Mr. Grenon's legendary RRSP and its implications for fund manufacturers

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On July 4, 2025, the Federal Court of Appeal (the Court) released its long-awaited decision in *The RRSP of James T. Grenon by its trustee CIBC Trust Corporation v. His Majesty the King* (*Grenon*). *Grenon* is the first court decision to consider the requirements of the mutual fund trust definition in the *Income Tax Act* (ITA) and its associated requirements in the *Income Tax Regulations* (ITR) and, as such, has implications for both (i) fund manufacturers (as discussed below) and (ii) trustees of registered plans and their administrative agents (as discussed in a separate BLG bulletin).

Requirements to be a "mutual fund trust" for tax purposes

Trusts are the most popular Canadian investment fund vehicle. One of the reasons for their popularity over other forms of fund structures is that units of certain types of trust funds, such as those that are "mutual fund trusts" for tax purposes, are "qualified investments" for registered plans.

A trust will be a "mutual fund trust" for tax purposes at any time, if at that time, certain requirements are met. These requirements include[1]:

1. The trust meets either of two requirements (the Distribution Requirement):
    a. There has been at or before that time a lawful distribution in a province to the public of units of the trust, provided that a prospectus, registration statement or similar document was not required to be filed in respect of the distribution[2]; or
    b. A prospectus, registration statement or similar document has been filed for a class of the units of the trust (and, where required by law, accepted for filing) pursuant to and in accordance with the law of Canada or of any province, and there has been a lawful distribution to the public of units of that class in accordance with that document.[3]
2. In respect of a class of the trust's units that meets the Distribution Requirement, there are at that time at least 150 beneficiaries of the trust, each of whom holds

(i) at least a "block of units"[4] of the class and (ii) units of the class having an aggregate fair market value of at least $500 (the Dispersal Requirement).[5]

Facts in *Grenon*

The Court's decision in *Grenon* involved the appeal by CIBC Trust Corporation as the trustee of Mr. Grenon's registered retirement savings plan (RRSP). As trustee, CIBC Trust Corporation appealed the Tax Court's holding that the units of various trust funds held by Mr. Grenon's RRSP were not qualified investments, that the general anti-avoidance rule (GAAR) applied and that the 2004 to 2008 assessments were not statute-barred. Because the Court agreed with the Tax Court's findings that the trust funds did not satisfy the requirements to be mutual fund trusts, it was not required to, and refrained from considering the GAAR.

Between 2003 and 2009, Mr. Grenon's RRSP paid over $300,000,000 to subscribe for units of certain trust funds that were established and promoted by Mr. Grenon (the Grenon Funds). The saga of how Mr. Grenon's RRSP acquired these investments has become the stuff of legend in the investment fund industry. However, due to the subsequent enactment of the prohibited investment rules applicable to registered plans, we are unlikely to see another similar case. Nevertheless, for the reasons discussed below, the *Grenon* decision is essential reading for fund manufacturers.

Each of the Grenon Funds relied on an exemption from the prospectus requirement under the securities laws of Alberta and British Columbia to distribute their units. Specifically, each Grenon Fund relied on the "offering memorandum exemption" (OME) in either (i) Part 4 of Multilateral Instrument 45-103 *Capital Raising Exemptions* or (ii) Part 2 of National Instrument 45-106 *Prospectus and Registration Exemptions*. The requirements for the OME were as follows:

- Each investor purchases units as principal (and not as agent for someone else);
- Each investor signs an agreement to purchase the securities (such as a subscription agreement);
- Each investor receives a copy of the fund's offering memorandum; and
- Each investor signs a risk acknowledgement form.

The offering memorandum for each Grenon Fund provided that the fund would seek subscriptions from a minimum of 160 investors resident in Alberta or British Columbia, each of whom would subscribe for a minimum of 100 units at a subscription price of $7.50 per unit (the Minimum Subscription). The Minimum Subscription for the distribution was chosen by Mr. Grenon to ensure that each of the Grenon Funds would meet the Dispersal Requirement before the Grenon RRSP would acquire units of the Grenon Funds.

The subscription agreement for each Grenon Fund further provided as follows:

- The investor represented that they were purchasing as principal for their own account, and not for the benefit of any other person;
- The investor represented that they had attained the age of majority and had the legal capacity and competence to execute the subscription agreement; and

- The terms of the subscription agreement could not be modified except by an instrument in writing.

The offering memorandum also provided that following the Mininium Subscription, Mr. Grenon would invest at least $1 million in each of the Grenon Funds. However, when it came time to make his investment, he directed the trustee of the Grenon RRSP to make each of the subscriptions into the Grenon Funds. Before making such investments, the trustee required a copy of the offering memorandum and a legal opinion from a reputable law firm confirming each of the Grenon Funds qualified as a mutual fund trust for tax purposes.

The Tax Court identified one or more deficiencies in approximately 40 per cent of the subscribers for each of the Grenon Funds. Specifically, the investors who acquired units under the offering memorandum included minors and those that did not purchase as principal (such as investors that did not personally sign their subscription agreement and investors that did not personally pay their subscription price). It was those deficiencies that resulted in the Tax Court's finding that the distribution was unlawful.

Learnings from *Grenon*

Distribution Requirement: When is a distribution "lawful"?

The Distribution Requirement mandates that there not only be a distribution of units, but that the distribution is "lawful". The Court held that a distribution is "lawful" if it is completed in compliance with the relevant provincial securities laws. In determining whether the Distribution Requirement was met for the Grenon Funds, the Court looked for compliance with the requirements of the OME, the terms of the offering memorandum and the terms of the subscription agreement.

The Court also acknowledged that not every deviation under securities laws will result in a distribution being unlawful, as "perfect" compliance with securities laws is not required to achieve lawfulness (even if the deviation from securities laws might attract liability or enforcement action).

With respect to the Grenon Funds, the Court noted the offering memoranda indicated that there was to be a Minimum Subscription.[6] The Court took the view that where an offering document establishes a minimum investor requirement, strict adherence to this minimum is critical in order for the distribution to be lawful. As a result, the Court concluded that a **single** distribution under the offering memorandum was only lawful if there were at least 160 separate subscribers whose subscriptions compiled with provincial securities laws (*i.e.,* each of the 160 subscriptions was not viewed as a separate distribution given the minimum investor requirement). Since approximately 40 per cent of the subscribers were found to be non-compliant with one or more of the requirements of the OME, the offering memorandum and/or the subscription agreement, the Court agreed with the Tax Court and held that each of the Grenon Funds failed to meet the Distribution Requirement.

Interaction between the Distribution Requirement and the Dispersal Requirement

The Court confirmed that the Distribution Requirement and the Dispersal Requirement must be interpreted **separately** and not conjunctively, which reversed the Tax Court's decision on the interaction of the two requirements. This is welcome news to the investment funds industry that had long relied on the same interpretation, which had also been previously confirmed by the Canada Revenue Agency in their published administrative positions. In particular, at paragraph 285 of the Court's decision, Monaghan J.A. expressly states:

> "In my view, [the Distribution Requirement] requires a trust to have completed at least one lawful distribution to the public of units of a class of a trust before or at the determination time. While there is no minimum number of persons who must participate, nor a minimum number of units that must be distributed, the distribution must strictly comply with provincial securities laws."

In other words, the Court's decision confirms that once a single lawful distribution to the public has been completed, the Distribution Requirement is satisfied. Furthermore, the Court confirmed that in counting the unitholders for purposes of the Dispersal Requirement, any unitholder may be counted towards the 150 beneficiaries (even if they did not acquire the units under a lawful distribution to the public).

The importance of the Court's conclusion on the Distribution Requirement extends beyond the requirements of the mutual fund trust definition, as the same Distribution Requirement is one of the requirements for a trust to qualify as an "investment fund" for purposes of the loss restriction event rules in the ITA. This definition has become even more important, as meeting the "investment fund" definition in the ITA allows a trust that is not a mutual fund trust to qualify for the new exception for alternative minimum tax. As a result, the *Grenon* decision confirms that a trust needs to only have made a distribution to one member of the "public" before the end of its first calendar year in order to meet the Distribution Requirement for the "investment fund" definition.

Reliance on commercial law for interpreting tax law

The Court reminds taxpayers that in accordance with the modern principle of statutory interpretation, it is important to consider the broader commercial law when interpreting words and expressions that are undefined in the ITA and ITR but have well-defined meanings outside of the tax context.

The *Grenon* decision therefore highlights the importance of the interaction between tax and securities laws for fund manufacturers.

For example, law firms are often engaged to provide trustees of registered plans with opinions on the qualified investment status of securities. When the legal opinions are given for units of a mutual fund trust, the *Grenon* decision cautions investment fund participants that they cannot assume away the securities law compliance which is central to meeting the Distribution Requirement, or rely solely on the confirmations of issuers without taking appropriate due diligence steps to test the reasonableness of such confirmations.

Key takeaways for fund manufacturers

Fund manufacturers with trusts that qualify, or intend to qualify, as mutual fund trusts for tax purposes should consider the following to ensure compliance with the Distribution Requirement:

- Update internal policies and controls regarding the determination of whether a trust meets the Distribution Requirement. These policies and controls should identify the particular distribution of a trust's units that is relied upon for the Distribution Requirement. Once a particular distribution is identified, fund manufacturers should review the subscription(s) under the distribution to ensure compliance with applicable securities laws, the terms of any offering document and the terms of any subscription agreement. Where non-compliance is identified, consideration should be given as to whether the non-compliance is of such a significant deviation that it would cause the distribution to be unlawful.
- Review the conditions and restrictions contained in your offering documents. Where offering documents contain non-essential conditions and restrictions that are applicable to a distribution of units, consider removing such conditions and restrictions (as the failure to strictly comply with them may result in a distribution being considered unlawful).

If you have any questions regarding the impact of *Grenon* on your trust funds, please contact Grace Pereira and Tony Zhang.

Footnotes

[1] The other requirements are that the trust (i) is a "unit trust" (within the meaning of subsection 108(2) of the ITA), (ii) is resident in Canada, and (iii) meets certain restrictions regarding its undertakings.

[2] ITA s. 132(6)(c) and ITR s. 4801(a)(i). For a trust fund that was created before the year 2000, additional requirements must be met.

[3] ITA s. 132(6)(c) and ITR s. 4801(a)(ii).

[4] The term "block of units" is defined in ITR s. 4803(1) to mean **100 units** (if the fair market value of one unit of the class is less than $25), **25 units** (if the fair market value of one unit of the class is $25 or more but less than $100), or **10 units** (if the fair market value of one unit of the class is $100 or more).

[5] ITA s. 132(6)(c) and ITR s. 4801(b).

[6] This was consistent with the securities law form requirements for the offering memorandum. While a minimum number of investors does not need to be specified (in which case the cover page must state "you may be the only purchaser"), the offering memorandum may provide a minimum in which case the offering memorandum must also provide an explanation of how funds would be returned if the minimum was not reached.

By

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