# HARD TO KILL – Donation Deals Live On*

By: David Louis, J.D., C.A., Tax Partner, Minden Gross

*(*This release is based on an article published in Tax Notes, No. 492, January 2004, CCH Canadian Limited)*

For some, year-end is the time to give and receive. For others, it's exciting holiday movies. But to tax drones last month it was a bit of everything. Courtesy of often-aggressive donation deals, clients could take more than they gave; and last minute tax changes in the area created more suspense than a Steven Segal cliffhanger (actually, a lot more).

In fact the charity game had been heating up for some time. Early on, the deals got the attention of promoters because the tax shelter rules - which force government registration of high write-off deals - did not apply to charitable donation credits (as opposed to tax *deductions* which are available to corporations). But the feverish activity didn't escape Ottawa's eye: last winter's federal budget extended the tax shelter reporting rules to donation credits and announced anti-avoidance rules pertaining to limited recourse financing. By this time, though, promoters were committed to their deals, which were hastily revamped to cope with the new rules. Although some structures took the position that the tax shelter rules didn't apply because they were dependent on a "representation" in the strict (contractual) sense, most registered their deals as tax shelters. Ironically, most promoters figured that since they were now on file with CanRev anyway, they might as well peddle their wares to corporate donors, to which the tax shelter rules potentially applied all along.

## Above the Law?

So as the year went on, there were more and more signs that the volume of deals was ramping-up. Unlike earlier generations of tax deals, details of the new deals, including tax opinions - even glitzy presentations - could now be readily accessed on the net. And it was hard to turn on talk radio without listening to some pitch or other about how these schemes were feeding the hungry, educating the needy, or providing medical supplies to third world countries. Of course, listeners were also reminded that prospective donors who embraced such lofty ideals would have the added incentive of a big fat tax refund in their pocket.

Some of the deals were quite simple: donors would buy in at a low price and receive a donation receipt many times the amount – with tax coverage more than sufficient to cover associated capital gains tax on the donation. Others were more sophisticated. For example, one variation involved a cash donation funded by a loan; the individual also bought an investment initially worth only a portion of the associated loan, but which could later be anteed-up to repay it. In some structures, the investment pot might be enlarged by a contribution of a third party, with the borrower being able to draw the funds out. The tax opinions invariably given on these sort of deals made much of deficiencies in the drafting of provisions from the year before**[i]** which were designed to reduce the amount of the donation by the amount of benefit or advantage that came with the deal.**[ii]**

## Under Siege

On the morning of December 8th, though, people returning to their offices after the week-end got a rather nasty surprise, in the form of a last-minute press release. As most readers are aware, the release was aimed at the buy-low-donate-high schemes. As of 6:00 p.m. on December 5th, the value of property for charitable donation purposes would be limited to a donor's cost of property, where it is donated within three years of acquisition, or is otherwise acquired through a "gifting arrangement"**[iii]**, or it is reasonable to conclude that the taxpayer expected to make a donation.**[iv]**

It looks like the government was successful in attacking this type of scheme. Several websites I had been following announced that they were no longer open for business.

The release also announced other rules for more sophisticated structures. They expanded the application of a benefit (i.e., reducing the amount of the donation) to amounts that *are in any way related* to the gift. In addition, the release gave formal rules in respect of limited recourse debt associated with a donation scheme, as originally announced in the February 2003 federal budget.

Actually these announcements were just the latest in what is now a long series of anti-avoidance rules, including the restriction of the "$1,000 threshold" for personal-use property which is part of a donation arrangement,**[v]** the December 20, 2002 announcements reducing donations based on associated benefits, and the 2003 federal budget provisions. In addition, the CCRA has issued several "warning" releases concerning donation schemes, including late last year and the year before.

Although the press was generally favourable to the December announcement, not all commentators were sympathetic: just days after the announcement, an article appeared in the *Globe and Mail* chastising the government's apparent heartlessness.**[vi]** Claiming that its action halts the delivery food and supplies to the third world, it ignored the fact that a lot more could be done if government dough didn't go into the pockets of well-heeled taxpayers.

After this, many readers probably went on their holiday vacations with the assumption that these schemes were now gone for good. But just a few days after the government's announcement, I started receiving phone calls on behalf of some promoters - that their tax shelter had either survived the government onslaught, or had hastily been tweaked - with the first set of revised opinions crossing my desk by the end of the week.**[vii]**

As you read this column, rest assured that the promoters whose buy-low-donate-high schemes were plugged are hastily revamping the schemes so that they follow the "structured" approach, and are no doubt pouring over the midnight oil to replicate the structures that (arguably, at least) survived the December press release.

## On Deadly Ground

But throughout the piece, tax colleagues who I consider to be knowledgeable have been reluctant to get their clients into these deals. For one thing, the consensus is that it is a virtual certainty that most deals will be looked at and probably attacked on some grounds or other. In fact, any self-respecting deal now includes a defence fund of half a million bucks or so, to go 12 rounds with the CCRA. But between now and then, even if the defence fund is taking care of business, participants can look forward to notices of reassessment with hefty interest charges and perhaps even penalties, as has been the case with the 10,000 or so art deal donations currently under scrutiny. And, at the end of the day, the defence fund does not guarantee success.

On the other hand, if duking it out is your cup of tea, and besides, nothing's in your name anyway, maybe this sort of thing could have allure.

## Out for Justice

While there have been plenty of art donations and the like that have hit the courts,**[viii]** I am not aware of a "structured" donation deal that has ended up in a tax court, and my personal feeling is that judges will not be overly sympathetic to these structures. Some of the issues that will no doubt be tackled include whether a third party who has enriched the donor has conferred a benefit, or, on the other hand, has received an equivalent amount in return.**[ix]** The government might also attack on lack of donative intent, under GAAR, and so on.

While it's tough to foretell how this will ultimately turn out, a safer prediction is that there'll be lots of deals in 2004 - and pitch battles with the CCRA sure to follow.

***The author wishes to thank Daniel Sandler, Faculty of Law, The University of Western Ontario, Associated with Minden Gross LLP.***

---

**[i]** December 20th, 2002.

**[ii]** For a fascinating article on charitable donations and the history of tax shelters in general, see Tax Shelters – Past, Present and Future" by Graham Turner, *Tax Topics,* No. 1654, November 20, 2003.

**[iii]** Per section 237.1.

**[iv]** See proposed subsections 248(35) and (36). Also included is an anti-avoidance rule (proposed subsection 248(37)) directed at transactions designed to increase the deemed value of a gift.

[v] The threshold does not apply where it is reasonable to conclude that the acquisition of the property relates to an arrangement, plan or scheme that is promoted by another person under which it is reasonable to conclude that the property will be donated.

[vi] "Hands off the helping hand", Marilou McPhedran and Gardner Church, December 17, p. 23.

[vii] One approach is knocking out contractual arrangements that would have plugged investors into various anti-avoidance rules and instead, using the "trust me" approach.

[viii] The challenge of some major mass-marketed art deals – which included arm's length valuations – is scheduled to be heard by the Tax Court some time this month.

[ix] No doubt, the CCRA will be using hindsight on this sort of issue.