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ESTATE AND TRUST PLANNING

New Tax Reporting Obligations for Trusts: UPDATE 2022

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We reported on the enhanced tax reporting obligations for trusts here on February 4, 2021. Since that time, there have been updates to these new rules and their effective date.

Most recently, on November 4, 2022, the government announced that the enhanced tax reporting obligations for trusts will be postponed by one year, such that they will now apply to tax years ending on or after December 31, 2023.

Introduced by the 2018 Federal Budget, these rules were initially set to come into effect for tax years ending on December 31, 2021 and later. The rules generally impose an obligation on most family trusts to file tax returns and disclose details of their trustees, beneficiaries, settlors, and protectors (refer to our 2021 article for a more comprehensive discussion of the rules). Earlier this year the rules were postponed to taxation years ending on December 31, 2022 and later. This second postponement to December 31, 2023 is a welcome relief to trustees and advisers, giving them further time to prepare for compliance obligations.

Draft legislation addressing these enhanced tax reporting obligations was released on February 4, 2022 and August 9, 2022. The legislative proposals released on February 4, 2022 confirmed that application of these obligations would extend to "bare trusts." A bare trust exists where a trustee holds legal title to property, but control over the property is retained by the beneficiary. As they are not technically true trust arrangements, bare trusts have been historically ignored for Canadian income tax purposes (such that the beneficiary is regarded as the owner of the property).

Bare trusts are commonly used as an estate planning tool to reduce the amount of estate administration tax payable on a person's death (by having legal title of, for example, a person's home held by a nominee corporation, the shares of which flow through a secondary Will that need not be probated). Appetite for this type of planning will likely wane due to the administrative cost and burden of the new annual income tax filing requirement.

Bare trusts are used for other purposes too and, in many cases, compliance may be an issue as people may not be aware that certain asset arrangements they have are, in fact, bare trusts.

The Department of Finance describes the purpose of the new enhanced tax reporting obligations as a way to help counter aggressive tax avoidance, tax evasion, and money laundering by enhancing CRA's collection of beneficial ownership information.

Penalties will be imposed on trustees if they fail to comply with the new obligations. Trustees should use this extra year to familiarize themselves with the enhanced reporting rules and gather the required information and/or – where appropriate – consider a trust wind-up.

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