Your file

Our file [redacted]

Robin J. MacKnight
Wilson Vukelich LLP
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OCT 2 2 2012

October 16, 2012

Dear Mr. MacKnight:

Re: Donation of private company flow-through shares

We are writing in response to your letter dated July 4, 2012 concerning the donation of shares that are issued to investors, pursuant to a flow-through share agreement, by a resource company that is a "private corporation" as defined in subsection 89(1) of the *Income Tax Act* (the "Act").

In your letter, you describe a situation where each issued share would qualify as a "flow-through share" ("FTS") under subsection 66(15) of the Act. The issuance of the FTS would be part of a "gifting arrangement" which will be registered as a "tax shelter" as these terms are defined in subsection 237.1(1) of the Act. In addition, you advise that each FTS will be capital property to the investors and would not be a "non-qualifying security" as defined in subsection 118.1(18) of the Act. Immediately after the income tax benefits relating to the renunciation of qualifying resource expenses by the resource company are realized, each investor may donate the FTS to a registered charity.

You note that, pursuant to the proposed split-receipting legislation, a donor of such FTS would, in effect, not benefit from any donation incentives, that normally arise from a donation of property to a registered charity. In your view, proposed subsection 248(35) of the Act would apply, with the result that the cost of the donated FTS (which is deemed to be nil by virtue of subsection 66.3(3) of the Act) would become their fair market value ("FMV") for the purpose of determining the eligible amount of the gift. By contrast, a donation by a taxpayer of publicly-listed FTS would be exempt from this proposed rule and therefore the donor would generally qualify for donation incentives. From a tax policy perspective, you suggest that, the actual cost to the taxpayer of the private company FTS without regard to any deeming provisions should be used for purposes of determining the donation incentives.

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Our Comments

Under the proposed split-receipting legislation, only the eligible amount of a gift will qualify for purposes of the donation incentives. Proposed subsection 248(31) of the Act defines the eligible amount of a gift as the amount by which the FMV of the property that is the subject of the gift exceeds the amount of the advantage, if any, in respect of the gift. Proposed subsection 248(35) of the Act generally provides that for the purposes of proposed subsections 248(31), 110.1(2.1) and (3) and 118.1(5.4) and (6) and paragraph 69(1)(b) of the Act, the FMV of a property that is the subject of a gift is deemed to be the lesser of the FMV of the property otherwise determined and the cost, or in the case of capital property, the adjusted cost base ("ACB"), or in the case of a life insurance policy in respect of which the taxpayer is a policyholder, the adjusted cost basis, of the property immediately before the gift is made.

Proposed subsection 248(37) of the Act provides exceptions to the application of proposed subsection 248(35) of the Act. In particular, proposed paragraph 248(37)(d) of the Act provides an exception in respect of property to which paragraph 38(a.1) or (a.2) of the Act applies. Under paragraph 38(a.1) of the Act, an exemption from income tax is provided for capital gains that arise on the donation of certain property, including shares listed on a designated stock exchange, to a qualified donee.

In the situation described, where neither paragraph 38(a.1) nor (a.2) of the Act is applicable, proposed paragraph 248(37)(d) of the Act would not apply to the donation of private company FTS. Assuming that none of the other exceptions in proposed subsection 248(37) of the Act apply, proposed subsection 248(35) of the Act would apply to deem the FMV of such FTS to be the lesser of their FMV otherwise determined and their cost or ACB, whichever is applicable. Since subsection 66.3(3) of the Act deems a taxpayer, who acquired a FTS pursuant to a FTS agreement with a resource company, to have acquired that share at a cost of nil for tax purposes, such amount would be the deemed FMV of the FTS under proposed 248(35) of the Act. As a result, the eligible amount of the gift in respect of the FTS would be nil for tax purposes.

However, it should be noted that since proposed subsection 248(35) of the Act also applies for the purposes of paragraph 69(1)(b) of the Act, the taxpayer's deemed proceeds of disposition of the FTS would also be nil. Therefore, while a taxpayer in the situation described may not be able to claim a charitable donations tax credit in respect of the donation of the FTS, the taxpayer will also not realize a gain on the disposition thereof. We note that whether a gain on the disposition of a property is on account of income or on account of capital is a generally a question of fact that can only be determined on a case-by-case basis.

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The Canada Revenue Agency is responsible for administering the income tax legislation as enacted by Parliament. In our view, a legislative amendment would be required to provide for the cost or ACB of a donated private company FTS to be its actual cost without regard to any deeming provisions. The primary responsibility for tax policy and legislation rests with the Department of Finance. Accordingly, a request for such an amendment would need to be made to the Department of Finance.

We trust these comments will be of assistance.

Yours truly,

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