<u>What’s Mine is Yours – Including the Tax Bill</u>

Section 160 of the Income Tax Act is probably one of the most, if not the most, dangerous collection tools available to the Canada Revenue Agency (CRA). If (i) a taxpayer transfers property to his or her spouse, a minor, or anyone with whom he or she does not deal at arm’s length; (ii) the transferee does not pay fair market value consideration for the property; and (iii) the transferor has a tax liability for the year of transfer or any previous year, the transferee will be liable for some or all of the outstanding tax liability.

The transferee’s liability will be the lesser of the transferor’s liability and the shortfall in the consideration paid for the property. For example, if I owed the CRA $50,000 for 2010, and in 2011 I gave my child a property worth $20,000, for which he pays only $10,000, his liability will be limited to the $10,000 shortfall in consideration paid for the property. If my tax liability had been only $7,000, his liability cannot be more than that.

The transferee’s liability does not depend upon knowledge or intention. He may have no idea that I owe taxes. For that matter, I may have no idea. If I transfer a property to my son today, and three years from now CRA assesses me in respect of 2010 and establishes that there was a liability outstanding, Section 160 will fix a joint and several liability on my son, even though the transfer was in good faith and, to our knowledge, there was no tax liability at the time. The tax liability will include any income or capital gain triggered by the disposition of the property.

There is case law to support a Section 160 assessment against the recipient of a dividend from a non-arm’s length company, if the company had outstanding tax liabilities. For those inactive shareholders receiving dividends from family companies, this can be a major concern.

There is also authority for assessing the beneficiaries of an estate who receive a bequest, if the deceased had tax liabilities outstanding.

In a somewhat more rational vein, the Tax Court, in the 1998 decision of *Michaud,* found that payments made by a tax debtor on a mortgage on the family home, even though the home was in the wife’s name, did not constitute a transfer for no consideration. At the conclusion of the judgment, Judge Lamarre Proulx stated:

> *“when the evidence discloses that the payment on the hypothec was made in performing the legal obligation to provide for the family's requirements that it was made for valuable consideration within the meaning of s. 160(1) of the Act."*

The Courts have not been unanimous in their acceptance of the *Michaud* rationale, but neither has there been any clear rejection of this view.

Unlike normal tax liabilities which must be assessed within 3 or 4 years, there is no time limit on Revenue’s ability to assess the transferee. The subsequent bankruptcy of the transferor, which eliminates his or her liability, does not reduce the liability of the transferee. Payments of tax by the transferor are applied first to other tax liabilities and do not necessarily reduce the liability of the transferee.

The Courts have held that the transferee assessed under Section 160 is entitled to challenge the tax assessment of the transferor. Even if the transferor would have been out of time to challenge the assessment, since the CRA is not limited in the time to assess under Section 160, the transferee still has the ability to challenge the assessment.

Clearly, in any contemplated transfer of property, both the transferor and the transferee must have good advice and information.