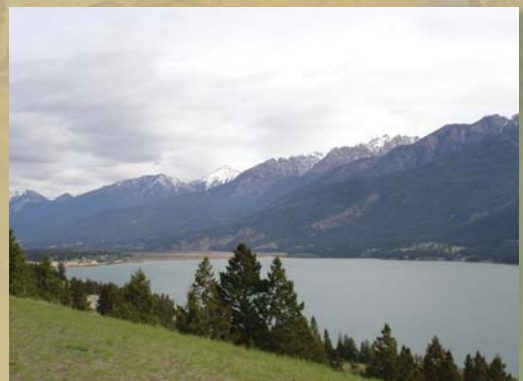


The ECOLOGICAL GIFTS PROGRAM

Retaining the Right to Use Land Donated as an Ecological Gift

Life Interests and Licences

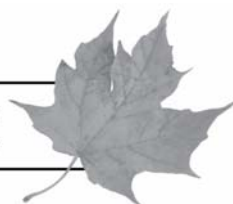
Usufruct, Right of Use, Superficies and Permission Agreements



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INTRODUCTION

THIS FACT SHEET provides information in brief, simplified terms about options for donating land as an ecological gift while retaining the right to continue to live on or use the land. It explains the difference between a life interest in land and a licence to use land in common law jurisdictions and the difference between the rights of use, usufruct and superficies and a permission agreement to use an immovable property in Quebec. It reviews the income tax implications of each.

The discussion in this fact sheet is brief and simplified. The rules governing land and the tax implications of gifts of land are complex. The legal and tax implications of any transaction depend on the circumstances of the transaction as a whole and on the landowner's individual circumstances. Donors and recipients proposing to engage in the kinds of transactions discussed in this fact sheet should each obtain independent legal and tax advice before completing any transaction.

THE CONCEPT OF REAL/IMMOVABLE PROPERTY

Understanding the concept of real or immovable property (land) is central to understanding the notion of life interests in land and the right to use land that has been given away. A brief explanation of the concept of real property in common law jurisdictions of Canada (the territories and all provinces except Quebec) and immovable property in the province of Quebec is necessary to understand the options available for retaining the right to use donated land.

Real property in common law jurisdictions

In common law jurisdictions of Canada (the territories and all provinces except Quebec), a person who owns land does not own the land itself. Rather, a landowner owns an estate (or interest) in land. The land itself is owned by the Crown.¹ Estates are classified according to the time the estate lasts. Two freehold² estates exist in Canada today—the fee simple estate and the life estate. The fee simple estate and the life estate are interests in land.

The fee simple is the largest estate and the one generally associated with ownership of land. The

owner of the fee simple has the unconditional power to dispose of the property during his or her life and to pass it on to his or her heirs. There is no limit on or end to a fee simple estate.

Historically, the fee simple estate was created by words of grant: "I grant the land to X and his heirs." The words "and his heirs" were essential, although this has been altered by statute.

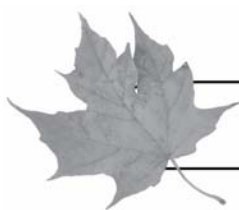
The concept of estates in land makes possible the fragmentation of ownership among different persons. The fee simple estate consists of a "bundle of rights." The owner of the fee simple estate in land has the right to:

- sell, mortgage, lease or will the estate;
- use and occupy the land to the exclusion of others; and



¹ Subject to unextinguished Aboriginal rights and title.

² As distinct from leasehold estates. A freehold estate is a right of title to land. A leasehold estate is an interest in real property held under a lease.



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- give away some of the rights that are connected to the fee simple estate, for example, by granting an easement, covenant or servitude.

As explained above, the fee simple estate may also be divided into smaller estates, such as life estates.

Immovable property in Quebec

The nature of ownership of immovable property in the province of Quebec was imported from French civil law and today is defined in the *Civil Code of Québec* (C.C.Q.):

Ownership is the right to use [usus], enjoy [fructus] and dispose [abusus] of property fully and freely, subject to the limits and conditions for doing so determined by law (section 947).

The right of ownership is a principal real right (similar to fee simple ownership). It is complete, exclusive, perpetual and absolute, subject to the “limits and conditions” referred to in section 947. In fact, many legislative restrictions today minimize the rights of property owners.

Under civil law, “ownership may be in various modes and dismemberments” (947(2) C.C.Q.). “Modes” refers to a particular way of being an owner or of exercising a right of ownership. The principal modes of ownership are co-ownership and superficies (1009 C.C.Q.). “Dismemberment” occurs when the three elements of the right of ownership (the rights to use, enjoy and dispose of property fully and freely) are not held by a single person. Usufruct and right of use are kinds of dismemberments (1119 C.C.Q.).

Usufruct and right of use both refer to the right to use and enjoy property owned by another. A landowner could give land away and retain a right of use or usufruct for his or her lifetime. The interest given away is bare ownership of the land. Under both Quebec and federal tax legislation, giving away land and reserving a right of use and usufruct is deemed to create a trust rather than an outright transfer of property in favour of the recipient. As a result, a gift of bare ownership of land with a reservation of a right of use or usufruct does not qualify as an ecological gift.

Proposed amendments to section 248 of the *Income Tax Act* change the presumption that a trust is created with respect to ecological gifts of the bare ownership of land. If the proposed subsection 248(3.1) is adopted, a gift of the bare ownership of land with a reserved usufruct or right of use could qualify as an ecological

gift and give rise to a tax credit. The new rules apply to dispositions made after July 18, 2005.

Because of these proposed changes, usufruct and right of use, together with superficies, are discussed in greater detail in this fact sheet. However, the discussion of usufruct and use assumes the proposed amendments will be adopted.

RIGHTS TO USE DONATED PROPERTY

Several options exist by which donors can retain the right to use land that has been donated as an ecological gift. As explained below, some of these options create an interest in or right of ownership of land. Others are personal rights negotiated between parties. An interest in land or right of ownership of land generally attaches to the land and binds future owners of the land while personal rights do not.

In common law jurisdictions, a donor can give away land but retain a life interest, the right to live on it for life or the right for someone else to live on the land for life. In Quebec, a number of options for retaining real rights in land donated for conservation purposes are available to donors. Donors who give away land can retain a usufruct, right of use or superficies, each of which allows ongoing use of the donated land.

Life estates and remainder interests

A life estate or life interest exists only for the life of a specified person, either the life of the person to whom it is granted, known as the life tenant, or the life of some other person (called an estate *pur autre vie*). Life estates may be created by deed, lease or will (conventional life estates) or by statute or otherwise by operation of law (legal life estates). This fact sheet only discusses conventional life estates.

Historically, a life estate could be created by a property owner transferring his or her property “to X for life.” A life estate was also created if the correct words were not used to create a fee simple estate. Today, a life estate generally can be created only by express words of limitation when property is transferred, for example, “to X for life.”

An estate *pur autre vie* is created by words such as “to X for as long as Y lives.” An estate *pur autre vie* is also created if the owner of a life estate assigns his or her life estate to another person.



A person wishing to create a life estate must define the estate in the deed or will in which it is created. The words used in the document determine the nature of the interest created.

A life estate may be made determinable (liable to end) by using words that limit its duration or make it conditional. For example, a person in her will may leave her land to her husband "for his use and benefit during the remainder of his life or until his remarriage." The husband's life estate would end on his death or remarriage. A property owner also can grant successive life estates, for example, "to X for her life and, on her death, to Y for his life." A life estate ends with the death of the owner of the life estate.

A life estate is an interest in land. The owner of the life estate is the owner of the land during the term of the life estate and, with some exceptions, has the same right to use and possess the land as the owner of the fee simple estate.

Life estates are distinguishable from licences, which are contractual arrangements only and do not constitute interests in land. They also are distinguishable from leases, which are transfers of the right to exclusive possession of real property from the lessor to the lessee, generally on certain conditions, for a defined term. Licences are discussed below.

When a property owner transfers land but retains a life estate or transfers a life estate to another person, the estate or interest that is left after the life estate ends is the remainder interest. Remainder interests are sometimes called residual interests. For example, if Jane Bloggs transfers her land "to Jane Bloggs (herself) for life, the remainder to Fireweed Conservancy Association in fee simple," Fireweed's interest is the remainder interest. Each of Jane Bloggs and Fireweed has an estate or interest in the land that exists in the present, is capable of being owned in the present and has a value in the present. However, as

explained below, Fireweed's remainder interest is a future interest.

Jane Bloggs might also choose to transfer her land "to Jane Bloggs (herself) for life, remainder to Joe Bloggs (her son) for his life, remainder to Fireweed Conservancy Association in fee simple." Both Joe Bloggs and Fireweed hold remainder interests although Joe Bloggs' remainder interest is a life estate only. A number of rules govern what constitutes a valid remainder interest. However, a detailed discussion of remainder interests is beyond the scope of this fact sheet.

A remainder interest is an interest in land, but it is a future interest. In other words, the right to possession or enjoyment of the land is postponed to a future time.

As with the creation of a life estate, whether or not a document creates a remainder interest will be a matter of interpretation of the document creating the interest, through close examination of the document itself.

Usufruct and right of use and bare ownership

Usufruct is "the right of use and enjoyment, for a certain time, of property owned by another as one's own, subject to the obligation of preserving its substance" (1120 C.C.Q.). A right of use is "the right to enjoy the property of another for a time and to take the fruits and revenues [of the property] to the extent of the needs of the user" (1172 C.C.Q.). The aim of usufruct³ and use,⁴ as dismemberments of the right of ownership of property, is to allow the usufructuary or user to benefit from the use and enjoyment of the immovable property for a certain period of time.

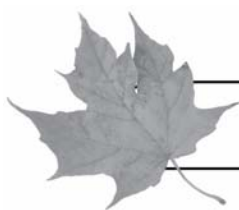
Usufruct and right of use are temporary rights that can remain in effect for a maximum of 100 years.⁵ A right of use is more restricted than usufruct in that it can only be granted to natural persons. Generally, a usufruct and right of use are created by agreement. Although the C.C.Q. sets out various rules governing usufruct and use, the agreement that establishes the right of usufruct or use outlines the terms and conditions of the rights.

If a donor donates land to a qualified recipient but retains a right of use or usufruct or assigns such a right to another person, the donor transfers bare ownership of the land to the recipient. The bare owner has the right to dispose of the property fully and freely but does not have the right to use and enjoy it. At the end of the

³ Section 1120 and following, C.C.Q.

⁴ Section 1172 and following, C.C.Q.

⁵ Section 1123, C.C.Q.



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usufruct or use, the bare owner acquires full ownership of the immovable property. In addition to having the right to dispose of the property, the owner then also has the right to use and enjoy the property.

As with a remainder interest, bare ownership of land is a presently existing interest in the land. The fact that bare ownership of land does not include the right to use and enjoy the land until some future date will be reflected in its value.

Superficies

The C.C.Q. defines “superficies” as follows:

Superficies is ownership of the constructions, works or plantations situated on an immovable belonging to another person, the owner of the subsoil (section 1011).

Superficies is in itself a full right of ownership, including all the rights associated with ownership, but in a particular form. The superficiary owns the structures, works or plantations situated on land, the subsoil of which is owned by someone else.

Provisions for the establishment of superficies are contained in section 1110 of the C.C.Q. Generally speaking, superficies results from an agreement expressly entered into by the superficiary and the owner of the subsoil. The agreement usually includes provisions for the various terms and conditions regarding use of the subsoil by the superficiary, the duration of the agreement and the rights and obligations of the parties, as well as the fate of the constructions, works or plantations when the superficies ends. The provisions contained in the *Civil Code of Québec* apply where an agreement is silent about one of these matters.

Personal rights – licences and permission agreements

In common law jurisdictions and in Quebec, a donor can make an agreement with a recipient of an ecological gift to continue to use the land. In common law jurisdictions, this arrangement may take the form of a licence and, in Quebec, a permission agreement to use.

A licence in relation to real property is the right to go onto the property of the person granting the licence, for a specified purpose. It is a personal right between the person granting the licence and the licence holder. Unlike a life estate or remainder interest, a licence does not create any estate or interest in the land.

Like a licence, a permission agreement to use is a right of access to land for a specific purpose. It is a personal right granted by the owner to another person. Unlike usufruct, right of use and superficies does not create a real right.

Generally a licence or permission agreement to use is created in a contract or agreement, the terms of which set out the nature of the licence granted, its duration, whether it can be assigned and so on. The licence or permission agreement holder will be entitled to the rights that are given to the holder in the agreement. For example, a licence or permission agreement may give the holder the right to use the property for hiking or camping at certain times of the year.

Neither a licence nor a permission agreement can be the subject of an ecological gift because neither is an interest in land or real right.

HOW TO DETERMINE THE NATURE OF THE INTEREST

This fact sheet does not contain a comprehensive discussion of options available to a donor wanting to make an ecological gift of land while maintaining the right to use the land in some way. Other alternatives may be available. Depending on the document and circumstances, it may be difficult to determine whether the interest or right created is a life estate, lease,⁶ or licence in common law jurisdictions or a usufruct, right of use, superficies or permission agreement in Quebec.

If a document is ambiguous, what it calls itself does not necessarily determine what it is, although what the document is called will be one factor used to interpret its intent. The words of the document as a whole and, in some circumstances, the surrounding circumstances and conduct of the parties, will be relevant to determining the nature of the interest created.

Prospective donors with questions about a specific gift, such as whether the gift would be viewed as a gift of the full ownership of the land involved or the gift of a right or interest in the land, or who wish to discuss the appropriate documentation for the type of donation they are planning, should contact their legal and tax

⁶ A lease is a contract between a landowner, the landlord, and a tenant by which the tenant obtains exclusive possession of the landlord's property, generally on certain conditions, for a specific period of time. A gift of a lease does not qualify as an ecological gift.



advisors or the Income Tax Rulings Directorate of the Canada Revenue Agency.

TAX IMPLICATIONS OF RETAINING THE RIGHT TO USE DONATED LAND

The tax implications of a donation depend, in part, on the nature of the right or rights donated. Some of the tax implications of retaining the right to use donated land are discussed below. Simple examples are provided to illustrate the tax implications.

The examples below are simplified. The legal and tax implications of any transaction depend on the circumstances of the transaction as a whole and on the landowner's individual circumstances. Donors and recipients proposing to engage in the types of transactions discussed in this fact sheet should each obtain independent legal and tax advice before completing any transaction.

For additional information about the tax implications of various donation options, see the hypothetical tax scenarios illustrating the federal income tax implications of making an ecological gift on the Ecological Gifts Program's website at <http://www.cws-scf.ec.gc.ca/egp-pde/>.

be certified as ecologically sensitive, the recipient must be qualified to receive the gift and the remainder interest or bare ownership must be appraised and its value determined by the Minister of the Environment through the Appraisal Review and Determination Process. The relevant value will be the value of the remainder interest or bare ownership at the time of the gift.

A gift of a life estate or right of use or usufruct does not qualify as an ecological gift since it terminates at the death of the life tenant, usufructuary or user, or at the end of a pre-established period of time. It therefore cannot be a gift in perpetuity, one of the criteria of an ecological gift.

When a donor makes an ecological gift of a remainder interest or bare ownership, the recipient must take reasonable steps to protect the land during the tenure of the life tenant or for the duration of the usufruct or right of use so that the ecological values are protected until the recipient takes full ownership and possession of the property. This could be accomplished by way of an agreement between the donor and recipient or any other parties involved.



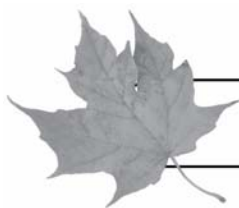
Gift of remainder interest or bare ownership

If a donor donates his or her land to a qualified recipient but retains a life estate or grants a life estate to someone else such as a family member, the donor has donated the remainder interest to the recipient. A donor who donates land to a qualified recipient but maintains a right of use or usufruct or assigns such a right to another person donates bare ownership of the land to the recipient.

As long as it meets the requirements of the *Income Tax Act* and the Ecological Gifts Program,⁷ a gift of the remainder interest or bare ownership of land will be a valid ecological gift. Specifically, the donated land must

Photos Credits in order of appearance: K. Fournier, R. Amy

⁷ And assuming the proposed amendments to section 248 discussed above are adopted.



Retaining the Right to Use Land Donated as an Ecological Gift

Life Interests and Licences: Usufruct, Right of Use, Superficies and Permission Agreements

Example of life estate and remainder interest

Anna Santini owns five hectares of land in Saskatchewan, three hectares of which are valuable marshland. The current value of the property is \$200,000. Her home is located on the land and she has lived on it for the last 35 years. Anna has a son, Bill, who loves the land as much as his mother. Anna is 80 and is finding it difficult to continue living in her home. She does not want to sell because she is deeply concerned about protecting the marshland. Bill, who has been living in the city, wants to spend his retirement years in his family home and on the land he loves. Anna has decided to give the property to a local conservancy organization but wants Bill to be able to live on it for the rest of his life. Bill is 52 at the time of the gift.

After consulting her lawyer and accountant, Anna decides to transfer the land to Bill for his life and, on his death, to the conservancy organization. She decides to go through the Ecological Gifts Program to maximize the tax benefits associated with the gift of the remainder interest. The transfer of the remainder interest to the conservancy organization meets all the qualifications of an ecological gift. The land is certified as ecologically sensitive. The conservancy organization is approved to receive the gift.

Anna has the property and the value of the remainder interest appraised and completes the ecological gift application process. The remainder interest is valued at \$25,000. The Minister of the Environment determines this amount as the fair market value of the remainder interest. Once the life estate is transferred to Bill and the remainder interest to the conservancy organization, Anna receives a Statement of Fair Market Value and a tax receipt for \$25,000.

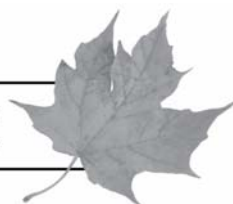
The conservancy organization enters into an agreement with Bill about using and caring for the property during his lifetime in a way that is consistent with protecting the marshland.

Example of donation with conservation of usufruct

In the example above, assume Anna Santini's property is located in the province of Quebec. She decides to transfer usufruct of the immovable property to her son Bill and bare ownership of the immovable property to a conservancy organization. As in the example above, she can use the Ecological Gifts Program to maximize the tax benefits associated with donation of the bare ownership as long as the transfer of bare ownership meets the criteria for an ecological gift outlined in the above example.

Anna has the immovable property and the value of the bare ownership appraised and goes through the ecological gift application process. The bare ownership is valued at \$25,000 and the Minister of the Environment determines this amount as its fair market value. Once the usufruct is transferred to Bill and bare ownership is transferred to the organization, Anna receives a Statement of Fair Market Value and a tax receipt in the amount of \$25,000.

The agreement entered into by Anna, Bill and the organization sets out the terms and conditions of use and maintenance of the property for the duration of the usufruct to ensure, among other things, protection of the marsh.



Gift of land with conservation of superficies

If a donor donates land to a qualified recipient but retains ownership of certain structures on the land or transfers ownership of the structures to another person, the land donation can be considered an

ecological gift if it meets the requirements of the *Income Tax Act* and the Ecological Gifts Program.⁸ The relevant value will be the value of the land, taking into account the superficies at the time of the gift.

Example of a gift with conservation of superficies

Steven Burke owns three hectares of land on which his main residence is built. Steven would like to take advantage of the Ecological Gifts Program to preserve the ecologically sensitive nature of his land while benefiting from the tax incentives associated with the Program. However, he also wants to continue living in his home until he retires in 25 years.

Steven transfers his land to a conservancy organization while reserving superficies of the house on the land. Steven remains owner of his home, while the organization becomes owner of the land. The donation meets all the qualifications of an ecological gift. The land is certified as ecologically sensitive. The conservancy organization is approved to receive the gift. The land is appraised, taking into account the superficies reserved by Steven, and the Minister of the Environment determines the fair market value of the land to be this appraised value. The tax receipt is issued to Steven based on this value.

The agreement between Steven and the organization sets out the rights and obligations of each of the parties as well as terms and conditions governing Steven's use of the land intended to ensure protection of the land's ecologically sensitive nature.

Gift of land with a licence or permission agreement

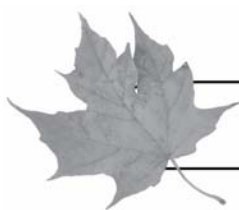
If a fee simple estate or immovable property is transferred to a qualified recipient and a licence or permission agreement to use is given to the donor, the value of the licence or permission agreement to use will be a benefit or advantage to the donor. The proposed changes to the *Income Tax Act* authorizing split-receipting⁹ provide generally that a gift is recognized for the purposes of the Act even if the donor receives consideration for the transfer, provided that the fair market value of the benefit received by the donor is less than 80% of the fair market value of the property transferred to the qualified recipient.

If land is donated to a qualified recipient and the donor is given a licence back or receives a permission agreement to occupy the land, the amount included in the donor's "total ecological gifts" for the taxation year will be the difference between the fair market value of the land transferred to the qualified recipient and the fair market value of the licence or permission agreement (and any other advantage) given to the donor by the qualified recipient. The fair market value of the land in this case will be the amount determined by the Minister of the Environment to be its fair market value.

If the licence or permission agreement to use has value and therefore constitutes a benefit to the donor, the recipient must satisfy itself about the fair market value of the benefit or advantage to the donor before issuing a tax receipt for the gift. If a gift involves a split-receipt, the official tax receipt must record the fair market value of the transferred property and the eligible amount of the gift for which the donor may receive a tax deduction or credit.

⁸ Certain actions or agreements may have an impact on superficies and on the value of the land donation. Donors and recipients should obtain professional advice about the implications of this kind of donation.

⁹ The interpretational guidelines are contained in *Income Tax Technical News*, no. 26, at <http://www.cra-arc.gc.ca/E/pub/tp/itnews-26/itnews-26-e.pdf>, and the legislative proposals, draft regulations and explanatory notes relating to income tax can be found at <http://www.fin.gc.ca/toce/2004/ita04-introe.html>. The proposed changes to the Act are in effect even though the amendments are not yet in force.



Retaining the Right to Use Land Donated as an Ecological Gift

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Example of licence/permission agreement

Pat Murphy owns 10 hectares of land. The land is valuable habitat for two endangered species. Pat has decided to transfer the land to a local conservancy organization to ensure its protection in the future. The conservancy organization has agreed to pay Pat \$50,000 for the land, which is valued at \$250,000. In addition, in return for Pat's gift, the organization has agreed that Pat can visit the property regularly and camp in one area of the property two or three weekends a year.

After consulting with the conservancy organization, Pat decides to make an ecological gift of the land to maximize the tax benefits. The donation meets all the qualifications of an ecological gift. The land is certified as ecologically sensitive. The conservancy organization is approved to receive the gift. The land is appraised at \$250,000 and the Minister of the Environment determines the fair market value of the land to be this appraised value.

As part of the transaction, Pat enters into a licence agreement with the conservancy organization (in Quebec, obtains a permission agreement to occupy from the organization). Under the licence/permission agreement Pat can use the property for life for walking and hiking at any time and for camping but only in a defined area and only for up to three weekends per year between June 1 and September 30. The licence/permission agreement also contains terms requiring Pat to ensure the ecological values of the property are protected during Pat's use of the property.

The licence/permission agreement provides an additional advantage (beyond the \$50,000) to Pat in return for making the donation. However, neither the licence agreement nor the payment of \$50,000 disqualifies the transfer as a gift. The value of the licence to use the land is appraised at \$5,000.

After the land is transferred, Pat receives a Statement of Fair Market Value from the Minister of the Environment for \$250,000, the value of the land. Pat receives a tax receipt from the conservancy organization showing the fair market value of the land (\$250,000) and the eligible amount of the gift. The eligible amount of the gift is \$195,000: the fair market value of the land minus \$55,000, the amount of the advantage Pat received in return for making the gift (\$50,000 plus \$5,000, the value attributed to the licence agreement). Pat can claim a tax credit based on the eligible amount of the gift.

The background of the entire page is a close-up photograph of autumn leaves. The top half shows a dense layer of leaves in various shades of green, yellow, and brown. The bottom half is a lighter, more uniform yellowish-brown, possibly representing a different set of leaves or a different lighting condition. The leaves are mostly maple-like in shape, with prominent veins.

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ISBN: 978-0-662-46792-2
Cat No.: CW66-238/6-2007E-PDF

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Cover photos: A. Holbrook, R. Amy, K. Fournier