

Federal Court of Appeal



Cour d'appel fédérale

Date: 20250811

Docket: A-264-23

Citation: 2025 FCA 143

**CORAM: WEBB J.A.
BIRINGER J.A.
DAWSON D.J.C.A.**

BETWEEN:

HIS MAJESTY THE KING

**Appellant/
Respondent on cross-appeal**

and

**VEFGHI HOLDING CORPORATION and
S.O.N.S. ENVIRONMENTAL LTD.**

**Respondents/
Appellants on cross-appeal**

Heard at Vancouver, British Columbia, on March 4, 2025.

Judgment delivered at Ottawa, Ontario, on August 11, 2025.

REASONS FOR JUDGMENT BY:

WEBB J.A.

CONCURRED IN BY:

**BIRINGER J.A.
DAWSON D.J.C.A.**

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REASONS FOR JUDGMENT

WEBB J.A.

[1] This is an appeal and a cross-appeal from the Order of the Tax Court of Canada answering a question that was raised in an application under Rule 58 of the *Tax Court of Canada Rules (General Procedure)*, SOR/90-688a. The question that was posed to the Tax Court was:

Where a trust designates a portion of a taxable dividend (the "Amount") received on a share of the capital stock of a taxable Canadian corporation (the "Issuer"), pursuant to subsection 104(19) of the federal Income Tax Act (the "Act"), such that the Amount is deemed to have been received by a beneficiary (the "Beneficiary"), when is it determined whether the Issuer is connected with the Beneficiary for purposes of paragraph 186(1)(a) of the Act?

[2] The Tax Court Judge provided the following answer (2023 TCC 135):

Where a trust designates a portion of a taxable dividend (the "Amount") received on a share of the capital stock of a taxable Canadian corporation (the "Issuer"), pursuant to subsection 104(19) of the federal Income Tax Act (the "Act"), such that the Amount is deemed to have been received by a beneficiary (the "Beneficiary"), the determination of whether the Issuer is connected with the Beneficiary is made at the time that the taxable dividend was, as a question of fact, received by the trust provided that the Beneficiary is deemed under subsection 104(19) to have received the Amount in the same taxation year as the taxable dividend was, as a question of fact, received by the trust.

However, if the Beneficiary is deemed under subsection 104(19) to have received the Amount in a taxation year that is subsequent to its taxation year in which the taxable dividend was, as a question of fact, received by the trust, then the determination of whether the Issuer is connected with the Beneficiary is made in the subsequent taxation year of the Beneficiary.

[3] The Crown appealed this Order. The Crown's proposed answer to the Rule 58 question was refined between the filing of the notice of appeal and the filing of the Crown's memorandum. The refined response as proposed by the Crown is:

Where a trust designates the Amount pursuant to s. 104(19), such that the Amount is deemed to have been received by the Beneficiary, the determination of whether the Issuer is connected with the Beneficiary for purposes of s. 186(1)(a) is made when the deemed dividend takes effect, being when the Amount is designated by the trust at the end of the particular taxation year of the trust in which the trust received the dividend from the Issuer.

[4] Vefghi Holding Corporation (Vefghi Holding) and S.O.N.S. Environmental Ltd.

(S.O.N.S.) filed a cross-appeal. They also refined their proposed response between the filing of the cross-appeal and the filing of their memorandum. Their refined proposed response is:

Where a trust designates a portion of a taxable dividend (the “Amount”) received on a share of the capital stock of a taxable Canadian corporation (the “Issuer”), pursuant to subsection 104(19) of the federal Income Tax Act (the “Act”), such that the Amount is deemed to have been received by a beneficiary (the “Beneficiary”), the time at which it is to be determined whether the Issuer is connected with the Beneficiary for purposes of paragraph 186(1)(a) of the Act is the time at which the dividend is declared or paid.

Or, alternatively

Where a trust designates a portion of a taxable dividend (the “Amount”) received on a share of the capital stock of a taxable Canadian corporation (the “Issuer”), pursuant to subsection 104(19) of the federal Income Tax Act (the “Act”), such that the Amount is deemed to have been received by a beneficiary (the “Beneficiary”), the time at which it is to be determined whether the Issuer is connected with the Beneficiary for purposes of paragraph 186(1)(a) of the Act is the time at which the dividend is actually received by the trust.

[5] For the reasons that follow, I would allow the appeal with a clarification to the response as proposed by the Crown and dismiss the cross-appeal. In these reasons there are references to a number of provisions of the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) (the Act). The full text of the current version of the provisions that are relevant in answering the Rule 58 question is set out in the Appendix attached to these Reasons. The only provision that was amended after 2014 was paragraph 186(1)(a) of the Act. The amendment only changed the amount set out in paragraph 186(1)(a) of the Act (from 1/3 to 38 1/3%) and therefore does not impact the response to the Rule 58 question.

I. Background

[6] The Rule 58 question arose in the context of the assessments by the Minister of National Revenue (the Minister) of tax under Part IV of the Act on certain deemed dividends received by corporations who were beneficiaries of certain trusts that owned the shares on which dividends were paid by taxable Canadian corporations. The Rule 58 question was premised on the assumption that the corporation paying the dividend was, for the purposes of Part IV of the Act, controlled by the corporation that was deemed to receive the dividends at the time that the dividends were paid to the trust but ceased to be so controlled prior to the trust's year-end.

[7] The parties submitted two separate Agreed Statements of Facts at the Tax Court hearing – one for Vefghi Holding and the other for S.O.N.S.

[8] The following is a summary of the relevant facts for Vefghi Holding:

1. Vefghi Holding was a beneficiary of the Vefghi Family Trust;
2. The Vefghi Family Trust owned all of the issued Class A voting common shares of R. Vefghi Environmental Consultant Inc. (Vefghi Environmental);
3. Rahmatollah Vefghi and Parvin Yavari were the trustees of the Vefghi Family Trust and they also owned all of the issued non-voting preferred shares of Vefghi Environmental and all of the issued shares of Vefghi Holding;

4. The taxation year end for the Vefghi Family Trust and Vefghi Holding was December 31;
5. On July 1, 2015, Vefghi Environmental declared and paid a dividend of \$1,363,283 on the Class A common shares held by the Vefghi Family Trust and the Vefghi Family Trust then sold these shares to a person with whom the Vefghi Family Trust and Vefghi Holding were dealing at arm's length;
6. Vefghi Holding and Vefghi Environmental were taxable Canadian corporations and private corporations for the purposes of the Act;
7. The Vefghi Family Trust declared an income allocation to Vefghi Holding effective July 1, 2015 in the amount of the dividend received by the Vefghi Family Trust from Vefghi Environmental;
8. In filing its tax return for its taxation year ending December 31, 2015, the Vefghi Family Trust designated the amount of \$1,363,283 as a taxable dividend deemed to be received by Vefghi Holding as provided in subsection 104(19) of the Act; and
9. Vefghi Holding included the amount designated by the Vefghi Family Trust as a taxable dividend in filing its tax return for its year ending December 31, 2015.

[9] The following is a summary of the relevant facts for S.O.N.S.:

1. S.O.N.S. was a beneficiary of the Mate Family Trust;

2. The Mate Family Trust owned the majority of the issued non-voting Class B common shares of M&R Environmental Ltd. (M&R);
3. George Mate was the trustee of the Mate Family Trust;
4. George Mate and his spouse owned the majority of the issued voting Class A common shares of M&R and, together with four other related family members, owned all of the issued shares of S.O.N.S.;
5. The taxation year end for the Mate Family Trust was December 31 and for S.O.N.S. was August 31;
6. On June 30, 2015, M&R declared a series of dividends payable on its Class B common shares and the portion of such dividends payable to the Mate Family Trust was \$1,968,500;
7. The dividends were paid on June 30, 2015 by M&R issuing promissory notes;
8. On July 1, 2015, George Mate, his spouse and the Mate Family Trust sold all of their shares of M&R to a person with whom the Mate Family Trust and S.O.N.S. were dealing at arm's length;
9. S.O.N.S. and M&R were taxable Canadian corporations and private corporations for the purposes of the Act;
10. The Mate Family Trust declared an income allocation to S.O.N.S. effective July 1, 2015 in the amount of \$1,967,731;

11. In filing its tax return for its taxation year ending December 31, 2015, the Mate Family Trust designated the amount of \$1,967,731 as a taxable dividend deemed to be received by S.O.N.S. as provided in subsection 104(19) of the Act; and
12. S.O.N.S. included the amount designated by the Mate Family Trust as a taxable dividend in filing its tax return for its taxation year ending August 31, 2015, even though the taxation year of S.O.N.S., in which the taxation year of the Mate Family Trust ended, was the taxation year of S.O.N.S. ending the following year on August 31, 2016.

[10] The Minister reassessed Vefghi Holding for its taxation year ending December 31, 2015, for tax payable under Part IV of the Act on the dividend that it was deemed to receive and reassessed S.O.N.S. for its taxation year ending August 31, 2016 for tax payable under Part IV of the Act on the dividend that it was deemed to receive.

II. Part IV Tax

[11] A dividend received by a corporation resident in Canada is to be included in computing the income of that corporation (subsection 82(1) of the Act). Subsection 112(1) of the Act provides that when a corporation resident in Canada receives a dividend from a taxable Canadian corporation, the recipient corporation is entitled to deduct, in computing its income, an amount equal to such dividend. The net result is that there is no tax under Part I arising as a result of the receipt of this dividend.

[12] However, there will be a refundable tax imposed under Part IV of the Act on a private corporation or a subject corporation that receives a dividend from a corporation with which the recipient corporation is not connected. Although the recipient will pay a tax under Part IV, that recipient will be entitled to a refund of that tax as provided in subsection 129(1) of the Act based on the amount of taxable dividends that such recipient corporation pays.

[13] Generally, two corporations will be connected (and hence no Part IV tax will be payable) if one corporation controls the other corporation or owns more than 10% of the shares with full voting rights and shares having a fair market value of more than 10% of the fair market value of all of the issued shares of the other corporation. Subsection 186(2) of the Act provides that a corporation will control another corporation if more than 50% of its voting shares are held by the other corporation and / or persons with whom the other corporation does not deal at arm's length.

[14] The Tax Court Judge described the purpose of Part IV in paragraph 7 of his reasons:

... The refundable Part IV tax is intended to reduce or eliminate the corporate tax deferral on passive investment income. Its general purpose and operation were explained by Linda Woo and Gavin Friedley in Chapter 9 of the 5th edition of the publication *Taxation of Private Corporations and Their Shareholders* [5th ed. by Richard Gervais et al. (Toronto, Ontario: Canadian Tax Foundation, 2020)] as follows:

Refundable taxes were introduced to eliminate the corporate tax deferral on passive investment income. Under the refundable tax regime, private corporations are required to prepay the tax on their investment income earned; the prepaid tax approximates the amount of tax an individual subject to tax at the highest marginal rate would have paid if she had earned that investment income personally. A portion of the tax is subsequently refunded to the corporation upon the payment of taxable dividends by the corporation to its shareholders. This refundable tax mechanism is

intended to discourage individuals from using a corporation to earn passive investment income to defer tax.

III. Subsection 104(19) of the Act

[15] In the matter that gave rise to the Rule 58 question, a trust was interposed between the corporations that paid the dividends and the corporations that ultimately were deemed to receive dividends as beneficiaries of the trusts. Subsection 104(19) of the Act allows a trust to designate an amount equal to a portion of a taxable dividend that was received by a trust during its taxation year and that was payable by that trust to a particular beneficiary (and therefore would be included in that particular beneficiary's income pursuant to subsection 104(13) of the Act). The amount so designated is deemed to be a taxable dividend received by that beneficiary in that beneficiary's taxation year in which the trust's taxation year ends. The dividend is also, for the purposes of paragraphs 82(1)(b) and 107(1)(c) and (d) and section 112, deemed not to have been received by the trust.

[16] Subsection 104(19) does not specify the day on which the beneficiary is deemed to receive the dividend. Since, for a corporate beneficiary, it is relevant whether it receives the dividend from a corporation with which it was connected, the Rule 58 question was posed.

IV. Decision of the Tax Court

[17] The Tax Court Judge found that the relevant point in time for the purposes of determining whether two corporations are connected for the purposes of Part IV of the Act, is when a dividend is received by a shareholder corporation:

[39] The wording of subsections 186(1) and 186(3) clearly states that Part IV tax is levied on dividends received by a taxpayer. In other words, the tax is levied on dividends *received* by a corporation, not on dividends *paid* by a payer corporation.

[40] Since subsection 186(1) levies the Part IV tax on dividends *received* by the taxpayer, the logical conclusion is that the determination of when two corporations are connected is made at the time that the dividend is received by the corporate taxpayer, although in most instances, the dividend will be paid by the payer corporation at the same time as it is received by the corporation liable for the Part IV tax.

[41] Further, this conclusion is consistent with the purpose of subsection 186(1), which is to only levy the Part IV tax on dividends that the taxpayer receives from payer corporations that it does not control or exercise influence over through its 10% or more holding of the voting shares of the payer corporation--in other words, dividends it receives from shares that it holds, at the time that it receives the dividends, as portfolio investments.

[Emphasis added by the Tax Court Judge.]

[18] The Tax Court Judge then stated, at paragraph 21 of his reasons, that “[i]f the conditions of subsection 104(19) are satisfied, then all or a portion of a taxable dividend received by a trust on a share of the capital stock of a taxable Canadian corporation is deemed, for the purposes of the Act, to be a taxable dividend on the share received by a beneficiary”.

[19] The Tax Court Judge also noted, at paragraph 50 of his reasons, that while the dividend is deemed to be received by the beneficiary in its taxation year in which the trust's taxation year ends, subsection 104(19) of the Act does not specify on what day during that beneficiary's taxation year the beneficiary is deemed to have received that dividend.

[20] The Tax Court Judge concluded that a corporate beneficiary of a trust will be deemed to have received a dividend on the same date that it was received by the trust:

[56] Subsection 104(19) creates the legal fiction that a beneficiary, including a corporate beneficiary, received a dividend on the shares of the payer corporation. The beneficiary is deemed to have received the same dividend as the dividend received by the trust.

[57] As a question of fact, this dividend was received by the trust on a specific date. In my view, unless the legal fiction created by the deeming rule specifically results in the dividend being received at a different point in time, then the dividend is received by a corporate beneficiary on the same date as the date that it was received by the trust. It is at this point in time that one determines, for the purposes of subsection 186(1), whether the relevant corporations are connected.

[21] However, the Mate Family Trust received the dividend from M&R on June 30, 2015, and the taxation year for S.O.N.S. ended on August 31, 2015. Since the Mate Family Trust's taxation year ended on December 31, 2015, the taxation year of S.O.N.S. that included December 31, 2015, ended on August 31, 2016. As a result, the Tax Court Judge adopted the alternate interpretation in paragraph 64 of his reasons that resulted in S.O.N.S. being deemed to have received the dividend from M&R "sometime during its taxation year ending on August 31, 2016".

V. Issue and Standard of Review

[22] The issue in this appeal is when is the determination to be made of whether two corporations are connected for the purposes of Part IV of the Act when a trust is interposed between the corporation paying the dividend and the beneficiary corporation that, as a result of an allocation of income by the trust and a designation under 104(19) of the Act made by the trust, is deemed to have received a dividend on the shares.

[23] This is a question of statutory interpretation and therefore the standard of review is correctness (*Housen v. Nikolaisen*, 2002 SCC 33).

VI. Analysis

[24] The Supreme Court of Canada, in *Canada Trustco Mortgage Co. v. The Queen*, 2005 SCC 54, [2005] 2 S.C.R. 601, set out the approach to be adopted in interpreting statutory provisions:

[10] It has been long established as a matter of statutory interpretation that "the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament": see 65302 *British Columbia Ltd. v. Canada*, [1999] 3 S.C.R. 804, at para. 50. The interpretation of a statutory provision must be made according to a textual, contextual and purposive analysis to find a meaning that is harmonious with the Act as a whole. When the words of a provision are precise and unequivocal, the ordinary meaning of the words play a dominant role in the interpretive process. On the other hand, where the words can support more than one reasonable meaning, the ordinary meaning of the words plays a lesser role. The relative effects of ordinary meaning, context and

purpose on the interpretive process may vary, but in all cases the court must seek to read the provisions of an Act as a harmonious whole.

[25] Subsection 186(1) of the Act imposes Part IV tax on dividends received by a private corporation or a subject corporation on “all assessable dividends received by the particular corporation in the year from corporations other than payer corporations connected with it”.

[26] “Assessable dividend” is defined in subsection 186(3) of the Act as “an amount received by a corporation at a time when it is a private corporation ... as, on account of, in lieu of payment of or in satisfaction of, a taxable dividend from a corporation, to the extent of the amount in respect of the dividend that is deductible under section 112 ... in computing the recipient corporation’s taxable income for the year”.

[27] The definition of assessable dividend makes it clear that the determination of whether a particular dividend is an assessable dividend is to be made when the private corporation receives that dividend.

[28] Subsection 186(4) of the Act provides, in part, that “a payer corporation is connected with a particular corporation at any time in a taxation year ... of the particular corporation if ... the payer corporation is controlled ... by the particular corporation at that time”.

[29] Subsection 186(2) of the Act provides that one corporation will be controlled by another corporation if more than 50% of the voting shares are held by that other corporation and / or by persons who do not deal at arm’s length with that other corporation.

[30] Whether the control test as provided in subsection 186(2) and paragraph 186(4)(a) or the share ownership test as provided in paragraph 186(4)(b) of the Act is applied to determine if two corporations are connected, subsection 186(4) of the Act provides that this test is to be applied at a particular point in time. Subsection 186(4) of the Act does not explicitly link the particular time at which the connected test is to be applied to the time that the dividend is received by a corporate shareholder.

[31] Since Part IV tax is only imposed on assessable dividends received by a private corporation that is not connected to the payor corporation and since the question of whether two corporations are connected is to be applied at a particular time, the logical implication is that the time when the determination is to be made that two corporations are connected is when the private corporation receives the dividend. The Tax Court Judge reached the same conclusion (paragraphs 37 to 41 of his reasons).

[32] The Tax Court Judge also noted, at paragraph 43 of his reasons, that if the dividends would have been paid directly to Vefghi Holding and S.O.N.S. there would have been no Part IV tax.

[33] However, the dividends were not received directly by Vefghi Holding and S.O.N.S. In each case, the dividends were received by a family trust that, at its year end, designated an amount equal to (or almost equal to) the amount of those dividends. In my view, the Tax Court Judge erred in his determination of the implications of the trust designating these amounts as dividends under subsection 104(19) of the Act.

[34] The structure adopted by the taxpayers cannot be ignored. As noted by the Supreme Court in *Shell Canada Ltd v Canada*, [1999] 3 S.C.R. 622, [1999] S.C.J. No. 30, at paragraph 39, “absent a specific provision of the Act to the contrary or a finding that they are a sham, the taxpayer's legal relationships must be respected in tax cases”.

[35] Subsection 104(2) of the Act provides that a trust “shall, for the purposes of this Act ... be deemed to be in respect of the trust property an individual”. Therefore, the respective family trusts were deemed to be individuals with respect to the shares that they held in Vefghi Environmental and M&R.

[36] As an individual, the dividend that each family trust received was not an assessable dividend. Pursuant to subsections 104(13) and 104(19) of the Act, Vefghi Holding and S.O.N.S., as beneficiaries of their respective trusts, had to include in their income the deemed dividends that became payable to them during their respective trusts’ taxation years. These amounts were included in the income of Vefghi Holding and S.O.N.S. for their taxation years in which their respective trusts’ taxation years ended.

[37] Subsection 104(13) of the Act provides for the inclusion of amounts in the income of beneficiaries of a trust and subsection 108(5) of the Act provides that “except as otherwise provided in this Part” any amount included in income of a beneficiary is income from property. Subsection 104(19) of the Act, if the conditions set out in this subsection are satisfied, is a provision that provides otherwise in relation to dividends received by a trust and passed on to its beneficiaries.

[38] The effect of the deeming provision in subsection 104(19) of the Act is at the heart of this appeal. As noted by the Supreme Court of Canada in *R. v. Verrette*, [1978] 2 S.C.R. 838, at page 845, a deeming provision is a statutory fiction:

... A deeming provision is a statutory fiction; as a rule it implicitly admits that a thing is not what it is deemed to be but decrees that for some particular purpose it shall be taken as if it were that thing although it is not or there is doubt as to whether it is. A deeming provision artificially imports into a word or an expression an additional meaning which they would not otherwise convey beside the normal meaning which they retain where they are used; it plays a function of enlargement analogous to the word "includes" in certain definitions; however, "includes" would be logically inappropriate and would sound unreal because of the fictional aspect of the provision....

[39] Since a deeming provision “effectively alters reality, its meaning should be limited to what is clearly expressed” (*La Survivance v. The Queen*, 2006 FCA 129, at paragraph 55).

[40] In the case before us, the Tax Court Judge noted that it is essential to determine what legal fiction is created by a particular deeming provision:

[55] Once it is determined that a deeming provision applies, one must then look at the actual wording of the deeming provision to determine what legal fiction is created. Specifically, one must determine to what extent the created legal fiction changes what, as a question of fact, actually occurred. In making this determination, one must remember that the scope of a deeming provision is limited to what is clearly expressed in the provision.

[41] Having correctly determined that the actual legal fiction created by a deeming provision must be determined, in my view the Tax Court Judge erred in his interpretation of the consequences of the deeming provision in issue. In paragraph 56, he found that subsection

104(19) of the Act deems a beneficiary “to have received the same dividend as the dividend received by the trust”:

[56] Subsection 104(19) creates the legal fiction that a beneficiary, including a corporate beneficiary, received a dividend on the shares of the payer corporation. The beneficiary is deemed to have received the same dividend as the dividend received by the trust.

[42] This conclusion that the beneficiary is deemed to have received the same dividend as the dividend received by the trust led to his conclusion, in the immediately following paragraph in his reasons, that the beneficiary would be deemed to receive the dividend on the same date that the trust received the dividend:

[57] As a question of fact, this dividend was received by the trust on a specific date. In my view, unless the legal fiction created by the deeming rule specifically results in the dividend being received at a different point in time, then the dividend is received by a corporate beneficiary on the same date as the date that it was received by the trust. It is at this point in time that one determines, for the purposes of subsection 186(1), whether the relevant corporations are connected.

[43] Subsection 104(19) provides, in part, as follows:

A portion of a taxable dividend received by a trust, in a particular taxation year of the trust, on a share of the capital stock of a taxable Canadian corporation is ... deemed to be a taxable dividend on the share received by a taxpayer, in the taxpayer’s taxation year in which the particular taxation year ends ... if

(a) an amount equal to that portion

(i) is designated by the trust, in respect of the taxpayer, in the trust’s return of income under this Part for the particular taxation year ...

[44] While subsection 104(19) of the Act deems the amount of the portion of a dividend received by a trust that is designated by the trust to be a taxable dividend on the same share as the share on which the dividend was paid to the trust, it does not deem the dividend to be the same dividend that was received by the trust. The deeming provision is only applicable once the appropriate designation is made by the trust and the other conditions of subsection 104(19) of the Act are satisfied. Subsection 104(19) of the Act does not deem the beneficiary to receive the deemed dividend on the same date that the trust received the dividend. Rather, this subsection stipulates that the deemed dividend is received in the beneficiary's taxation year in which the trust's taxation year ends.

[45] If a taxable dividend is received by a trust and the trust makes the appropriate designation and otherwise satisfies the conditions of subsection 104(19) of the Act, the beneficiary is deemed to receive a taxable dividend from the corporation that paid the dividend. Such dividend will not be income from property. However, if for any reason, a trust does not make the appropriate designation or does not otherwise satisfy the requirements of subsection 104(19) of the Act, even though the amount that was payable by the trust to the beneficiary can be traced to a dividend received by the trust, it will be income from property to that beneficiary.

[46] All of the conditions of subsection 104(19) of the Act, including the designation by the trust of the particular amount, must be satisfied before the corporate beneficiary is deemed to receive a dividend.

[47] The designation cannot be made before the trust's year end. The trust must be resident in Canada throughout the taxation year during which it received the taxable dividend (paragraph 104(19)(c) of the Act). As well, the designation is to be made in the tax return filed by the trust for the particular taxation year in which the dividend is received by the trust.

[48] Although subsection 104(19) of the Act stipulates the taxation year of the beneficiary in which the dividend is deemed to be received, it does not stipulate the particular day on which the deemed dividend is received. Since the designation cannot be made before the end of the trust's taxation year, the last day of the trust's taxation year is the earliest date on which this designation could be made. It is only once the designation is made and the corporate beneficiary is deemed to receive a dividend, that the determination of whether the beneficiary corporation is connected to the corporation that paid the dividend to the trust can be made.

[49] The Tax Court Judge found, at paragraph 65 of his reasons, that the date on which the determination of whether the corporate beneficiary and the payor corporation are connected is the date that the trust received the dividend, provided that this date would be during the corporate beneficiary's taxation year that included the year end of the trust.

[50] However, using the date that the trust received the dividend could conflict with the requirement that the dividend be included in the taxation year of the beneficiary as specified in subsection 104(19) of the Act. This was the case with S.O.N.S. which led the Tax Court Judge to provide two different interpretations. This same conflict would arise if S.O.N.S.' year end was December 30.

[51] Vefghi Holding and S.O.N.S. argued in their memorandum that the Crown's interpretation of subsection 104(19) of the Act that the dividend is deemed to be received on the last day of the trust's taxation year cannot be correct because the trust does not make the required designation until after its year end:

125. The legal reasoning underlying the Appellant's claim that s. 104(19) deems the beneficiary to receive the dividend at the trust's year-end is fundamentally flawed and self-contradictory. The Appellant reasons that, as the conditions in s. 104(19) can be [*sic*] only be met at the end of the trust's taxation year, the deemed dividend does not take effect until that time.

126. First, this assumes that a deeming provision cannot deem an effect to occur earlier than the date on which the conditions of the provision are met. This assumption is unjustified, and the Appellant has not cited any authority for it. Instead, as noted by the Tax Court, "once it is determined that a deeming provision applies, one must then look at the actual wording of the deeming provision to determine what legal fiction is created."

127. Even if the Appellant's assumption was correct, the condition in s. 104(19) that the trust designate the dividend in its tax return *is not satisfied at the year-end of the trust*. This condition is satisfied when the trust files its tax return for the year, the timing of which is in the trustee's control and in practice occurs well after the year-end. Using the Appellant's reasoning, the beneficiary would not be deemed to receive the dividend until the trust files its tax return. If the trust filed its tax return after the end of the beneficiary's year that included the trust's year-end, the Appellant's interpretation would deem the beneficiary to receive the dividend at a time subsequent to the year specified in s. 104(19).

[Emphasis added by Vefghi Holding and S.O.N.S.]

[52] The Crown's proposed response to the Rule 58 question is also ambiguous with respect to the date that is to be used to determine when the beneficiary is deemed to receive the dividend (and hence when the determination of whether the beneficiary corporation is connected to the payer corporation is to be made). Although the Crown argued that the determination is to be made as of the end of the trust's taxation year, the Crown's proposed response to the Rule 58

question stipulates that the time for the determination of whether a beneficiary corporation is connected to a payer corporation is “when the Amount is designated by the trust at the end of the particular taxation year of the trust in which the trust received the dividend from the Issuer”. The reference to “when the Amount is designated by the trust” causes some ambiguity as it could suggest that the Crown is proposing that the date when the designation is made by a trust for a particular taxation year is the date on which the determination of whether a beneficiary corporation is connected to a payer corporation is to be made.

[53] However, finding that the date the trust makes the designation is the relevant date could also lead to a conflict with the wording of subsection 104(19) of the Act, as noted by Vefghi Holding and S.O.N.S. Assume that a dividend is received by a trust (with a December 31 year end) in a particular calendar year. Assume that the taxation year of the corporate beneficiary also ends on December 31. If the trust makes the designation when it files its tax return after December 31, this would be after the taxation year of the corporate beneficiary in which the trust’s taxation year ends. Since subsection 104(19) of the Act specifies that the particular taxation year of the beneficiary in which the dividend will be deemed to be received is the taxation year of the beneficiary in which the trust’s taxation year ends, the date that the trust makes the designation cannot be the relevant date.

[54] As a result, the only date on which the dividend could be deemed to be received by a corporate beneficiary without resulting in a potential conflict between the date of deemed receipt and the stipulation that the dividend is deemed to be received in the taxation year of the beneficiary in which the trust’s taxation year ends, is the last day of the trust’s taxation year.

[55] Vefghi Holding and S.O.N.S. submit that interpreting subsection 104(19) of the Act to mean that the taxable dividend is deemed to be received on the last day of the trust's taxation year would mean that a corporate beneficiary would be denied the deduction under subsection 112(1) of the Act if the payor corporation, following the payment of a dividend to a trust, ceases to be a taxable Canadian corporation before the end of the trust's taxation year. The interpretation of subsection 112(1) of the Act is not in issue in this appeal. The Rule 58 question only focuses on when the determination is to be made regarding whether a corporation paying a dividend and a corporation that is deemed to receive the dividend are connected for the purposes of the Part IV tax.

[56] However, the interaction of subsection 112(1) and 104(19) of the Act would be relevant, for example, if the payor corporation pays a dividend to a trust, the payor corporation is wound up and ceases to exist before the trust's taxation year ends (and hence ceases to be a taxable Canadian corporation), and the trust makes the designation resulting in the dividend being deemed to be received by a corporate beneficiary.

[57] In that event, in determining how subsection 104(19) will apply for the purposes of subsection 112(1) of the Act, the wording of subsection 104(19) of the Act is important:

A portion of a taxable dividend received by a trust, in a particular taxation year of the trust, on a share of the capital stock of a taxable Canadian corporation is, for the purposes of this Act other than Part XIII, deemed to be a taxable dividend on the share received by a taxpayer, in the taxpayer's taxation year in which the particular taxation year ends, ...

[58] The deeming rule only applies if a trust has received a taxable dividend on a share of the capital stock of a taxable Canadian corporation. If such a dividend is received by a trust, the trust makes the appropriate designation for a portion of such dividend, and the other conditions of subsection 104(19) of the Act are satisfied, the beneficiary is deemed to receive a taxable dividend on the same share as the share on which the dividend was received by the trust. Since it is deemed to be a dividend on the share (which must have been a share of the capital stock of a taxable Canadian corporation), the deeming rule would treat that deemed dividend as a dividend on the same share of the taxable Canadian corporation that paid the dividend to the trust, for the purposes of subsection 112(1) of the Act.

[59] Therefore, while subsection 104(19) of the Act affects the timing of the receipt of the deemed dividend by the corporate beneficiary, it does not affect the status of the deemed dividend as a dividend received on the share of the capital stock of a taxable Canadian corporation. However, the timing of the receipt of the deemed dividend is relevant for the purposes of determining if Part IV tax is payable. If, as in the above example, the payor corporation ceases to exist prior to the end of the trust's taxation year in which a dividend is paid to the trust, the corporate beneficiary would not be connected to the payor corporation at the end of the trust's taxation year (as the payor corporation was dissolved before that year end). As a result, Part IV tax would be payable.

[60] Vefghi Holding and S.O.N.S. placed particular emphasis on the purpose of Part IV tax. The purpose of Part IV tax, as found by the Tax Court Judge at paragraph 7 of his reasons, is "to reduce or eliminate the corporate tax deferral on passive investment income". The passive

investment income would be dividend income from corporations that are not connected to the recipient corporation.

[61] Since the dividends were declared and paid by Vefghi Environmental and M&R at a time when the payor corporations and the corporate beneficiaries would have been connected for the purposes of Part IV, if the corporate beneficiaries owned the shares in the payor corporations on which the dividends were paid, the dividends arguably would not have been the passive investment income that is targeted by Part IV tax. However, as noted above, the structure adopted by the taxpayers cannot be ignored and the purpose cannot override the clear language of subsection 104(19) of the Act that the dividend is deemed to be received in the taxation year of the beneficiary in which the trust's taxation year ends.

[62] As noted by the Supreme Court in *Placer Dome Canada Ltd. v. Ontario (Minister of Finance)*, 2006 SCC 20, [2006] 1 S.C.R. 715, at paragraph 23:

The interpretive approach is thus informed by the level of precision and clarity with which a taxing provision is drafted. Where such a provision admits of no ambiguity in its meaning or in its application to the facts, it must simply be applied. Reference to the purpose of the provision "cannot be used to create an unexpressed exception to clear language"...

[63] In this appeal, the dividend was paid to a trust, which is deemed to be an individual. Without the deeming rule in subsection 104(19) of the Act, the corporate beneficiaries would have received income from property and would not have been deemed to receive a dividend. The deeming rule in subsection 104(19) of the Act is clear that the dividend is deemed to be received by the beneficiary (including a corporate beneficiary) in the taxation year of that beneficiary in

which the trust's taxation year ends. The purpose of the Part IV tax provisions cannot override the deeming rule in subsection 104(19) of the Act. This subsection cannot be interpreted to provide a deemed date of receipt of a deemed dividend other than the last day of the trust's taxation year.

[64] Both parties referred to subsection 186(6) of the Act, which applies to partnerships. This subsection is of little assistance in the interpretation of subsection 104(19) of the Act. Paragraph 186(6)(b) of the Act provides that:

each member of a partnership shall be deemed to own at any time that proportion of the number of the shares of each class of the capital stock of a corporation that are property of the partnership at that time that the member's share of all dividends received on those shares by the partnership in its fiscal period that includes that time is of the total of all those dividends.

[65] There is no similar provision applicable to a trust. Since a trust is an individual for the purposes of the Act, a specific deeming rule would be required to deem a beneficiary to own shares held by a trust.

VII. Conclusion

[66] As a result, I substantially agree with the response to the Rule 58 question as proposed by the Crown. However, as noted above, the ambiguity in the Crown's proposed response should be corrected. Since the earliest time the trust could satisfy the condition that it be resident in Canada "throughout the particular taxation year" is when its year end is concluded, the time for the determination should be the end of trust's taxation year.

[67] I would therefore allow the appeal and dismiss the cross-appeal. I would set aside the Order issued by the Tax Court and I would answer the Rule 58 question as follows:

Where the conditions of subsection 104(19) of the Act are satisfied and a trust designates the Amount pursuant to s. 104(19), such that the Amount is deemed to have been a dividend received by the Beneficiary, the determination of whether the Issuer is connected with the Beneficiary for purposes of s. 186(1)(a) is made at the end of the particular taxation year of the trust in which the trust received the dividend from the Issuer.

[68] The parties requested that they be allowed to make submissions on costs. I would allow the Crown to serve and file submissions on costs within fifteen days of the date of the Judgment issued with these reasons, provided that such submissions shall not exceed five pages. I would allow Vefghi Holding and S.O.N.S. to serve and file joint submissions on costs within fifteen days of the date that the submissions of the Crown are served and filed, provided that such submissions shall not exceed five pages. The Crown will have a right to serve and file reply submissions, not exceeding three pages, within seven days of Vefghi Holding and S.O.N.S. serving and filing their joint submissions.

“Wyman W. Webb”
J.A.

“I agree.
Monica Biringer J.A.”

“I agree.
Eleanor R. Dawson D.J.C.A.”

APPENDIX

Relevant Provisions of the *Income Tax Act*

Subsection 104(2)

A trust shall, for the purposes of this Act, and without affecting the liability of the trustee or legal representative for that person's own income tax, be deemed to be in respect of the trust property an individual...

Pour l'application de la présente loi, et sans que l'assujettissement du fiduciaire ou des représentants légaux à leur propre impôt sur le revenu en soit atteint, une fiducie est réputée être un particulier relativement aux biens de la fiducie

Subsection 104(13)

104 (13) There shall be included in computing the income for a particular taxation year of a beneficiary under a trust such of the following amounts as are applicable:

(a) in the case of a trust (other than a trust referred to in paragraph (a) of the definition trust in subsection 108(1)), such part of the amount that, but for subsections (6) and (12), would be the trust's income for the trust's taxation year that ended in the particular year as became payable in the trust's year to the beneficiary;

104 (13) Les montants applicables suivants sont à inclure dans le calcul du revenu du bénéficiaire d'une fiducie pour une année d'imposition donnée :

a) dans le cas d'une fiducie qui n'est pas visée à l'alinéa a) de la définition de fiducie au paragraphe 108(1), la partie du montant qui, si ce n'était les paragraphes (6) et (12), représenterait son revenu pour son année d'imposition s'étant terminée dans l'année donnée, qui est devenue payable au bénéficiaire au cours de l'année de la fiducie;

Subsection 104(19)

104 (19) A portion of a taxable dividend received by a trust, in a particular taxation year of the trust, on a share of the capital stock of a taxable Canadian corporation is, for the purposes of this Act other than Part XIII, deemed to be a taxable dividend on the share received by a taxpayer, in the taxpayer's taxation year in which the particular taxation year ends, and is, for the purposes of paragraphs 82(1)(b) and 107(1)(c) and (d) and section 112, deemed not to have been received by the trust, if

- (a) an amount equal to that portion
 - (i) is designated by the trust, in respect of the taxpayer, in the trust's return of income under this Part for the particular taxation year, and
 - (ii) may reasonably be considered (having regard to all the circumstances including the terms and conditions of the trust) to be part of the amount that, because of paragraph (13)(a), subsection (14) or section 105, was included in computing the income for that taxation year of the taxpayer;
- (b) the taxpayer is in the particular taxation year a beneficiary under the trust;
- (c) the trust is, throughout the particular taxation year, resident in

104 (19) La partie d'un dividende imposable qu'une fiducie reçoit, au cours de son année d'imposition donnée, sur une action du capital-actions d'une société canadienne imposable est réputée, pour l'application de la présente loi, sauf la partie XIII, être un dividende imposable sur l'action reçu par un contribuable au cours de son année d'imposition dans laquelle l'année donnée prend fin, et est réputée, pour l'application des alinéas 82(1)b) et 107(1)c) et d) et de l'article 112, ne pas avoir été reçue par la fiducie, si, à la fois :

- a) une somme égale à cette partie :
 - (i) d'une part, est attribuée au contribuable par la fiducie dans la déclaration de revenu qu'elle produit pour l'année donnée en vertu de la présente partie,
 - (ii) d'autre part, peut raisonnablement être considérée, compte tenu des circonstances, y compris les modalités de l'acte de fiducie, comme faisant partie du montant qui, par l'effet de l'alinéa (13)a), du paragraphe (14) ou de l'article 105, a été inclus dans le calcul du revenu du contribuable pour l'année d'imposition en cause de celui-ci;
- b) le contribuable est bénéficiaire de la fiducie au cours de l'année donnée;
- c) la fiducie réside au Canada tout au long de l'année donnée;

Canada; and

(d) the total of all amounts each of which is an amount designated, under this subsection, by the trust in respect of a beneficiary under the trust in the trust's return of income under this Part for the particular taxation year is not greater than the total of all amounts each of which is the amount of a taxable dividend, received by the trust in the particular taxation year, on a share of the capital stock of a taxable Canadian corporation.

d) le total des sommes représentant chacune une somme que la fiducie a attribuée à l'un de ses bénéficiaires, aux termes du présent paragraphe, dans la déclaration de revenu qu'elle produit pour l'année donnée en vertu de la présente partie n'excède pas le total des sommes dont chacune est un dividende imposable qu'elle a reçu au cours de cette année sur une action du capital-actions d'une société canadienne imposable.

Subsection 108(5)

108 (5) Except as otherwise provided in this Part,

(a) an amount included in computing the income for a taxation year of a beneficiary of a trust under subsection 104(13) or (14) or section 105 shall be deemed to be income of the beneficiary for the year from a property that is an interest in the trust and not from any other source,

...

108 (5) Sauf disposition contraire de la présente partie :

a) un montant inclus, en vertu du paragraphe 104(13) ou (14) ou de l'article 105, dans le calcul du revenu d'un bénéficiaire d'une fiducie pour une année d'imposition est réputé être un revenu que le bénéficiaire a tiré, pour l'année, d'un bien qui constitue une participation dans la fiducie et non un revenu tiré d'une autre source;

[...]

Subsection 112(1)

112 (1) Where a corporation in a taxation year has received a taxable dividend from

112 (1) Lorsqu'une société a reçu, au cours d'une année d'imposition, un dividende imposable :

(a) a taxable Canadian corporation,
or

(b) a corporation resident in Canada
(other than a non-resident-owned
investment corporation or a
corporation exempt from tax under
this Part) and controlled by it,

an amount equal to the dividend may
be deducted from the income of the
receiving corporation for the year for
the purpose of computing its taxable
income.

a) soit d'une société canadienne
imposable;

b) soit d'une société résidant au
Canada (autre qu'une société de
placement appartenant à des non-
résidents et une société exonérée
d'impôt en vertu de la présente
partie) et dont elle a le contrôle,

une somme égale au dividende peut
être déduite du revenu pour l'année
de la société qui le reçoit, dans le
calcul de son revenu imposable.

Subsection 186(1)

Every corporation (in this section
referred to as the "particular
corporation") that is at any time in a
taxation year a private corporation or
a subject corporation shall, on or
before its balance-due day for the
year, pay a tax under this Part for the
year equal to the amount, if any, by
which the total of

(a) 38 1/3% of all assessable
dividends received by the particular
corporation in the year from
corporations other than payer
corporations connected with it

...

Toute société qui est une société
privée ou une société assujettie au
cours d'une année d'imposition est
tenue de payer, au plus tard à la date
d'exigibilité du solde qui lui est
applicable pour l'année, un impôt
pour l'année en vertu de la présente
partie égal à l'excédent éventuel du
total des montants suivants :

a) 38 1/3 % de l'ensemble des
dividendes imposables déterminés
qu'elle a reçus au cours de l'année
de sociétés autres que des sociétés
payantes auxquelles elle est
rattachée;

[...]

Subsection 186(2)

For the purposes of this Part, other than for the purpose of determining whether a corporation is a subject corporation, one corporation is controlled by another corporation if more than 50% of its issued share capital (having full voting rights under all circumstances) belongs to the other corporation, to persons with whom the other corporation does not deal at arm's length, or to the other corporation and persons with whom the other corporation does not deal at arm's length.

Pour l'application de la présente partie, sauf pour ce qui est de déterminer si une société est une société assujettie, une société est contrôlée par une autre société si plus de 50 % des actions émises de son capital-actions (comportant plein droit de vote en toutes circonstances) appartiennent à l'autre société, à des personnes avec lesquelles cette autre société a un lien de dépendance ou à la fois à l'autre société et à des personnes avec lesquelles l'autre société a un lien de dépendance.

Subsection 186(3)

assessable dividend means an amount received by a corporation at a time when it is a private corporation or a subject corporation as, on account of, in lieu of payment of or in satisfaction of, a taxable dividend from a corporation, to the extent of the amount in respect of the dividend that is deductible under section 112, paragraph 113(1)(a), (a.1), (b) or (d) or subsection 113(2) in computing the recipient corporation's taxable income for the year.

dividende imposable déterminé
Somme reçue par une société, à un moment où elle est une société privée ou une société assujettie, au titre ou en paiement intégral ou partiel d'un dividende imposable d'une société, jusqu'à concurrence de la somme relative au dividende qui est déductible en application de l'article 112, des alinéas 113(1)a), a.1), b) ou d) ou du paragraphe 113(2) dans le calcul du revenu imposable pour l'année de la société qui a reçu le dividende.

Subsection 186(4)

For the purposes of this Part, a payer corporation is connected with a

Pour l'application de la présente partie, une société payante est

particular corporation at any time in a taxation year (in this subsection referred to as the “particular year”) of the particular corporation if

(a) the payer corporation is controlled (otherwise than by virtue of a right referred to in paragraph 251(5)(b)) by the particular corporation at that time; or

(b) the particular corporation owned, at that time,

(i) more than 10% of the issued share capital (having full voting rights under all circumstances) of the payer corporation, and

(ii) shares of the capital stock of the payer corporation having a fair market value of more than 10% of the fair market value of all of the issued shares of the capital stock of the payer corporation.

rattachée à une société donnée à un moment donné d’une année d’imposition (appelée l’« année donnée » au présent paragraphe) de cette dernière dans l’un ou l’autre des cas suivants :

a) la société payante est contrôlée (autrement qu’au moyen du droit visé à l’alinéa 251(5)b)) par la société donnée à ce moment;

b) la société donnée a possédé à ce moment :

(i) d’une part, plus de 10 % des actions émises (comportant plein droit de vote en toutes circonstances) du capital-actions de la société payante,

(ii) d’autre part, des actions du capital-actions de la société payante dont la juste valeur marchande est de plus de 10 % de la juste valeur marchande de toutes les actions émises du capital-actions de la société payante.

Subsection 186(6)

For the purposes of this Part,

(a) all amounts received in a fiscal period by a partnership as, on account or in lieu of payment of, or in satisfaction of, taxable dividends shall be deemed to have been received by each member of the partnership in the member’s fiscal period or taxation year in which the

Pour l’application de la présente partie :

a) les montants qu’une société de personnes reçoit au cours d’un exercice au titre de dividendes imposables sont réputés reçus par chaque associé de la société de personnes, à concurrence de sa part, au cours de l’exercice ou de l’année d’imposition de l’associé au cours

partnership's fiscal period ends, to the extent of that member's share thereof; and

(b) each member of a partnership shall be deemed to own at any time that proportion of the number of the shares of each class of the capital stock of a corporation that are property of the partnership at that time that the member's share of all dividends received on those shares by the partnership in its fiscal period that includes that time is of the total of all those dividends.

desquels l'exercice de la société de personnes se termine;

b) chaque associé est réputé propriétaire au moment considéré des actions de chaque catégorie du capital-actions d'une société qui sont des biens de la société de personnes à ce moment proportionnellement à sa part du total des dividendes reçus par la société de personnes sur ces actions au cours de l'exercice de celle-ci qui comprend ce moment.

FEDERAL COURT OF APPEAL

NAMES OF COUNSEL AND SOLICITORS OF RECORD

DOCKET:	A-264-23
STYLE OF CAUSE:	HIS MAJESTY THE KING v. VEFGHI HOLDING CORPORATION and S.O.N.S. ENVIRONMENTAL LTD.
PLACE OF HEARING:	VANCOUVER, BRITISH COLUMBIA
DATE OF HEARING:	MARCH 4, 2025
REASONS FOR JUDGMENT BY:	WEBB J.A.
CONCURRED IN BY:	BIRINGER J.A. DAWSON D.J.C.A.
DATED:	AUGUST 11, 2025

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