRA assessed the children for taxes of $27,824 ($13,912 each) because this was considered to be the amount transferred from Mr. D to his children when they were put on title. The kids lost their battle in court. Another common Section 160 scenario is where one spouse transfers the family home to the name of the other or moves the home from joint names into a single name.

Contributing to a spousal RRSP. In the case Wannan v. R (2003 DTC 76), Mr. W owed the taxman $26,333, at which time he contributed more than this amount to a spousal RRSP for his wife, Mrs. W. He then accumulated another $150,608 in tax debts and contributed $7,500 more to the spousal RRSP. Mr. W then declared bankruptcy to get rid of his tax debts. But the taxman still assessed Mrs. W for the total of all amounts contributed to her spousal RRSP while her husband was a tax debtor, since those amounts were considered to be a transfer of property by Mr. W. She lost her case in court.

Inheriting from a deceased person. In the case Biderman v. R (98 DTC 2188), Mrs. B died and her husband, Mr. B, was her executor and he also inherited her assets. Mr. B owed money to the taxman at that time, so he disclaimed his interests as a beneficiary so that his children would inherit Mrs. B’s assets instead. The court ruled that Mr. B’s right to the assets was considered to be property that was transferred to his kids. In the end, the kids were on the hook to pay Mr. B’s taxes.

The moral? If you receive a gift from someone close to you, ask them if they owe the taxman money. This could prevent a nasty surprise later.

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