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PROPOSED CHANGES TO THE INCOME TAX ACT CONCERNING FLOW-THROUGH SHARES

(OTTAWA) Finance Minister Don Mazankowski and the Minister of Energy, Mines and Resources, Jake Epp today released details of a measure with respect to flow-through shares proposed in the Economic and Fiscal Statement of December 2, 1992. This measure is designed to stimulate new equity investment in the junior oil and gas sector.

This measure will allow the first \$2 million of eligible Canadian development expenses that are renounced by a company to shareholders under a flow-through share agreement to be reclassified as Canadian exploration expenses. This will allow shareholders to deduct 100 percent of the amount of such expenses renounced. Canadian development expenses are ordinarily only deductible at a rate of 30 percent per year.

Minister Mazankowski said: "The oil and gas sector is facing difficulty in financing exploration. The proposed change will provide tax relief amounting to about \$10 million annually to assist junior oil and gas companies to raise badly needed risk capital."

Minister Epp said: "I am pleased with my colleague's announcement made today. This change will facilitate raising equity and stimulate drilling activity."

The \$2 million reclassification will be available on an annual basis, to each company or associated group of companies, for eligible expenses incurred after December 2, 1992. The proposal also permits eligible expenses incurred in the first 60 days of a calendar year to be treated as having being incurred at the end of the preceding year.

Details of this measure in the form of draft legislation and explanatory notes are attached.

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DRAFT INCOME TAX LEGISLATION ON FLOW-THROUGH SHARES

1.(1) All that portion of subsection 66(12.6) of the *Income Tax Act* preceding paragraph (a) thereof is repealed and the following substituted therefor:

Canadian exploration expenses to flow-through shareholder

(12.6) Where a person gave consideration under an agreement to a corporation for the issue of a flow-through share of the corporation and, during the period commencing on the day the agreement was entered into and ending 24 months after the end of the month that included that day, the corporation incurred Canadian exploration expenses, the corporation may, after it complies with subsection (12.68) in respect of the share and before March of the first calendar year commencing after that period, renounce, effective on the date on which the renunciation is made or on such earlier date as may be set out in the form prescribed for the purposes of subsection (12.7), to the person in respect of the share the amount, if any, by which those expenses incurred by it during that period and on or before the effective date of the renunciation exceed the total of

(2) Paragraph 66(12.6)(d) of the said Act is repealed and the following substituted therefor:

(d) exceeding the amount, if any, by which the consideration for the share exceeds the total of other amounts renounced in respect of the share under this subsection or subsection (12.601), (12.62) or (12.64) on or before the date on which the renunciation is made, or

(3) Subsection 66(12.61) of the said Act is repealed and the following substituted therefor:

Flow-through share rules for first \$2 million of Canadian development expenses

(12.601) Where

(a) a person gave consideration under an agreement to a corporation for the issue of a flow-through share of the corporation, and

(b) during the period commencing on the later of December 3, 1992 and the particular day the agreement was entered into and ending on the day that is 24 months after the end of the month that included that particular day, the corporation incurred Canadian development expenses described in subparagraph 66.2(5)(a)(i) or (i.1) or that would be described in subparagraph 66.2(5)(a)(iv) if the words "subparagraphs (i) to (iii)" in that subparagraph were read as "subparagraphs (i) and (i.1)",

the corporation may, after it complies with subsection (12.68) in respect of the share and before March of the first calendar year commencing after that period, renounce, effective on the day on which the renunciation is made or on such earlier day as may be set out in the form prescribed for the purposes of subsection (12.7), to the person in

respect of the share the amount, if any, by which those expenses incurred by it during that period and on or before the effective date of the renunciation exceed the total of

(c) the assistance that it has received, is entitled to receive, or can reasonably be expected to receive at any time, and that can reasonably be related to those expenses or Canadian development activities to which those expenses relate (other than assistance that may reasonably be attributable to expenses referred to in paragraph (b)),

(d) any of those expenses that are prescribed Canadian exploration and development overhead expenses of the corporation, and

(e) the total of amounts that are renounced on or before the day on which the renunciation is made by any other renunciation under this subsection or subsection (12.62) in respect of those expenses.

Idem

(12.602) A corporation shall be deemed not to have renounced any particular amount under subsection (12.601) in respect of a share where

(a) the particular amount exceeds the amount, if any, by which the consideration for the share exceeds the total of other amounts renounced in respect of the share under subsection (12.6), (12.601), (12.62) or (12.64) on or before the day on which the renunciation is made;

(b) the particular amount exceeds the amount, if any, by which

(i) the cumulative Canadian development expense of the corporation on the effective date of the renunciation, computed before taking into account any amounts renounced under subsection (12.601) on the day on which the renunciation is made,

exceeds

(ii) the total of all amounts renounced under subsection (12.601) by the corporation in respect of any other share

(A) on the day on which the renunciation is made, and

(B) effective on or before the effective date of the renunciation; or

(c) the particular amount relates to Canadian development expenses incurred by the corporation in a calendar year and the total amounts renounced, on or before the day on which the renunciation is made, under subsection (12.601) in respect of

(i) Canadian development expenses incurred by the corporation in that calendar year, or

(ii) Canadian development expenses incurred in that calendar year by another corporation associated with the corporation at the time the other corporation incurred such expenses

exceeds \$2,000,000.

Effect of renunciation

(12.61) Subject to subsections (12.69) to (12.701), where under subsection (12.6) or (12.601) a corporation renounces an amount to a person

(a) the Canadian exploration expenses or Canadian development expenses to which the amount relates shall be deemed to be Canadian exploration expenses incurred in that amount by the person on the effective date of the renunciation; and

(b) the Canadian exploration expenses or Canadian development expenses to which the amount relates shall, except for the purposes of that renunciation, be deemed on and after the effective date of the renunciation never to have been Canadian exploration expenses or Canadian development expenses incurred by the corporation.

(4) All that portion of subsection 66(12.62) of the said Act preceding paragraph (a) thereof is repealed and the following substituted therefor:

Canadian development expenses to flow-through shareholder

(12.62) Where a person gave consideration under an agreement to a corporation for the issue of a flow-through share of the corporation and, during the period commencing on the day the agreement was entered into and ending 24 months after the end of the month that included that day, the corporation incurred Canadian development expenses, the corporation may, after it complies with subsection (12.68) in respect of the share and before March of the first calendar year commencing after that period, renounce, effective on the date on which the renunciation is made or on such earlier date as may be set out in the form prescribed for the purposes of subsection (12.7), to the person in respect of the share the amount, if any, by which those expenses incurred by it during that period and on or before the effective date of the renunciation exceed the total of

(5) All that portion of subsection 66(12.62) of the said Act following paragraph (b) thereof and preceding paragraph (e) thereof is repealed and the following substituted therefor:

(c) the total of amounts that are renounced on or before the day on which the renunciation is made by any other renunciation under this subsection or subsection (12.601) in respect of those expenses,

but not in any case

(d) exceeding the amount, if any, by which the consideration for the share exceeds the total of other amounts renounced in respect of the share under this subsection or subsection (12.6), (12.601) or (12.64) on or before the date on which the renunciation is made, or

(6) All that portion of subsection 66(12.64) of the said Act preceding paragraph (a) thereof is repealed and the following substituted therefor:

Canadian oil and gas property expenses to flow-through shareholder

(12.64) Where a person gave consideration under an agreement to a corporation for the issue of a flow-through share of the corporation and, during the period commencing on the day the agreement was entered into and ending 24 months after the end of the month that included that day, the corporation incurred Canadian oil and gas property expenses, the corporation may, after it complies with subsection (12.68) in respect of the share and before March of the first calendar year commencing after that period, renounce, effective on the date on which the renunciation is made or on such earlier date as may be set out in the form prescribed for the purposes of subsection (12.7), to the person in respect of the share the amount, if any, by which those expenses incurred by it during that period and on or before the effective date of the renunciation exceed the total of

(7) Paragraph 66(12.64)(c) of the said Act is repealed and the following substituted therefor:

(c) exceeding the amount, if any, by which the consideration for the share exceeds the total of other amounts renounced in respect of the share under this subsection or subsection (12.6), (12.601) or (12.62) on or before the date on which the renunciation is made, or

(8) Subsection 66(12.66) of the said Act is repealed and the following substituted therefor:

Expenses in the first 60 days of year

(12.66) Where

(a) a corporation that issues a flow-through share to a person under an agreement incurs, within 60 days after the end of a calendar year, Canadian exploration expenses or Canadian development expenses,

(b) the expenses are expenses described in subparagraph 66.1(6)(a)(i), (ii.1) or (iii) or 66.2(5)(a)(i) or (i.1),

(c) before the end of the year, the agreement was entered into between the corporation and the person and the person paid the consideration for the share in money,

(d) the corporation and the person deal with each other at arm's length throughout the 60 days, and

(e) within 90 days after the end of the year, the corporation renounces an amount in respect of the expenses to the person in respect of the share in accordance with subsection (12.6) or (12.601) and the effective date of the renunciation is the last day of the year,

the corporation shall for the purposes of subsection ((12.6) or (12.601)) be deemed to have incurred the expenses on the effective date of the renunciation.

(9) Subsection 66(12.67) of the said Act is repealed and the following substituted therefor:

Restrictions on renunciation

(12.67) A corporation shall be deemed not

(a) to have renounced under any of subsections (12.6), (12.601), (12.62) and (12.64) any expenses that are deemed to have been incurred by it because of a renunciation under this section by another corporation that is not related to it;

(b) to have renounced under subsection (12.601) to a trust, corporation or partnership, any Canadian development expenses (other than expenses renounced to another corporation that renounces under subsection (12.6) any Canadian exploration expense deemed to have been incurred by it because of the renunciation under subsection (12.601)) if, in respect of the renunciation under subsection (12.601), it has a prohibited relationship with the trust, corporation or partnership;

(c) to have renounced under subsection (12.601), any Canadian development expenses deemed to have been incurred by it because of a renunciation under subsection (12.62); or

(d) to have renounced under subsection (12.6) to a particular trust, corporation or partnership, any Canadian exploration expenses (other than expenses ultimately renounced by another corporation under subsection (12.6) to an individual (other than a trust) or to a trust, corporation or partnership with which that other corporation does not have, in respect of such ultimate renunciation, a prohibited relationship) deemed to be incurred by it because of a renunciation under subsection (12.601), if, in respect of the renunciation under subsection (12.6), it has a prohibited relationship with the particular trust, corporation or partnership.

Prohibited relationship

(12.671) For the purposes of subsection (12.67), where a trust, corporation (in paragraph (b) referred to as the "shareholder corporation") or partnership, as the case may be, gave consideration under a particular agreement for the issue of a flow-through share of a particular corporation, the particular corporation has, in respect of a renunciation under subsection (12.6) or (12.601) in respect of the share, a prohibited relationship

(a) with the trust if, at any time after the particular agreement was entered into and before the share is issued to the trust, the particular corporation or any corporation related to the particular corporation is beneficially interested in the trust,

(b) with the shareholder corporation if, immediately before the particular agreement was entered into, the shareholder corporation was related to the particular corporation, or

(c) with the partnership if any part of the amount renounced would, but for subsection (12.7), be included because of subparagraph 66.1(6)(a)(iv) in the Canadian exploration expense of

(i) the particular corporation, or

(ii) any other corporation that, at any time

(A) after the particular agreement was entered into, and

(B) before such part of the amount renounced would, but for this paragraph, be incurred,

would, if flow-through shares issued by the particular corporation under agreements entered into at the same time as or after the time the particular agreement was entered into were disregarded, be related to the particular corporation.

(10) Subsection 66(12.69) of the said Act is repealed and the following substituted therefor:

Filing re partners

(12.69) Where, in a fiscal period of a partnership, an expense is or, but for this subsection, would be incurred by the partnership as a consequence of a renunciation of an amount under subsection (12.6), (12.601), (12.62) or (12.64), the partnership shall, on or before the last day of the third month following the end of that period, file with the Minister a prescribed form indicating the share of the expense attributable to each

member of the partnership at the end of the period and, where the prescribed form is not so filed, the partnership shall be deemed not to have incurred the expense.

(11) Subsection 66(12.7) of the said Act is repealed and the following substituted therefor:

Filing

(12.7) Where a corporation renounces an amount in respect of Canadian exploration expenses, Canadian development expenses or Canadian oil and gas property expenses under subsection (12.6), (12.601), (12.62) or (12.64), the corporation shall file a prescribed form in respect of the renunciation with the Minister before the end of the first month following the month in which the renunciation is made and, where the prescribed form is not so filed, subsections (12.61), (12.63) and (12.65) shall not apply in respect of the amount so renounced.

(12) Subsections 66(12.71) to (12.73) of the said Act are repealed and the following substituted therefor:

Restriction on renunciation

(12.71) A corporation may renounce an amount under subsection (12.6), (12.601), (12.62) or (12.64) in respect of Canadian exploration expenses, Canadian development expenses or Canadian oil and gas property expenses incurred by it only to the extent that, but for the renunciation, it would be entitled to claim a deduction in respect of the expenses in computing its income for the purposes of this Part.

Application of sections 231 to 231.3

(12.72) Without restricting the generality of sections 231 to 231.3, where a corporation has renounced an amount under subsection (12.6), (12.601), (12.62) or (12.64), sections 231 to 231.3 apply, with such modifications as the circumstances require, for the purpose of permitting the Minister to verify or ascertain the Canadian exploration expenses, Canadian development expenses or Canadian oil and gas property expenses of the corporation in respect of which the amount was renounced, the amounts renounced in respect of those expenses, any information in respect of those expenses or the amounts renounced and the amount of, or information relating to any assistance in respect of those expenses.

Adjustment in renunciation

(12.73) Where the total of all amounts that a corporation purported to renounce to persons under subsection (12.6), (12.601), (12.62) or (12.64) in respect of expenses incurred by it in any period ending on the effective date of the purported renunciation exceeds the total amount of such expenses in respect of which it may renounce amounts under that subsection, it shall

(a) reduce the amount so renounced to one or more persons to effect a reduction in the total of the amounts so purported to be renounced by the amount of the excess, and

(b) file a statement with the Minister indicating the adjustments made in the renunciations

and if the corporation has failed to so reduce the amounts and file such statement with the Minister within 30 days after notice in writing by the Minister has been forwarded to the corporation that such a reduction is or will be required for the purposes of any assessment of tax under this Part, the Minister may, for the purposes of this section, reduce the amounts purported to be renounced by the corporation to one or more persons to effect a reduction in the total of the amounts so purported to be renounced by the amount of the excess, and in any such case, notwithstanding subsections (12.61), (12.63), and (12.65), the amount renounced to each of the persons shall be deemed to be the amount as reduced by the corporation or the Minister, as the case may be.

(13) Section 66 of the said Act is further amended by adding thereto, immediately after subsection (12.74) thereof, the following subsection:

Late renunciation

(12.741) Where a corporation purports to renounce an amount under subsection (12.6), (12.601), (12.62) or (12.64) after the period during which the corporation would otherwise be entitled to renounce the amount, the amount shall, except for the purposes of this subsection and subsections (12.7) and (12.75), be deemed to have been renounced at the end of the period if

(a) the corporation purports to renounce the amount

(i) on or before the day that is 90 days after the end of that period, or

(ii) after the day that is 90 days after the end of that period where, in the opinion of the Minister, the circumstances are such that it would be just and equitable that the amount be renounced; and

(b) the corporation pays to the Receiver General a penalty in respect of the renunciation not more than 90 days after the renunciation.

(14) All that portion of subsection 66(12.75) of the said Act preceding paragraph (a) thereof is repealed and the following substituted therefor:

Penalty

(12.75) For the purposes of subsections (12.74) and (12.741), the penalty in respect of the late filing of a document referred to in subsection (12.68), (12.69), (12.691), (12.7) or (12.701) or in respect of a renunciation referred to in subsection (12.741) is the lesser of \$15,000 and

(15) Subsection 66(12.75) of the said Act is further amended by striking out the word "and" at the end of paragraph (a) thereof, by adding the word "and" at the end of paragraph (b) thereof and by adding thereto the following paragraph:

(c) where the penalty is in respect of a renunciation referred to in subsection (12.74), the greater of

(i) \$100, and

(ii) 1/4 of 1% of the amount of the renunciation.

(16) Subsection 66(19) of the said Act is repealed and the following substituted therefor:

Renunciation by member of partnership, etc.

(19) Notwithstanding subsections (12.6), (12.601), (12.62) and (12.64), where at any time a corporation

(a) would, but for this subsection, be entitled to renounce

(i) all or part of its share of an outlay or expense made or incurred by a partnership of which the corporation is a member or former member at that time, or

(ii) all or part of an amount renounced to the corporation under subsection (12.6), (12.601), (12.62) or (12.64),

under subsection (12.6), (12.601), (12.62) or (12.64) to another person, and

(b) would, if

(i) the expression "end of that fiscal period" in subsection (18) were read as "time the outlay or expense was made or incurred by the partnership", and

(ii) the expression "on the effective date of the renunciation" in each of paragraphs (12.61)(a), (12.63)(a) and (12.65)(a) were read as "at the earliest time that any part of such expense was incurred by the corporation"

not be entitled to so renounce the amount described in subparagraph (a)(i) or (ii) to the other person,

the corporation shall not be entitled to renounce such amount under subsection (12.6), (12.601), (12.62) or (12.64), as the case may be, at that time to the other person.

(17) Subsections (1), (4) and (6) apply with respect to expenses incurred after February 1986.

(18) Subsections (2), (3), (5), (7), (9) and (10) and subsection 66(12.73) of the said Act, as enacted by subsection (12), apply with respect to expenses incurred after December 2, 1992.

(19) Subsection (8) applies with respect to expenses incurred after 1992.

(20) Subsection (11) and subsection 66(12.71) of the said Act, as enacted by subsection (12), apply with respect to renunciations after December 2, 1992.

(21) Subsection 66(12.72) of the said Act, as enacted by subsection (12), applies after December 2, 1992.

(22) Subsections (13) to (15) apply with respect to renunciations purported to be made after February 1993.

(23) Subsection (16) applies to renunciations of outlays or expenses incurred after December 2, 1992.

2.(1) Subparagraph 66.1(6)(c)(iii) of the said Act is repealed and the following substituted therefor:

(iii) that was renounced by the taxpayer under subsection 66(10.2), (12.601) or (12.62),

(2) Subsection (1) applies to expenses incurred after December 2, 1992.

3.(1) Clause 66.3(4)(a)(ii)(B) of the said Act is repealed and the following substituted therefor:

(B) 50% of the total of the expenses that were renounced by the corporation under subsection (12.6), (12.601), (12.62) or (12.64) in respect of the share; and

(2) Subsection (1) applies after December 2, 1992.

4.(1) All that portion of subsection 66.7(10) of the said Act following paragraph (b) thereof and preceding paragraph (c) thereof is repealed and the following substituted therefor:

for the purposes of the provisions of the *Income Tax Application Rules, 1971* and this Act (other than subsections 66(12.6), (12.601), (12.602), (12.62), (12.64) and (12.71)) relating to deductions with respect to drilling and exploration expenses, prospecting, exploration and development expenses, Canadian exploration and development expenses, foreign exploration and development expenses, Canadian exploration expenses, Canadian development expenses and Canadian oil and gas property expenses (in this subsection referred to as "resource expenses") incurred by the corporation before that time, the following rules apply:

(2) Subsection (1) applies to taxation years ending after December 2, 1992.

5.(1) All that portion of subsection 87(4.4) of the said Act following paragraph (d) thereof and preceding paragraph (e) thereof is repealed and the following substituted therefor:

for the purposes of subsection 66(12.66) and for the purposes of renouncing an amount under subsection 66(12.6), (12.601), (12.62) or (12.64) in respect of Canadian exploration expenses, Canadian development expenses or Canadian oil and gas property expenses that would, but for the renunciation, be incurred by the new corporation after the amalgamation,

(2) Subsection (1) applies with respect to amalgamations occurring after December 2, 1992.

6.(1) Paragraph (d) of the definition "investment expense" in subsection 110.6(1) of the said Act is repealed and the following substituted therefor:

(d) 50% of the total of all amounts each of which is an amount deducted under subsection 66(4), 66.1(3), 66.2(2) or 66.4(2) in computing the individual's income for the year in respect of expenses incurred and renounced under subsection 66(12.6), (12.601), (12.62) or (12.64) by a corporation or incurred by a partnership of which the individual was a specified member of the partnership in which the expense was incurred, and

(2) Subsection (1) applies to the 1992 and subsequent taxation years.

7. All that portion of subsection 163(2.2) of the said Act preceding paragraph (a) thereof is repealed and the following substituted therefor:

False statement or omissions

(2.2) Every person who, knowingly or under circumstances amounting to gross negligence, has made or has participated in, assented to or acquiesced in the making of, a false statement or omission in any renunciation that is effective as of a particular date and that is made under any of subsections 66(10) to (10.3), (12.6), (12.601), (12.62) and (12.64) is liable to a penalty of 25% of the amount, if any, by which

**EXPLANATORY NOTES TO
DRAFT INCOME TAX LEGISLATION ON FLOW-THROUGH SHARES**

ITA

66(12.6), (12.62) and (12.64)

Subsections 66(12.6), (12.62) and (12.64) of the *Income Tax Act* permit a principal-business corporation to renounce Canadian exploration expenses (CEE), Canadian development expenses (CDE) and Canadian oil and gas property expenses (COGPE) that it incurs to a person who acquires flow-through shares issued by it. Among the conditions which must be met under these provisions are:

- ° the CEE, CDE or COGPE must be incurred by the corporation on or after the day, and within 24 months from the end of the month, the agreement to acquire the shares was entered into;
- ° the renunciation must be made no later than 30 days after the end of the 24-month period referred to above; and
- ° the total renounced amounts of CEE, CDE and COGPE in respect of a flow-through share cannot exceed the consideration for the share.

Subsections 66(12.6), (12.62) and (12.64) are amended to extend the time in which the renunciation must be made. The amendments allow a renouncing corporation to renounce expenses before March of the first calendar year commencing after the 24-month period referred to above. They apply in respect of expenses incurred after February 1986, at which time subsections 66(12.6), (12.62) and (12.64) became effective.

Paragraphs 66(12.6)(d), (12.62)(d) and (12.64)(c) are amended to make reference to new subsection 66(12.601), which permits the renunciation of a corporation's CDE. This ensures that the third condition described above applies in respect of CDE renounced under the new subsection. These amendments apply in respect of expenses incurred after December 2, 1992.

Paragraph 66(12.62)(c) is amended to ensure that the same CDE cannot be renounced under both subsection 66(12.601) and 66(12.62). This amendment applies in respect of expenses incurred after December 2, 1992.

ITA

66(12.601), (12.602) and (12.61)

New subsections 66(12.601) and (12.602) of the Act permit a principal-business corporation to renounce specified CDE that it incurs to a person who acquires flow-through shares issued by the corporation. Where an amount is renounced by a corporation to a person under subsection 66(12.601), amended subsection 66(12.61) provides that the person is deemed, on the effective date of the renunciation, to have

incurred CEE (rather than CDE) equal to the amount of specified CDE renounced. Except for the purposes of the renunciation, the corporation is deemed never to have incurred the specified CDE.

The conditions for renouncing specified CDE under subsection 66(12.601) are the same as renouncing CDE under amended subsection 66(12.62) with the following exceptions:

- the CDE must have been incurred by the renouncing corporation after December 2, 1992;
- the renouncing corporation (and corporations associated with the renouncing corporation) cannot collectively renounce under subsection 66(12.601) more than \$2 million of CDE incurred in a calendar year; and
- there are new restrictions described in the commentary to subsections 66(12.67) and (12.671).

Specified CDE is CDE described in subparagraphs 66.2(5)(a)(i) and (i.1), which relate to the development of oil and gas properties. Specified CDE also includes a corporation's share of such expenses incurred by a partnership and thereby included in the corporation's CDE under subparagraph 66.2(5)(a)(iv).

With the exception of the amendments to subsections 66(12.66), (12.67) and (12.75) and the introduction of subsections 66(12.671) and (12.741), the changes described below are strictly consequential to the introduction of new subsection 66(12.601). In addition, it is intended to make any necessary consequential changes to the *Income Tax Regulations* to reflect the new renunciation mechanism. (In particular, it is intended to make references to new subsection 66(12.601) in section 228 and subsection 1206(4.2) of the Regulations.)

These subsections apply with respect to expenses incurred after December 2, 1992.

ITA 66(12.66)

Subsection 66(12.6) of the Act permits a principal-business corporation to renounce CEE to a flow-through shareholder. A corporation may only renounce CEE incurred by it on or before the effective date of the renunciation. For this purpose, where a number of stated conditions are met, subsection 66(12.66) deems specified CEE incurred in the first 60 days of a calendar year to have been incurred by the corporation at the end of the preceding calendar year.

Subsection 66(12.66) is amended so that the same rule applies, for the purposes of new subsection 66(12.601), with respect to specified CDE. For this purpose, specified CDE is CDE related to oil and gas development that is described in subparagraph 66.2(5)(a)(i) or (i.1).

This amendment applies with respect to expenses incurred after 1992.

ITA

66(12.67)

Subsection 66(12.67) of the Act is a rule that restricts the resource expenses that may be renounced under subsections 66(12.6), (12.62) and (12.64). The rule provides that a corporation may not, under those subsections, renounce resource expenses renounced to it under those subsections unless it was related to the corporation that renounced those expenses to it.

Subsection 66(12.67) is amended so that the existing rule also applies in respect of renunciations under new subsection 66(12.601). The amended version of the existing rule is contained in new paragraph 66(12.67)(a).

Paragraph 66(12.67)(b) is introduced so that a corporation cannot, under new subsection 66(12.601), renounce any amount to a trust, another corporation or a partnership if the renouncing corporation has a "prohibited relationship" with the trust, other corporation or partnership. "Prohibited relationships" are defined in new subsection 66(12.671), which is discussed below. An exception to this rule permits a renunciation under subsection 66(12.601) to a related corporation which renounces the same amount under subsection 66(12.6), in accordance with new paragraph 66(12.67)(d).

Paragraph 66(12.67)(c) is introduced so that a corporation cannot, under new subsection 66(12.601), renounce any CDE deemed to have been incurred by it because of a renunciation under subsection 66(12.62). This amendment is intended to ensure that the \$2 million annual limit in respect of renunciations under subsection 66(12.601) is not avoided by virtue of renunciations between related corporations.

Paragraph 66(12.67)(d) is introduced so that a corporation cannot, under subsection 66(12.6), renounce any amount to a trust, another corporation or a partnership if the renouncing corporation has a "prohibited relationship" with the trust, other corporation or partnership. This paragraph applies only to CEE that is deemed to have been incurred by the renouncing corporation by virtue of a renunciation under new subsection 66(12.601) and that is not ultimately renounced by another corporation under subsection 66(12.6) to an individual or to a trust, corporation or partnership with which that other corporation does not have a prohibited relationship. The meaning of "prohibited relationship" is discussed below. This amendment is intended to ensure that the requirements under new paragraph 66(12.67)(b) cannot be avoided by virtue of renunciations between related corporations.

These amendments apply with respect to expenses incurred after December 2, 1992.

ITA
66(12.671)

New subsection 66(12.671) defines the expression "prohibited relationship" for the purposes of amended subsection 66(12.67). Subsection 66(12.67) applies where a trust, corporation or partnership has given consideration under an agreement for the issue of a flow-through share by a particular corporation.

In these circumstances, the particular corporation has a "prohibited relationship" with a shareholder trust if, at any time after the agreement was entered into and before the flow-through share was issued, the particular corporation (or a corporation related to the particular corporation) is beneficially interested in the shareholder trust. (Under proposed subsection 248(25), a person is "beneficially interested" in a trust if the person has any direct or indirect interest in the income or capital of the trust.)

The particular corporation has a "prohibited relationship" with the shareholder corporation if, immediately before the agreement was entered into, the shareholder corporation was related to the particular corporation.

The particular corporation has a prohibited relationship with the shareholder partnership if any part of the amount renounced is allocated through one or more tiers of partnership to the particular corporation or to another corporation in respect of which a specified condition is satisfied. This condition is that, at any time after the agreement was entered into and before the allocated amount would otherwise be considered to be incurred by it, the other corporation was (disregarding flow-through shares issued pursuant to the agreement and subsequent agreements) related to the particular corporation.

New subsection 66(12.671) applies in respect of expenses incurred after December 2, 1992.

ITA
66(12.69)

Subsection 66(12.69) of the Act requires that a partnership file an information return reporting allocations to its partners of amounts renounced to it under subsections 66(12.6), (12.62) and (12.64).

Subsection 66(12.69) is amended to apply the same rule with respect to renunciations under new subsection 66(12.601).

This amendment applies in respect of expenses incurred after December 2, 1992.

ITA
66(12.7)

Subsection 66(12.7) of the Act requires that a corporation file a prescribed form in respect of resource expenditures renounced by the corporation under subsections 66(12.6), (12.62) and (12.64). Subsection 66(12.7) is amended to apply the same rule with respect to renunciations under new subsection 66(12.601).

This amendment applies with respect to renunciations after December 2, 1992.

ITA
66(12.71)

Subsection 66(12.71) of the Act provides that a corporation may renounce an amount under new subsection 66(12.6), (12.62) or (12.64) in respect of CEE, CDE or COGPE only to the extent that the corporation would otherwise have been able to claim a deduction in respect of the CEE, CDE or COGPE.

Subsection 66(12.71) is amended to apply the same rule with respect to renunciations under new subsection 66(12.601).

This amendment applies with respect to renunciations after December 2, 1992.

ITA
66(12.72)

Subsection 66(12.72) of the Act permits the Minister of National Revenue to verify or ascertain information pertaining to Canadian resource expenses renounced by a corporation under subsection 66(12.6), (12.62) and (12.64), as well as information pertaining to assistance in respect of such expenses.

Subsection 66(12.72) is amended to apply the same rule with respect to renunciations under new subsection 66(12.601).

This amendment applies after December 2, 1992.

ITA
66(12.73)

Subsection 66(12.73) of the Act provides that, where a corporation renounces amounts under subsection 66(12.6), (12.62) or (12.64) to one or more persons in excess of the amount the corporation was entitled to renounce, the corporation shall reduce the amount so renounced and shall file a statement with the Minister indicating the adjustments made.

Subsection 66(12.73) is amended to apply the same rule with respect to renunciations under new subsection 66(12.601).

This amendment applies with respect to expenses incurred after December 2, 1992.

ITA

66(12.741) and (12.75)

Amended subsections 66(12.6), (12.62) and (12.64) (as well as new subsection 66(12.601)) generally provide for the renunciation, to a holder of a flow-through share, of resource expenditures incurred in the 24-month period following the first month ending after the date on which the agreement to issue the share is entered into. As discussed in the commentary below, the deadline for the renunciation is now the last day of February of the first calendar year commencing after the end of that period.

New subsection 66(12.741) allows a renouncing corporation to make a late renunciation, provided a penalty set out in amended subsection 66(12.75) is paid not more than 90 days following the late renunciation. The Minister of National Revenue must be satisfied that it is just or equitable to allow the late renunciation, unless the late renunciation is made not more than 90 days after the February deadline referred to above. Where a late renunciation is made, it is deemed for most purposes as having been made on the date of the February deadline. However, in order to avoid circularity and not provide an additional penalty for a corporation which files a prescribed form in respect of the late renunciation with the Minister before the end of the first month following the actual time of the late renunciation, the deeming rule does not apply for the purposes of subsections 66(12.7), (12.741) or (12.75).

Amended subsection 66(12.75) sets out the penalty in respect of a late renunciation under new subsection 66(12.741). The penalty in respect of a late renunciation is equal to the lesser of \$15,000 and the greater of

- \$100, and

- 1/4 of 1% of the amount of the late renunciation.

This penalty is consistent with the penalties already provided in subsection 66(12.75) with respect to late filing of documents in connection with flow-through shares.

These amendments apply with respect to late renunciations made after February 1993.

ITA

66(19)

Subsection 66(19) of the Act is an "anti-warehousing" rule which applies for the purposes of renunciations under subsections 66(12.6), (12.62) and (12.64). In general

terms, the rule requires a corporation which proposes to renounce an amount under those subsections to examine whether it would have been able to renounce the amount if amounts renounced to it by another corporation and its share of partnership expenses had been considered to have been incurred by it at the time the other corporation or the partnership incurred the renounced amount. This is intended to prevent a corporation from renouncing expenses that were originally incurred before the corporation had entered into a flow-through share agreement.

Subsection 66(19) is amended so that the same rule applies for the purposes of a renunciation under new subsection 66(12.601). This amendment applies to renunciations of outlays or expenses incurred after December 2, 1992.

ITA
66.1(6)(c)

Under subsection 66.1(9) of the Act, certain amounts of a taxpayer's CDE incurred in a taxation year may be re-classified as CEE in a subsequent taxation year. The subsection does not apply to "restricted expenses", as defined in paragraph 66.1(6)(c). "Restricted expenses" include CDE renounced by a taxpayer under subsection 66(12.62).

The definition is amended so that "restricted expenses" also include CDE renounced by a taxpayer under new subsection 66(12.601).

This amendment applies to expenses incurred after December 2, 1992.

ITA
66.3(4)(a)(ii)(B)

Subsection 66.3(4) of the Act provides rules for computing the paid-up capital of a corporation that issues flow-through shares. Paragraph 66.3(4)(a) requires a reduction in a corporation's paid-up capital in connection with the issue of a flow-through share equal to the amount, if any, by which

- the increase in the paid-up capital, otherwise determined, as a result of the issue of the share

exceeds

- the consideration received for the share minus 50% of amounts renounced under subsections 66(12.6), (12.62) or (12.64) in respect of the share.

Paragraph 66.3(4)(a) is amended so that amounts renounced under subsection 66(12.601) have the same effect on the computation of a corporation's paid-up capital.

This amendment applies after December 2, 1992.

ITA
66.7(10)

Subsection 66.7(10) of the Act provides a number of rules which generally apply when a corporation undergoes a change of control or ceases to be exempt from tax under Part I. Essentially, resource expenditures incurred by a corporation before that time are considered not to have been incurred by the corporation and instead are deemed, for the purposes of the successor rules, to have been incurred by an original owner. As a consequence, deductions by the corporation in respect of such expenditures may generally only be claimed against "streamed income" in connection with properties owned by the corporation before that time. Subsection 66.7(10) does not, however, apply for the purposes of determining a corporation's entitlement to renounce an amount under subsection 66(12.6), (12.62) or (12.64).

Subsection 66.7(10) is amended so that it also does not apply for the purposes of determining a corporation's entitlement to renounce an amount under new subsection 66(12.601).

This amendment applies to taxation years ending after December 2, 1992.

ITA
87(4.4)

Subsection 87(4.4) of the Act applies where a corporation that has entered into a flow-through share arrangement with a person amalgamates with another corporation. The rules in subsection 87(4.4) generally enable the corporation formed as a consequence of the amalgamation to renounce expenses incurred after the amalgamation to the person.

Subsection 87(4.4) of the Act is amended so that the same rules apply in respect of a renunciation under new subsection 66(12.601).

This amendment applies with respect to amalgamations occurring after December 2, 1992.

ITA
110.6(1)

"investment expense"

The definition "investment expense" in subsection 110.6(1) of the Act applies for the purposes of determining an individual's "cumulative net investment loss". An increase in an individual's "investment expenses" can result in an increase in an individual's cumulative net investment loss and a consequential decrease in the individual's entitlement to the capital gains exemption under section 110.6. An individual's

"investment expense" for a taxation year includes, under paragraph (d) of the definition, 50% of amounts deducted by the individual for the year in respect of resource expenses renounced to the individual under subsection 66(12.6), (12.62) or (12.64).

Paragraph (d) of the definition is amended so that the rule therein also applies in respect of resource expenses renounced under new subsection 66(12.601).

This amendment applies to the 1992 and subsequent taxation years.

ITA
163(2.2)

Subsection 163(2.2) of the Act provides a penalty where a taxpayer makes a false statement or omission in a renunciation of resource expenses under subsection 66(12.6), (12.62) or (12.64).

Subsection 163(2.2) is amended so that the same penalty apply in respect of a renunciation of resource expenses under new subsection 66(12.601).

This amendment applies on Royal Assent.