Federal government introduces proposed trust reporting rules

March 17, 2022

What Trustees Need to Know

On February 4, 2022, the Department of Finance re-introduced legislative proposals with respect to the enhanced tax reporting rules for trusts first announced in Budget 2018 (the Draft Rules). The Draft Rules will increase the categories of trusts that are required to file a *T3 Trust Income Tax and Information Return* (the T3 Tax Return), expand the information that must be reported and impose significant penalties for non-compliance. As announced on November 3, 2022, the Draft Rules apply to trusts with taxation years ending on December 31, 2023 or later. This is the second time these rules have been deferred.

Background

Changes to the trust reporting rules were first announced in Budget 2018 to provide the Canada Revenue Agency (the CRA) with more information about trusts and their stakeholders. Although initially intended to apply to the 2021 taxation year, the CRA announced on January 14, 2022 that the implementation would be deferred (see our prior article for more information).

Overview of the Draft Rules

Trusts Required to File a T3 Tax Return

The Draft Rules will require that all express trusts resident in Canada file a T3 Tax Return, with limited exceptions (each referred to as an Excepted Trust):

- Trusts that have been in existence for less than 3 months;
- Trusts that hold assets with a total fair market value (FMV) that does not exceed $50,000 throughout the year, if the only assets held by the trust throughout the year are one or more of
    - money,
    - certain government debt obligations,

- a share, debt obligation or right listed on a designated stock exchange,
- a share of the capital stock of a mutual fund corporation,
- a unit of a mutual fund trust,
- an interest in a related segregated fund, and
- an interest, as a beneficiary under a trust, that is listed on a designated stock exchange;

- Trusts required by rules of professional conduct or by law to hold funds for the purposes of the activity that is regulated under those rules or laws, provided that the trust is not maintained as a separate trust for a particular client or clients;[1]
- Trusts that qualify as non-profit organizations or registered charities;
- Mutual fund trusts, segregated funds and prescribed master trusts;
- A trust, all of the units of which are listed on a designated stock exchange;
- Graduated rate estates;
- Qualified disability trusts;
- Employee life and health trusts;
- Certain government funded trusts;
- Trusts under or governed by a deferred profit sharing plan, pooled registered pension plan, registered disability savings plan, registered education savings plan, registered pension plan, registered retirement income fund or registered retirement savings plan; and
- Cemetery care trusts and trusts governed by eligible funeral arrangements.

Disclosure of Beneficial Ownership

The name, address, date of birth, jurisdiction of residence and taxpayer identification number (social insurance number, business number, etc.) for *each* of the following persons must be disclosed:

- The trustees;
- The beneficiaries and where the beneficiary is not known or ascertainable with reasonable effort, the disclosure must provide "sufficiently detailed information to determine with certainty whether any particular person is a beneficiary of the trust". This can be satisfied by providing a copy of the relevant trust provisions;
- The settlors, which includes any person or partnership that made a loan or transfer of property in any manner to or for the benefit of the trust. The only exception is where (i) the person or partnership was arm's length with the trust at the time of the loan or transfer of property and (ii) either the loan was subject to a reasonable rate of interest or the transfer was for fair market value consideration; and
- Any person that has the ability, through the terms of the trust or a related agreement, to exert influence over trustee decisions regarding the appointment of income or capital of the trust (*e.g.,* a protector of the trust).

Reporting for Bare or Nominee Trusts

A bare trust is an arrangement where one person can reasonably be considered to act as agent for another person (the principal). Such an arrangement usually involves the trustee holding legal title to the trust property and dealing with the trust property in accordance with the principal's instructions. Under the current rules, a bare trust is disregarded and is not required to file a T3 Tax Return.

The Draft Rules provide that a bare trust will be required to file a T3 Tax Return and disclose details about the beneficial ownership of its principal, unless it otherwise qualifies as an Excepted Trust.

Penalty for Non-Compliance

Penalties for non-compliance may be assessed against any person or partnership that:

- Knowingly, or under circumstances amounting to gross negligence, makes a false statement or omission in a T3 Tax Return; or
- Fails to file the T3 Tax Return when required.

The amount of this new penalty is equal to the greater of

- $2,500; and
- 5% of the highest total fair market value of all the property held by the trust at any point during the taxation year.

Effective Date

The Draft Rules will apply to trusts with taxation year ending on December 31, 2022 or later. For trusts with a calendar year-end, the new trust reporting rules apply to the 2022 taxation year.

BLG Can Help

For more information on how the new trust reporting rules may affect your particular trust, reach out to BLG's Tax Group.

[1] For example, lawyers generally have two types of trust accounts: (i) general trust accounts (*i.e.,* a trust account where funds belonging to different clients are pooled together) and (ii) client specific trust accounts (*i.e.,* a separate trust account for a particular client's or clients' trust funds). A T3 Tax Return is required in respect of the latter but not the former.

By

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