

ALLOCATION OF PURCHASE PRICE AND TRANSALTA

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Introduction

The sale of a business usually involves an allocation of the purchase price among the various assets and services sold. The parties to the transaction are free to allocate the purchase price among the assets as long as the allocation is reasonable. If the allocation is not reasonable, Income Tax Act (the “ITA”) section 68 requires a re-allocation.

Often, the sale documents will set out an agreed allocation and require that the buyer and seller file income tax returns based on that allocation. This keeps the tax filings consistent as between the buyer and the seller. If the parties are dealing at arm’s-length, they expect that the Canada Revenue Agency (the “CRA”) will accept the allocation as a reasonable one and not question the allocation under section 68. In this context, the decision of Mr. Justice Miller in *Transalta*² surprised many practitioners. In that decision, the Tax Court varied a purchase price allocation even though the allocation had been arrived at between parties dealing with each other at arm’s length.

The decision in *Transalta* has caused some practitioners to wonder whether there is any sense in having arm’s-length parties continue to have the purchase agreement set out an allocation of the purchase price. Notwithstanding the result in *Transalta*, this will likely continue to be the standard practice. Indeed, while the actual result in *Transalta* may have surprised many, the Tax Court judgment supports the general rule of thumb that courts should give considerable respect to allocations arrived at by arm’s-length parties, provided that the arm’s-length parties have relatively equal bargaining positions and actually had divergent interests as to the allocation in question.

The Tax Court judgment in *Transalta* also deals with the nature of goodwill and gives some guidance as to how to analyze a price allocation for purposes of section 68. Given the paucity of case law under section 68, this is useful. The case is not likely to be the last word on the subject however, as the decision has been appealed to the Federal Court of Appeal.³ Accordingly, the

¹ This paper was presented at the 2011 British Columbia Tax Conference, sponsored by the Canadian Tax Foundation and held in Vancouver on September 26-27, 2011. I would like to thank Craig D. Young, my colleague at Dwyer Tax Lawyers, for his assistance with the preparation of this paper.

² *Transalta Corporation v. The Queen*, 2010 DTC 1241 (T.C.C.). This decision is under appeal to the Federal Court of Appeal.

³ Transalta filed an appeal of the Tax Court’s decision on September 29, 2010. The Minister of National Revenue filed a cross-appeal of the Tax Court’s decision on October 12, 2010. Both parties have submitted

following analysis is subject to what the Federal Court of Appeal may have to say on the matter.

Transalta Facts

Transalta involved the sale of an electrical power transmission business from Transalta Corporation (“**Transalta**”) to Altalink Limited Partnership (“**Altalink**”).

The transmission business was highly regulated by a provincial utilities board (the “**Board**”), which set the rates that could be charged. This rate was tied, in part, to the net regulated book value (the “**NRBV**”) of the assets used in the transmission business. At the time of the sale, Transalta’s book value for accounting purposes was approximately \$640 million and NRBV was approximately \$617 million.

In a sealed bid process, Altalink was the high bidder and went on to negotiate the terms of the purchase. After negotiations, the parties agreed to a global purchase price of just over \$818 million.⁴ The parties allocated approximately \$190 million to goodwill. This was roughly equal to the amount by which the purchase price exceeded the NRBV and working capital of the transmission business.

The Minister reassessed under section 68 of the ITA on the basis that there was no goodwill in a business that cannot set its own rates due to those rates being regulated. Of course, the vendor of the business disputed that allegation.

Goodwill

Before considering how section 68 might apply, Mr. Justice Miller of the Tax Court had to determine whether goodwill was in fact one of the sold assets. If the CRA was correct and there was in fact no sale of goodwill, any allocation to goodwill would have been unreasonable.

In determining whether goodwill existed, the court rejected use of the residual approach to the valuation of goodwill. Under the residual approach, goodwill is measured as the difference between the global purchase price and the value of the “hard” business assets. If a purchaser is willing to pay \$818 million for assets that have a value of only \$628 million, the residual approach holds that the difference must be goodwill.

While the court conceded that the residual approach was a useful method for valuing goodwill once one had determined that goodwill existed, use of the residual approach to prove the existence of goodwill begged the question. Instead, one first had to consider whether goodwill existed as an identifiable asset. In this regard, the court adopted the description of goodwill

their respective factums to the Federal Court of Appeal. On August 2, 2011, Transalta submitted a requisition for hearing. As of September, 6, 2011, no hearing date had been set down.

⁴ Altalink had submitted a bid of \$855 million but that amount was reduced during the negotiations to \$818,150,705. This reduced purchase price was still higher than the other bids that had been submitted as part of the sealed bid process.

articulated by Lord Macnaghten of the English House of Lords.⁵

... What is goodwill? It is a thing very easy to describe, very difficult to define. It is the benefit and advantage of the good name, reputation, and connection of a business. It is the attractive force which brings in custom. It is the one thing which distinguishes an old-established business from a new business at its first start. The goodwill of a business must emanate from a particular centre or source. However widely extended or diffused its influence may be, goodwill is worth nothing unless it has power of attraction sufficient to bring customers home to the source from which it emanates. Goodwill is composed of a variety of elements. It differs in its composition in different trades and in different businesses in the same trade. One element may preponderate here and another element there. To analyze goodwill and split it up into its component parts, to pare it down as the Commissioners desire to do until nothing is left but a dry residuum ingrained in the actual place where the business is carried on while everything else is in the air, seems to me to be as useful for practical purposes as it would be to resolve the human body into various substances of which it is said to be composed. The goodwill of a business is one whole, and in a case like this it must be dealt with as such.

Ultimately, Mr. Justice Miller accepted that goodwill did exist as an asset of the business. It was incorrect to say that no goodwill could exist simply because rates were regulated. The court specifically identified the following as forming part of the goodwill of the business in question.

- (a) Transalta had a skilled employee base.
- (b) The business included a merchant transmission component. Merchant transmission is the non-regulated business of transmission lines crossing certain territories, with capacity sold at unregulated market rates.

The court noted that these factors went directly to the retention and expansion of a profit-producing customer base.⁶ Mr. Justice Miller found that these factors fall squarely within Lord Macnaghten's definition of goodwill and were therefore goodwill of the business.

In contrast, the court decided that the following did not constitute goodwill of the business even though Altalink was willing to purchase the business assets for more than the book value of those assets.

- (a) Transalta argued that Altalink paid a premium for the assets because Altalink's partnership structure would result in more efficient use of provincial tax allowances.⁷ One of the partners of Altalink was a tax-exempt entity. If Altalink received the full tax allowance, the portion of the allowance that would otherwise

⁵ *The Commissioners of Inland Revenue v. Muller and Co.'s Margarine Limited*, [1901] A.C. 217.

⁶ See paragraph 36 of the decision.

⁷ The tax allowance in question was an amount granted by the Alberta government to a utility provider. The grant allows a utility provider to recover taxes it will pay in connection with the utility business.

have been distributed through the partnership to the tax-exempt entity could be distributed to the other partners, thus reducing the tax paid by those partners. The court rejected Transalta's argument on the basis that the tax allowance was an attribute of Altalink and did not constitute goodwill of the transmission business.

- (b) Transalta argued that the purchaser had a more effective overall debt ratio that it could use to its advantage and that this induced the purchaser to pay more for the assets. The court rejected this argument, again concluding that this was an attribute of the purchaser and not goodwill of the transmission business.

It is noteworthy that Mr. Justice Miller considered that a skilled workforce can constitute goodwill. Advisers often make the assumption that a professional practice has no goodwill (or at least no saleable goodwill) because any goodwill is personal to the professional in question. However, that would not necessarily be the case in every situation. As noted by Mr. Justice Miller, assembling a skilled workforce can result in an element of goodwill. If the professional business is not a one-person operation, there may be goodwill that can be sold to a new purchaser. Of course, the purchaser will want to ensure that the skilled workforce is likely to stay on and continue to be part of the business (and that their loyalty is not personal to the professional in question).

Just as it is insufficient to assume goodwill, it is equally insufficient to rely on the residual approach for valuing goodwill. The residual approach begs the question, because it assumes that any premium above the value of hard assets constitutes goodwill. To the extent that the purchaser is paying the premium because the purchaser has a more efficient business structure, that part of the premium represents a motivated purchaser rather than goodwill of the business being sold.

Mr. Justice Miller cited a couple of cases illustrating the above principle.

In the first case,⁸ Canada Post acquired 60 postal trucks for approximately \$34,000 above their trade-in value. The seller of the trucks argued that this difference represented goodwill of its business. The court in that case decided that the difference was simply a premium paid by Canada Post for reasons unique to Canada Post. Canada Post needed the trucks in a hurry in order to fulfill its business obligations, had no other supplier and was forced by circumstances to pay a premium. This was an example of a motivated buyer rather than goodwill of the business.

In the second case,⁹ a day-care operator sold a day-care business that had consistently operated at a loss and that had numerous licencing issues. Given that the business had never made any profit, had no promise for the future and had numerous operational issues, the court concluded that there could not possibly be any goodwill.¹⁰ While the purchaser and the vendor had been

⁸ The Queen v. *Jessiman Brothers Cartage Ltd.*, 78 DTC 6205.

⁹ *R.L. Petersen v Minister of National Revenue*, 88 DTC 1040 (TCC).

¹⁰ Of course, the result might have been different if the business was introducing new technology

operating at arm's-length, there had been no allocation of the purchase price.

In Mr. Justice Miller's view, attributes of the purchaser – such as the motivation of the purchaser or some special need of the purchaser -- do not constitute goodwill associated with the business being acquired. For an allocation to goodwill to stand up in court, the taxpayer will need to be able to point to the specific components that make up the goodwill.

Section 68

Having determined that goodwill existed, Mr. Justice Miller then turned his attention to the value of that goodwill and whether the allocation made to goodwill was reasonable for purposes of ITA section 68.

This analysis involved consideration of only paragraph (a) of section 68, which states as follows.

Where an amount received or receivable from a person can reasonably be regarded as being in part the consideration for the disposition of a particular property of a taxpayer or as being in part consideration for the provision of particular services by a taxpayer,

- (a) the part of the amount that can reasonably be regarded as being the consideration for the disposition shall be deemed to be proceeds of disposition of the particular property irrespective of the form or legal effect of the contract or agreement, and the person to whom the property was disposed of shall be deemed to have acquired it for an amount equal to that part;

Section 68 requires the parties involved in the transaction to make reasonable allocations between the properties that are being purchased and sold. Section 68 deems only that part of the purchase price that can reasonably be regarded as being the consideration for the particular property to be the proceeds of disposition of that property.¹¹ If the parties have not made a reasonable allocation, the unreasonable portion of the allocation can be re-allocated to other assets.

Rather than jumping directly into consideration of the competing valuations, Mr. Justice Miller carefully considered the parameters of section 68. The provision does not require that an allocation be spot on but merely that the allocation be within the range of what is reasonable.¹²

The framing of the issue is important in a case such as this where section 68 of the *Act* is not written in terms of an amount representing FMV, in other words an exact amount, but instead is written in terms of how an amount can

¹¹ If one is dealing only with property, of course. Section 68 can also apply to services and the granting of restrictive covenants.

¹² See paragraph 26 of the decision.

reasonably be regarded. This necessarily implies a range rather than a single definitive amount. For example, when valuers agree on a FMV of goodwill of \$100,000,000, does that mean that \$80,000,000 or \$120,000,000 could not reasonably be regarded as consideration for the goodwill? Not at all. But what if two valuers suggested FMV was \$60,000,000 and \$140,000,000 respectively? Is that now the range within which an amount can reasonably be regarded as consideration for goodwill? Because two reputable valuers have divergent views, is the Court bound to define a reasonable range accordingly? I am not convinced. I only raise this to confirm my view that the concept in section 68 of the *Act* of how to reasonably regard an amount cannot be an inquiry defining one number, and then suggesting anything other than that number is unreasonable. That would make no sense. So, why is this important in framing the issue? Presume I were to find that the range in this case is zero to \$190,000,000. If I framed the question in terms of whether the Minister's reallocation of zero can reasonably be regarded as consideration for goodwill, I would have to answer yes (given the range) and the Appellant would lose. But if I frame the question in terms of whether the arm's length parties' allocation \$190,000,000 could reasonably be regarded as consideration for goodwill, again I would have to answer yes (given the range) and the Appellant would win.

In other words, one has to start by considering whether the parties to the agreement made a reasonable allocation of the purchase price in respect of the asset in question. If they did (if their allocation falls within the reasonable range), one does not proceed any further (even if the CRA's desired allocation is also within the reasonable range for that asset).¹³ Accordingly, it is important that a taxpayer's allocation be within a reasonable range. Being within that range prevents the CRA from re-allocating.

While this initially sounds somewhat like baseball salary arbitration, it is not exactly the same. In baseball salary arbitration, the two sides each pick a position and the arbitrator has to choose one of those positions. In a section 68 matter, it seems that the taxpayer wins as long as the taxpayer is within the reasonable range – even if the CRA is closer to the middle of that range and the taxpayer is more at the edge of the range. While the CRA might win in baseball salary arbitration by being “more reasonable”, this should not be the case in a section 68 analysis (unless the court decides that the taxpayer has gone beyond the bounds of the reasonable range).

Even if the taxpayer's allocation is not reasonable, however, the taxpayer still has an advantage under the approach taken by Mr. Justice Miller. If a range is established and the taxpayer is outside of the range, great weight should nevertheless be given to the valuation established by arm's length parties. The end of the range that is closest to that agreed allocation should govern.¹⁴

Five Principles

Mr. Justice Miller set out five principles for determining whether the allocation of the purchase

¹³ See paragraph 27.

¹⁴ See paragraph 29.

price to an asset is reasonable.¹⁵ I have paraphrased these principles rather than quoting them directly.

The first principle is as follows.

Where there is sham or subterfuge, section 68 is engaged and the Court must determine what a reasonable range is taking into account the nature of the industry, including industry norms, the nature of the asset, the fair market value of the asset, the context of the transaction, the foundation for the allocation made by the CRA and any other relevant factors. If there is sham and the CRA allocation is within the reasonable range, then the CRA position shall govern.

This first principle must be considered *obiter*, as there was no suggestion of sham or subterfuge in *Transalta*. The principle imposes a judicial penalty on the taxpayer, as the taxpayer loses the benefit of the “reasonable range”. Indeed, the CRA position governs if the CRA position falls within the reasonable range – presumably, even if the taxpayer’s position is closer to the reasonable range.

Mr. Justice Miller does not define what is meant by sham or subterfuge. Presumably, since section 68 is specific to allocations, he is referring to some sham or subterfuge having to do with the allocation itself (as opposed to the transaction having been a sham, as there would then presumably have been no sale).

If this first principle is upheld, one can expect that the CRA will seek to find sham or subterfuge as the CRA would then have a considerable advantage in respect of the section 68 analysis.

The second principle applies if there is no sham or subterfuge but there is also no agreed-upon allocation (or the taxpayer is attempting to use some other allocation). This second principle is as follows.

If the parties to the agreement have not agreed to the allocation sought by the taxpayer, the court will determine the range based on the factors referred to in the first principle and the following additional considerations.

- (a) any allocation made in the agreement;
- (b) if there was no allocation in the agreement, the basis for the taxpayer’s allocation.

As part of this principle, Mr. Justice Miller went on to state that the following factors would be taken into account if there was an allocation agreed to by the

¹⁵ See paragraph 47.

parties in the agreement and the taxpayer is using some other allocation.

- (a) Whether the parties were dealing at arm's length.
- (b) The relative equality of the parties' respective bargaining positions.

Again, this principle is *obiter* because there was an allocation between buyer and seller in *Transalta*.

Mr. Justice Miller does not comment on how one deals with the "reasonable range" under this second principle. Presumably, the court would determine the appropriate allocation based on the court's analysis of the evidence.

If a taxpayer were trying to argue for a different allocation than the one made in the purchase agreement, the taxpayer would presumably have a difficult time of it unless the court concluded that the taxpayer was forced into an unreasonable allocation due to some weakness in the bargaining position of that taxpayer. Again, Mr. Justice Miller does not elaborate on this point.

The third principle is as follows.

If the parties are at arm's length, have relatively equal bargaining positions and have agreed on the allocation used by the taxpayer, evidence of *real bargaining* with respect to the allocation in question is *prima facie* proof of the reasonableness of the allocation.

Mr. Justice Miller found that there was no real bargaining between Transalta (as seller) and Altalink (as buyer) on the value of goodwill, so he did not treat the allocation made by them to goodwill as *prima facie* proof in this case.

This third principle generally reflects the understanding of most practitioners except for the reference to "real bargaining" between the parties with respect to the allocation in question. Most practitioners would have assumed that an arm's-length allocation with some evidence of "hard bargaining" would have been accepted as *prima facie* proof of reasonableness without having to show evidence of "real bargaining".

Mr. Justice Miller uses the term "real bargaining" rather than "hard bargaining". This terminology is significant. In *Transalta*, the taxpayer had tried to prove that there was "hard bargaining" between the buyer and the seller by producing summaries of the negotiations. This was to no avail.¹⁶ By "real bargaining", Mr. Justice Miller meant that each party has something to gain or lose by the manner in which the allocation is made. This is determined not on the tone

¹⁶ See paragraph 57, in which Mr. Justice Miller stated as follows: "The Appellant put great emphasis on the concept of "hard bargaining", whatever that might mean. I suppose evidence of considerable back and forth, with strongly worded letters from both sides as to how critical their particular position is on a certain item would constitute hard bargaining; whereas, a concession following a first request may be soft bargaining or indeed no bargaining at all, passive acceptance perhaps.

of the letters exchanged by the parties during negotiations but rather by an objective analysis of the importance of the specific allocation to each party. If the buyer is indifferent to the allocation and the seller has a real interest in making the allocation in a specific manner, Mr. Justice Miller would conclude that there was not real bargaining on that specific allocation. Usually, of course, a buyer and a seller have diametrically opposed interests on price allocations – but this is not always the case. For example, a buyer usually wants a higher allocation to depreciable assets rather than non-depreciable assets whereas a seller will want to keep the allocation to depreciable assets relatively low to avoid recapture of depreciation. However, what if the purchaser is a tax-exempt entity and does not care about depreciation? In that case, there would be no real bargaining on the allocation to depreciable assets because the purchaser would be indifferent to the outcome of that allocation.

This means that the parties to the purchase agreement cannot rely on “strategic bargaining” to justify an allocation. For example, assume that the purchaser is indifferent as to the amount allocated to goodwill but wants certain representations and warranties included in the purchase agreement and the vendor is reluctant to give those representations and warranties. However, the vendor really wants an allocation to goodwill. In this situation, a savvy purchaser could use the allocation to goodwill as a bargaining chip. The purchaser could agree to the vendor’s allocation to goodwill in exchange for the inclusion of the contentious representations and warranties. Based on his comments in *Transalta*, Mr. Justice Miller would conclude that there was not real bargaining as to the allocation to goodwill. There was certainly strategic bargaining, but the important consideration for Mr. Justice Miller would be the purchaser’s indifference to the goodwill allocation. In this situation, arguing that there was “hard bargaining” might boomerang as it might drive home the fact that one party was indifferent as to the allocation of goodwill.

Of course, it is not uncommon for a party to a transaction can give up on one item in order to win on another item. This should not preclude real bargaining from taking place as long as that party had some interest in the item that was given up. If the party was indifferent to giving up on that item, this would be an indication of no real bargaining. If the party lost something when giving up, that would presumably be an indication of real bargaining.

In order to show real bargaining, one will have to evaluate the position of the other party to the transaction in order to determine that the other party is not indifferent as to the allocation. This will not only help in the negotiations – on the “know thy enemy” principle – but should also help to judge the risk of any reallocation under section 68. If any notes are prepared on your client’s evaluation of the bargaining position of the other side, it may be useful to retain those notes in case there is a later need to evaluate whether real bargaining occurred.

Mr. Justice Miller then went to his fourth principle.

If the third principle applies and the allocation between the arm’s-length buyer and seller is treated as *prima facie* proof of the reasonableness of the allocation, the CRA can challenge the reasonableness of the allocation only by proving a *fundamental mistake* in the foundation of the parties’ agreement. A difference of opinion is not sufficient.

Again, the fourth principle is *obiter* because of Mr. Justice Miller's factual finding that there was no real bargaining as to the value of goodwill in the *Transalta* situation. However, taxpayers who can come within the third principle will be pleased by this fourth principle, which puts a fairly heavy burden on the CRA if it wants to challenge the allocation.

Of course, this burden makes it more likely that the CRA would seek to displace the third principle by alleging that there was no real bargaining as to the allocation of value to the specific asset in question. Presumably, it will be up to the taxpayer to refute this allegation by showing evidence of real bargaining.

The fundamental mistake has to be in the "foundation of the parties' agreement". Presumably, this refers to the agreement on allocation. But what is part of that foundation? If the allocation is *prima facie* proof of a reasonable allocation, the allocation is presumably also *prima facie* proof of what is within the reasonable range. Presumably, the CRA would have to do more than just point to a valuation disagreement, as that would be a mere difference of opinion.

Mr. Justice Miller did not give any examples of a "fundamental mistake". However, what if Mr. Justice Miller had concluded that real bargaining had taken place in respect of the goodwill allocation? Would he have found a fundamental mistake based on *Transalta's* argument that attempted to include attributes of the purchaser (the use of the tax allowance and the leverage) as part of the goodwill of the business? Presumably, mistake as to the nature of what was being sold could constitute a fundamental mistake in the foundation of the allocation agreement. However, that may merely mean that the parties thought that the elements that were actually part of goodwill were worth more (in which case there might not have been a fundamental mistake).

Because of this fundamental mistake notion, a taxpayer may have to be careful about the arguments used to support the value of goodwill. Throwing everything at the wall to see what might stick could backfire, as it may allow the court to conclude that there was a fundamental mistake as to what constituted goodwill.

Finally, we come to the fifth principle.

If the taxpayer fails to come within the third principle, the Court must determine the reasonable range. If there is an agreed allocation between the parties to the agreement and the parties dealt at arm's length, the amount within the court-determined "reasonable range" that is closest to the parties agreed allocation shall be the reallocated amount for the purposes of section 68.

In determining the reasonable range, Mr. Justice Miller indicated that a court should consider the following five factors when determining the "reasonable range".

- (i) The nature of the asset.
- (ii) The nature of the industry, including industry norms.

- (iii) The context of the transaction.
- (iv) The fair market value of the asset.
- (v) Any other relevant factors.

Based on these five principles, it will continue to make sense for arm's-length taxpayers to agree to an allocation. Even if there is no "real bargaining" (or the taxpayer cannot prove real bargaining), the taxpayer still has the benefit of having the allocation made on the taxpayer's end of the reasonable range.

While Mr. Justice Miller does not use numerical examples to illustrate this last principle, assume that the reasonable range was \$100,000 to \$125,000, that the CRA was arguing for an allocation of \$100,000 and that the taxpayer had allocated \$190,000 to the asset in question. In this case, it seems that the court would decide on an allocation of \$125,000 rather than \$100,000 (the CRA position) or \$112,500 (the mid-point of the range) because the high end of the range is closer to the allocation negotiated by the parties to the transaction.

Mr. Justice Miller did not clarify why the court should fix the allocation at the taxpayer's end of the reasonable range if there was in fact no real bargaining on that issue. This conclusion seems to go back to his view that it is the taxpayer's allocation that is being challenged and that the taxpayer's allocation should stand except to the extent that it is shown to fall outside the reasonable range. It will be interesting to see if this principle survives the appeal of his decision.

Application of the Five Principles in *Transalta*

As noted, principles 1 and 2 did not apply in *Transalta*. The Court applied principles 3 through 5.

With regard to principle 3, Mr. Justice Miller concluded that the buyer and seller dealt at arm's length and had relatively equal bargaining positions. However, Mr. Justice Miller concluded that there had been no real bargaining in respect of the allocation to goodwill because the purchaser was indifferent whether any amount was allocated to goodwill. He based this conclusion on his perception of the situation rather than on any evidence from the purchaser.

Mr. Justice Miller rendered his decision based on the fifth principle. The court determined a range of value for the goodwill that the court had found to exist. This goodwill did not include certain items that were actually attributes of the purchaser. Given that *Transalta* had argued that those purchaser attributes had been part of the goodwill of the business, it is perhaps not surprising that Mr. Justice Miller decided that the range of value applicable to the goodwill was less than the amount allocated in the sale agreement. Since there was an agreed allocation between arm's length parties, however, he selected the end of the range that was closest to that agreed allocation. In the result, he reduced the goodwill value by \$50 million and allocated that difference to the tangible assets.

Conclusion

In most cases, arm's-length parties will have competing interests in how the purchase price is allocated among the various assets. In these situations, the parties will continue to be able to rely on agreed allocations when filing income tax returns. Arriving at a mutually agreed-upon allocation of the purchase price will make that allocation *prima facie* proof of the value. The CRA will be able to challenge that *prima facie* proof only if the CRA can point to some fundamental mistake. A fundamental mistake could be present, however, if the parties did not properly understand what was being bought and sold.

If the transaction involves a special or highly motivated purchaser or seller, that party might not have anything to gain or lose in how the purchase price is allocated to a specific asset. In that case, there may not be any real bargaining on the allocation of the purchase price to that specific asset. Even in that case, however (assuming no sham or subterfuge), the other party would still be well advised to include an allocation of the purchase price in the agreement. Even if there was no real bargaining on the point, any reallocation under section 68 is more likely to end up on the end of the range that is more favorable to the taxpayer.