

BETWEEN:

TUSK EXPLORATION LTD.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on September 14, 2016, at Vancouver, British Columbia

Before: The Honourable Justice Valerie Miller

Appearances:

Counsel for the Appellant: David Pedlow
Parveen Karsan
Counsel for the Respondent: Victor Caux
Matthew Turnell

JUDGMENT

The appeal from the reassessments made under the *Income Tax Act* for the Appellant's 2002, 2003, 2004, 2005 and 2006 taxation years is allowed and the reassessments are referred back to the Minister of National Revenue for reconsideration and reassessment on the basis of the concessions made by the Respondent at the hearing of this appeal as follows:

- a. The amount of Part XII.6 tax is reduced by \$64,723, \$22,597 and \$4,502 in the 2004, 2005 and 2007 taxation years; and
- b. The subsection 162(1) penalties are reduced by \$15,610.

In all other respects, the appeal is dismissed.

The parties have thirty days from the date on the Judgment to make submissions with respect to costs. If no submissions are made, the Respondent is entitled to costs according to the tariff.

Signed at Ottawa, Canada, this 26th day of October 2016.

“V.A. Miller”

V.A. Miller J.

Citation: 2016TCC238
Date: 20161026
Docket: 2013-3525(IT)G

BETWEEN:

TUSK EXPLORATION LTD.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

V.A. Miller J.

Overview

[1] The Appellant is a Canadian company engaged in the business of mineral exploration and development. It is a Canadian Controlled Private Corporation within the meaning given in subsection 125(7) of the *Income Tax Act* (the “*Act*”) and a Principal Business Corporation as defined in subsection 66(15) of the *Act*. In its 2002, 2003, 2004, 2005 and 2006 taxation years, the Appellant issued flow-through shares to a number of investors. Throughout this Period, the Appellant filed the prescribed forms with the Canada Revenue Agency to renounce Canadian Exploration Expenses to its flow-through shareholders. Many of the renunciations were made on a look-back basis pursuant to subsection 66(12.66) – “Look-Back Renunciations”. This provision allows the shareholder to take a deduction in the year prior to the expenses being incurred by the Appellant. The Appellant is deemed to have incurred the expenses on the last day of the year in which the expenses are claimed if all of the conditions in subsection 66(12.66) are met. According to paragraph 66(12.66)(d), the Appellant and the shareholder had to deal with each other at arm’s length. That condition was not met in this appeal.

[2] When a corporation makes a Look-Back Renunciation, it must file a tax return and pay a tax pursuant to Part XII.6 (section 211.91) of the *Act*.

[3] The issue in this appeal is whether the Appellant must pay the tax under Part XII.6 of the *Act* when the Look-Back Renunciations under subsection 66(12.66) are invalid.

[4] The brief answer to this question is yes.

Facts

[5] The only witness at the hearing was Ward Hodgins, CPA. Mr. Hodgins is now retired but prior to his retirement, he was a Business Auditor with the Mining Tax Incentive Group of the Canada Revenue Agency (“CRA”) in Vancouver, British Columbia. He was the auditor on this file.

[6] The parties filed an Agreed Statement of Facts and Documents which I have attached to these reasons as Appendix A. A summary of those agreed facts, with a summary of Mr. Hodgins testimony, follows.

[7] The Appellant has a December 31st year-end for tax purposes. In its 2002, 2003, 2004, 2005 and 2006 taxation years (the “Period”), the Appellant issued flow-through shares to a number of investors pursuant to Flow-Through Share Subscription Agreements (“FTS Agreements”) between it and the various investors.

[8] The Appellant filed information forms with the CRA to receive an identification number (the “TIN #”) for the flow-through share offerings. When it received the TIN #, the Appellant then filed form T101A in which it renounced Canadian Exploration Expenses (“CEE”) to the shareholders included in the particular TIN #. During the Period, the effective date of the renunciations and the CEE renounced (the “Renunciations”) by the Appellant were as follows:

TIN#	Effective Date	Renunciations under s. 66
02-30542-5	June 30, 2002	\$800,000
02-31225-6	December 31, 2002	\$860,000
03-31361-9	January 31, 2003	\$700,000
03-31610-9	June 30, 2003	\$2,500,000
03-32541-5	December 31, 2003	\$1,545,000
04-33938-2	December 31, 2004	\$275,000

04-34021-6	June 30, 2004	\$1,500,000
05-35388-8	December 31, 2005	\$1,260,000
06-36179-0	December 31, 2006	\$450,000
06-37487-6	December 31, 2006	\$910,000
Total		\$10,800,000

[9] In its filings, the Appellant:

- a) claimed \$4,450,000 of the Renunciations on line 60 of the T101A forms;
and
- b) claimed \$6,350,000 of the Renunciations on a look-back basis by itemizing those Renunciations on line 61 of the T101A forms.

[10] The description on form T101A for the Renunciations at line 60 and line 61 are as follows:

Line 60 “Expenses incurred to the effective date of renunciation”

Line 61 “Expenses incurred or to be incurred in year 2(*) and renounced
under the look-back rule”

(*) Year 1 being the year in which the relevant FTS Agreements were signed or the warrants were exercised as applicable.

[11] The Appellant claimed Look-Back Renunciations in all but three of its filings during the Period.

[12] In each calendar year of the Period, Look-Back Renunciations were made to shareholders who were not at arm’s length with the Appellant. The parties agreed that, at the time the Appellant made the Look-Back Renunciations, it was not aware that paragraph 66(12.66)(d) of the *Act* required that Look-Back Renunciations be made to arm’s length shareholders only.

[13] The Appellant did not file returns under Part XII.6 of the *Act* for any of the years and it did not remit any amount on account of Part XII.6 tax liability for the 2002, 2003, 2004, 2005 and 2006 calendar years by February 29, 2004, February

28, 2005, February 28, 2006, February 28, 2007 and February 29, 2008, respectively.

[14] The CRA audited the Appellant and denied the Look-Back Renunciations which had been made to non-arm's length shareholders. The auditor prepared T101B forms to reduce the Look-Back Renunciations pursuant to subsection 66(12.73) and he requested that the Appellant sign and file these forms.

[15] The Appellant then late-filed renunciations of CEE to the non-arm's length shareholders, which renunciations were effective in the year the expenses were actually incurred. The Appellant paid the related late-filing penalty with respect to those renunciations.

[16] On May 19, 2010, the Minister of National Revenue (the "Minister") assessed the Appellant's income tax liability under Part XII.6 of the *Act* for each of the calendar years in the Period and she assessed penalties pursuant to section 162(1). The total amount of the assessments was \$573,974.

[17] On October 23, 2013, the Minister reassessed the Appellant for the 2002 and 2003 years. The amount of Part XII.6 tax was reduced by \$18,542 and the subsection 162(1) penalties were reduced by \$3,152.

[18] At the hearing of this appeal, counsel for the Respondent conceded that the amount of taxes assessed under Part XII.6 was incorrect. In the initial assessment, Part XII.6 tax had erroneously been assessed on all of the Renunciations made by the Appellant whereas they should have been assessed on only the Look-Back Renunciations. As a result, the amount of Part XII.6 tax is reduced by \$64,723, \$22,597 and \$4,502 in the 2004, 2005 and 2007 years and the subsection 162(1) penalties are reduced by \$15,610. By my calculations, after the concessions, the total amount of taxes and penalties at issue in this appeal is \$444,848.

Issue

[19] The issue in this appeal is whether the Appellant is required to pay tax pursuant to Part XII.6 of the *Act* on the Look-Back Renunciations under subsection 66(12.66) which were invalid. The answer to this question depends on the meaning of the phrase "purported to renounce" in section 211.91.

Scheme of the *Act* with respect to Flow-Through Shares

[20] Flow-through shares have been used by resource companies for many years as a method of financing their exploration activities. By issuing flow-through shares to its investors, a resource company gives its investors the opportunity to obtain tax deductions associated with exploration and development expenditures. Because “the flow-through shares are tax-assisted financing instruments”¹, there are numerous conditions associated with their issue.

[21] The relevant provisions of the *Act* are subsections 66(12.6), 66(12.61), 66(12.66), 66(15), 66(12.73) and Part XII.6 (section 211.91). I have included a copy of these provisions at Appendix B to my reasons. Counsel for the Respondent summarized these provisions in his Written Submissions and I have used portions of his summary to describe the criteria in each of the relevant sections.

[22] A Principal Business Corporation can renounce CEE pursuant to subsection 66(12.6) of the *Act* if it satisfies the requirements in the related provisions in section 66 of the *Act*.

[23] A flow-through share must be issued in accordance with subsection 66(15). It requires that:

- a) The share is issued by a Principal Business Corporation;
- b) It must not be a prescribed share;
- c) It must be issued to a person pursuant to an agreement in writing between the person and the corporation;
- d) It must be issued for consideration that does not include property to be exchanged or transferred by the person under the agreement in circumstances where any of sections 51, 85, 85.1, 86 or 87 apply;
- e) The corporation agrees to incur and renounce qualifying expenditures within a specified time frame; and,
- f) The amount agreed to be renounced cannot exceed the consideration for the share.

[24] According to subsection 66(12.6), a Principal Business Corporation can renounce CEE it incurs to a person who acquires a flow-through share of the corporation if the following conditions are met:

- a) The person and the corporation have entered into an agreement under which the corporation agrees to issue flow-through shares to the person in exchange for consideration;
- b) The person has given that consideration to the corporation;
- c) The corporation has incurred CEE during the period commencing on the day the agreement was made and ending 24 months after the end of the month in which the agreement was reached;
- d) The corporation has filed with the Minister the documents required by subsection 66(12.68) in respect of the shares;
- e) The corporation has, in respect of the share and before March of the first year that begins after the above mentioned 24 month period, renounced the CEE;
- f) The renunciation is effective on the day on which it is made or on such earlier day as may be set out in the form prescribed for the purposes of subsection 66(12.7);
- g) The renunciation is to a person in respect of a flow-through share and is in an amount of CEE incurred by it during that period on or before the effective day of the renunciation;
- h) The amount of the CEE which may be renounced are those incurred by the corporation on or before the effective date of the renunciation which exceeds the total of the following amounts;
 - i. assistance received or receivable by the corporation from any person, including any government or public authority;
 - ii. any expenses that are prescribed Canadian exploration and development overhead expenses, as defined in section 1206 of the *Regulations*;
 - iii. costs of, or for the use of seismic data acquired before the cost was incurred; and,

- iv. the total of all other amounts previously renounced in respect of those expenses under subsection 66(12.6) of the *Act*.
- i) The amount of CEE renounced in respect of the flow-through share cannot exceed the consideration paid for the share less the total of the CEE, Canadian Development and Canadian Oil and Gas Property Expenses previously renounced in respect of that share; and,
- j) The amount of CEE renounced cannot exceed the amount by which the corporation's cumulative CEE on the effective date of the renunciation exceeds the aggregate of all amounts of CEE previously renounced in respect of any other shares.

[25] The effect of a renunciation of CEE is given in subsection 66(12.61). It provides that the person, to whom the renunciation is made, is deemed to have incurred the expenses in the amount of the renunciation on the effective date of the renunciation. The corporation is deemed, on and after the effective date of the renunciation, never to have incurred the expenses.

[26] Usually a corporation may renounce only CEE that are incurred by it on or before the effective date of the renunciation. However, subsection 66(12.66) of the *Act* allows a corporation to renounce CEE that have not yet been incurred. Subsection 66(12.66) accomplishes this by deeming the corporation to have incurred the CEE on the last day of the year preceding that in which the CEE was actually incurred.

[27] In order for the Look-Back rule in subsection 66(12.66) to apply, the corporation must satisfy the following conditions:

- a) The flow-through share agreement is made in the year preceding the year in which the CEE is incurred;
- b) The expenses incurred qualify as CEE or CDE;
- c) The consideration for the flow-through share is paid before the end of that preceding year;
- d) The corporation and shareholder deal at arm's length throughout the calendar year of the renunciation;

- e) The renunciations are required to be made in January, February or March of a calendar year on the basis of CEE that the corporation plans to incur later in the year; and,
- f) If these conditions are met, the effective date of the renunciation is the last day of that preceding year.

[28] A consequence of making a claim under subsection 66(12.66) of the *Act* is that a corporation that makes a renunciation under this subsection is liable to tax under Part XII.6 of the *Act*. Section 211.91 in Part XII.6 of the *Act* imposes a tax on corporations that “purported to renounce” an amount in a calendar year under subsection 66(12.66).

[29] The tax in subsection 211.91(1) is in respect of each month, other than January, in the year of the purported renunciation in respect of CEE that were renounced but not incurred before the end of that month. As well, there is an additional tax of 10% on any amounts purportedly renounced but not incurred by the corporation by the end of December in the year of renunciation. The tax under Part XII.6 is calculated according to a formula contained in section 211.91.

[30] A corporation that has paid Part XII.6 tax or has Part XII.6 tax payable in a year is entitled to deduct that amount from income for the year pursuant to paragraph 20(1)(nn) of the *Act*.

Position of the Parties

Appellant

[31] It is the Appellant’s position that where one or more of the conditions in subsection 66(12.66) are not met, then this subsection will not have application and no amount will be included in Clause A in the formula contained in section 211.91. As a result, there will be no tax imposed by section 211.91.

[32] Counsel for the Appellant argues that the phrase “purported to renounce” in section 211.91 should be interpreted to mean “had the effect of renouncing”. She stated that the term “purport” has been defined in the jurisprudence in two conflicting ways. *Black’s Law Dictionary* defines the verb “purport” to mean “to profess or claim, esp. falsely; to seem to be”. It is counsel’s view that the more appropriate definition was used by Lord Denning in *Joseph v Joseph*, [1963] 3 All ER 486 at 490 where he stated:

The word “purports” ... does not mean “professes”. It means “has the effect of”.

Similarly, Lord Justice Russell noted the following at page 493 of *Joseph v Joseph (supra)*:

There was some discussion on the words “purports to”. For my part I would give a narrow construction to that phrase in this context; one meaning I take to be “to have as its effect”, and this seems to be a suitable meaning when the statute is avoiding an agreement and, therefore, is presumably aimed at its effect.

[33] The Appellant then argues that if the phrase “purported to renounce” in section 211.91 is replaced with “had the effect of renouncing”, then it can be seen that Clause A in the formula would only apply where the renunciation was effectively made in the year under subsection 66(12.6) or 66(12.601) because of the application of 66(12.66).

[34] Counsel for the Appellant undertook a textual, contextual and purposive approach to section 211.91 of the *Act* and she concludes that the section is not meant to apply in situations like the present. Rather, “it is part of a statutory scheme designed to allow for the smooth functioning of the look-back rules and to compensate the fisc for allowing investors to deduct expenses before they are actually incurred. Here, investors were not given that benefit. The imposition of tax is therefore inappropriate and operates as a penalty” which was not its intended use.

Respondent

[35] It is the Respondent’s position that a corporation that claims to renounce CEE pursuant to subsection 66(12.66) is subject to tax under Part XII.6 on all purported renunciations made under that subsection.

[36] Counsel for the Respondent also undertook a textual, contextual and purposive analysis to section 211.91. He relies on the definition of “purport” in *Black’s Law Dictionary* (given above) and the definition of “purport” in the *Oxford English Dictionary* which reads –

b. Esp. of a document, picture, or object: (originally, without implied doubt as to the validity of the claim) to seem; (in later use) to profess or claim by its tenor, be intended to seem, appear ostensibly to be or do something. (Now the usual sense.)

[37] Counsel states that the term “purported” refers to a claim that is not necessarily true or correct, but is held out as being true. Something that is “purported” makes the implication of a claim without reference to the accuracy of the claim.

[38] The Respondent concludes that according to the Appellant’s interpretation of the phrase “purported to renounce”, only a successful claim under subsection 66(12.66) would attract tax under section 211.91. If this was the intent of the legislators, it would have been sufficient for them to restrict Part XII.6 tax to claims made pursuant to the terms of subsection 66(12.66) without using the phrase “purported to renounce”. The Appellant’s interpretation would render the phrase “purported to renounce” superfluous.

Analysis

[39] Subsection 66(12.66) of the *Act* is a deeming provision. It provides that where a number of conditions are met, “the corporation is, for the purpose of subsection (12.6) or of subsection (12.601) and paragraph (12.602)(b), as the case may be, deemed to have incurred the expenses on the last day of the year”. One of the conditions in the subsection is that the Look-Back Renunciations must be made to arm’s length parties. It is agreed that this provision was not met for the following Look-Back Renunciations:

TIN #	AMOUNT
02-30542-5	\$800,000
02-31225-6	\$835,000
03-31361-9	\$700,000
03-32541-5	\$1,500,000
04-33938-2	\$250,000
05-35388-8	\$1,250,000
06-37487-6	\$850,000

[40] In interpreting the phrase “purported to renounce” in section 211.91, it is agreed that the section must be interpreted with regard to its text, context and purpose, harmoniously with the scheme and object of the *Act* as a whole: *Canada Trustco Mortgage Co v The Queen*, 2005 SCC 54 at paragraph 10, *Placer Dome Canada Ltd v Ontario (Minister of Finance)*, 2006 SCC 20 at paragraphs 21-22.

Textual

[41] The parties have relied on different dictionaries and different cases for the meaning they attach to the verb “purport”. It is apparent that the verb “purport” can have very different meanings depending on its use in a sentence and its context in the *Act*. Appellant’s counsel argues that the meaning to be given to “purport” is “has the effect of”. She then states that the phrase “purported to renounce” means “had the effect of renouncing” and Clause A in the formula in section 211.91 would only apply where the renunciation was effectively made in the year under subsection 66(12.6) or 66(12.601) because of the application of 66(12.66).

[42] However, it is my view that such an interpretation of “purport” makes no sense when this definition is used within the entire sentence. It is clear that “an amount purported to be renounced in respect of expenses incurred or to be incurred” must refer to an amount “claimed” to be renounced or “intended” to be renounced whether the claim is true or not. This interpretation is supported by the French version of section 211.91. There, the phrase “censément renoncé” is used and it generally means “supposedly renounced” or “apparently renounced”.

[43] The Appellant’s interpretation of the phrase “purported to renounce” in section 211.91 renders the word “purported” redundant. If the legislators intended that section 211.91 only applied where the corporation effectively renounced an amount, they could have achieved this goal by simply omitting the word purport. However, the rule against tautology makes it clear that all words in a statute must be given meaning: *Canada (Canadian Human Rights Commission) v Canada (Attorney General)*, 2011 SCC 53 at paragraph 38.

[44] With respect to the text of the section, it is my view that the phrase “purported to renounce” means “claimed to renounce” whether or not the claim is true.

Contextual

[45] When the phrase “purported to renounce” in section 211.91 is considered within the context of the scheme for flow-through shares in the *Act*, it is apparent that the phrase does not just refer to CEE that is effectively renounced as the Appellant contends. The phrase refers to CEE that the corporation claimed to renounce, whether the claim turns out to be true or not.

[46] Subsection 66(12.6) allows a principal business corporation to renounce CEE it has incurred to a person who has purchased flow-through shares. The *Act* accomplishes this by creating a legal fiction. According to subsection 66(12.61),

the effect of the renunciation is that the person is deemed to have incurred the CEE on the effective date of the renunciation and the corporation is deemed never to have incurred the CEE.

[47] Subsection 66(12.66) allows a corporation to renounce CEE that it has not yet incurred. In effect, it permits a corporation to back-date the expenses so that the shareholder can deduct amounts with respect to the CEE in the year prior to their being incurred. These are CEE that the corporation anticipates it will incur and “purports to renounce”. Clearly, this is a claim the corporation is making which may or may not be true.

[48] When the amount the corporation “purports to renounce” is excessive, subsection 66(12.73) of the *Act* stipulates that the corporation must make an adjustment to the amount of CEE renounced. The opening words of that subsection read:

Where an amount that a corporation purports to renounce to a person under subsection 66(12.6), 66(12.601) or 66(12.62) exceeds the amount that it **can renounce to the person** under that subsection... (**emphasis added**)

[49] It is my view that this subsection applies to the facts in this appeal. Here, the Appellant purported to renounce an amount of CEE to non-arms’ length persons who were not eligible recipients under paragraph 66(12.66)(d). Therefore, the amount renounced exceeded the amount that the corporation **can renounce** to those persons.

[50] Subsection 66(12.73) explicitly addresses renunciations made under subsection 66(12.66). It states that where **excessive renunciations** are made using the look-back rule, the corporation must file a prescribed form with the CRA in which it reduces the purported renunciations. The reduced renunciations are deemed to have always applied except for the purposes of the tax under Part XII.6. See paragraphs 66(12.73)(d) and (e). The corporation’s tax liability under Part XII.6 is based on the total CEE claimed to be renounced in the initial form filed by the corporation with the CRA.

[51] In this case, the Appellant filed the form prescribed by subsection 66(12.73) to reduce the CEE it renounced under subsection 66(12.66). In accordance with paragraphs 66(12.73)(d) and (e), the Appellant is liable to pay tax under Part XII.6 for the total CEE originally claimed on a look-back basis.

[52] If a corporation reduces the CEE it has renounced because it failed to incur the amount of CEE, the arm's length investors who were supposed to receive the benefit of the renunciations are entitled to interest relief under subsection 161(6.2). According to the definition of "specified future tax consequence" in section 248, non-arm's length investors do not get this interest relief.

Purpose

[53] Part XII.6 of the *Act* was enacted when subsection 66(12.66) was amended to extend the "look-back" period from the 60th day of a calendar year to the end of that year. According to the Technical Notes for section 211.91, the purpose of this new tax is to compensate "the fisc for the acceleration of the deduction resulting from the application of subsection 66(12.66) of the *Act*".

[54] Although Technical Notes are not binding interpretations of the provisions at issue, they offer useful insight of Parliament's intent when the sections were enacted. In this case, the words of the *Act* are in accord with the purpose stated in the Technical Notes for section 211.91.

[55] The formula for the calculation of Part XII.6 tax is found in subsection 211.91(1). The tax is calculated on a monthly basis in the year after the renunciation. It is the amount renounced minus the expenses actually incurred, multiplied by the prescribed rate of interest. The tax is essentially an interest charge as described by the Technical Notes. In addition, there is a 10% fee administered on any CEE renounced by the corporation that was not incurred by the end of the year.

[56] It is my view that the application of Part XII.6 tax in the present circumstances supports this stated purpose. During the Period, the Appellant made Look-Back Renunciations to shareholders who obtained the benefit of the CEE deductions in the year prior to their being actually incurred. This resulted in a cost to the fisc which the Appellant had to pay in accordance with Part XII.6.

[57] It is clear that the tax under Part XII.6 is calculated on "the total of all amounts each of which is an amount that the corporation purported to renounce in the year". I agree with the Appellant that my interpretation of the phrase "purported to renounce" may be punitive to the non-arm's length shareholders. Although they were initially allowed a deduction, it was adjusted for the year claimed and was allowed in a subsequent year. This presumably lead to an increase in tax owing for the shareholders in the prior years. In addition, interest would be

owed under subsection 161(1) on the excess tax and the non-arm's length shareholders would not receive interest relief under subsection 161(6.2).

[58] However, it is my view that this is an intentional consequence of the provisions of the *Act*. Subsection 66(12.73) specifically states that adjustments to renunciations do not affect the amount of Part XII.6 tax. Likewise, subsection 161(6.2) allows for interest relief only where paragraph (b) of the definition specified future tax consequence in section 248 is met. Paragraph (b) of this definition specifies that the Look-Back Renunciation must be made to an arm's length party.

[59] Although the Technical Notes do shed light on Parliament's intention in enacting Part XII.6 of the *Act*, it is not determinative of the interpretation to be given to the phrase "purported to renounce" in section 211.91.

Conclusion

[60] I have concluded that the Appellant is liable for Part XII.6 tax on all Look-Back Renunciations it made in its 2002, 2003, 2004, 2005 and 2006 taxation years.

[61] The appeal is allowed only to the extent of the concessions made by the Respondent. In all other respects, the appeal is dismissed.

[62] The parties have thirty days from the date on the Judgment to make submissions with respect to costs. If no submissions are made, the Respondent is entitled to costs according to the tariff.

Signed at Ottawa, Canada, this 26th day of October 2016.

"V.A. Miller"

V.A. Miller J.

¹ Canada Tax Service, McCarthy Tetrault Analysis, 211.91

Appendix A

AGREED STATEMENT OF FACTS AND DOCUMENTS

The parties agree to and admit the following facts for the purpose of these appeals. The parties may adduce further evidence at trial that is relevant to the issues in these appeals, provided that the evidence is not contrary to this statement of facts.

All references to the Joint Book of Documents are to the documents that form part of this statement and, together with it, are to be marked as exhibits AR1 and AR2, respectively, at the beginning of the hearing of these appeals. The parties agree as to the authenticity (as provided in section 129 of the *Tax Court of Canada Rules (General Procedure)* of these documents.

The Appellant

1. At all material times:
 - a. the Appellant was a Canadian Controlled Private Corporation as that term is defined in subsections 248(1) and 125(7) of the Income Tax Act (the “Act”);
 - b. the Appellant was a Principal Business Corporation as that term is defined in subsection 66(15) of the Act; and
 - c. the Appellant had a December 31st year-end for tax purposes.

Flow-through shares

2. The Appellant issued flow-through shares (the “Shares”) to a number of investors in and around its 2002, 2003, 2004, 2005 and 2006 taxation years (the “Relevant Period”).
3. The Shares were issued pursuant to agreements in writing entered into between the Appellant and the respective shareholders for the issue of flow-through shares of the Appellant.

Look-back Renunciations

4. Throughout the Relevant Period, the Appellant was unaware that early renunciations of Canadian exploration expenses (“CEE”) under subsection 66(12.66) of the Act (“Look back Renunciations”) could be made only to arm’s length persons.

5. The Appellant filed forms to renounce the following CEE (collectively, the “Renunciations”) to holders of the Shares effective the following dates and under the following information numbers:

TIN#	Effective Date	Total CEE renounced under s.66(12.6)
02-30542-5	June 30, 2002	\$800,000
02-31225-6	December 31, 2002	\$860,000
03-31361-9	January 31, 2003	\$700,000
03-31610-9	June 30, 2003	\$2,500,000
03-32541-5	December 31, 2003	\$1,545,000
04-33938-2	December 31, 2004	\$275,000
04-34021-6	June 30, 2004	\$1,500,000
05-35388-8	December 31, 2005	\$1,260,000
06-36179-0	December 31, 2006	\$450,000
06-37487-6	December 31, 2006	\$910,000
	TOTAL	\$10,800,000

6. Certain of the Renunciations were Look-back Renunciations in respect of CEE that the Appellant had not yet incurred as of the effective date of the Renunciations.
7. Look-back Renunciations were made in each calendar year of the Relevant Period to flow-through share investors with whom, in many instances, the Appellant did not deal at arm’s length.
8. Canada Revenue Agency denied certain Look-back Renunciations after an audit because subsection 66(12.66) of the Act required the parties to be in an arm’s length relationship.
9. The Appellant late-filed renunciations of CEE to the non-arm’s length flow-through share investors. These late-filed renunciations were effective as of the time when the expenses were actually incurred. The Appellant paid the related late filing penalties in respect of those renunciations.

Filings

10. The Appellant filed T101A forms with the Minister for each respective Renunciation which set out, among other things, the amount of the Renunciations.
11. In its filings, the Appellant:
 - a. claimed \$6,350,000 of the Renunciations on a look-back basis by itemizing those Renunciations on line 61 of the T101A forms; and
 - b. claimed \$4,450,000 of the Renunciations on line 60 of the T101A forms.
12. Upon learning that the prerequisites for Look-back Renunciations were not met in respect of the Renunciations, the Appellant late-filed renunciations of CEE to the non-arm's length flow-through share investors and paid the related late-filing penalty.
13. The Appellant did not file returns under Part XII.6 of the Act and did not remit any amount on account of its Part XII.6 tax liability for the 2002, 2003, 2004, 2005 and 2006 calendar years by February 29, 2004, February 28, 2005, February 28, 2006, February 28, 2007 and February 29, 2008, respectively.

Assessments

14. By Notices of Assessment dated May 19, 2010 (the "Assessments"), the Minister of National Revenue (the "Minister") assessed the Appellant under Part XII.6 of the Act for the 2002, 2003, 2004, 2005 and 2006 taxation years, plus penalties under subsection 162(1) of the Act in the aggregate amount of \$573,974.
15. The basis of the Assessments is that the Appellant had purported to renounce certain amounts to non-arm's length flow-through share investors under subsection 66(12.6) because of the application of subsection 66(12.66) and was therefore liable to Part XII.6 tax, which is disputed by the Appellant.
16. The Minister treated all such Renunciations as being claimed on a look-back basis.
17. On October 23, 2013, the Minister issued reassessments (the "Reassessments") in respect of the Part XII.6 assessments for the 2002 and 2003 years. As a result of the

Reassessments, the previously assessed Part XII.6 tax was reduced by \$18,542 and the penalties under subsection 162(1) of the Act were reduced by \$3,152.

Calculation of Part XII.6 Tax and Penalty

18. The Minister calculated the Part XII.6 tax according to the formula described in Schedules “C”, “D”, “E”, “F”, “G”, “H”, “I”, “J”, “K” and “L” of the Reply to the Amended Notice of Appeal, after taking into account the timing of the Appellant’s CEE incurred.
19. In the 2003 calendar year, the prescribed interest rate for the purposes of subsection 164(3) of the Act, for each month from February to December inclusive, was 5% per annum for February, March, April, May, June, October, November and December, and 6% per annum for July, August and September.
20. In the 2004 calendar year, the prescribed interest rate for the purposes of subsection 164(3) of the Act, for each month from February to December inclusive, was 5% per annum for February, March, April, May, June, October, November and December, and 4% per annum for July, August and September.
21. In the 2005 calendar year, the prescribed interest rate for the purposes of subsection 164(3) of the Act, for each month from February to December inclusive, was 5% per annum.
22. In the 2006 calendar year, the prescribed interest rate for the purposes of subsection 164(3) of the Act, for each month from February to December inclusive, was 5% per annum for February and March, 6% per annum for April, May, June, July, August, and September, and was 7% per annum for October, November and December.
23. In the 2007 calendar year, the prescribed interest rate for the purposes of subsection 164(3) of the Act, for each month from February to December inclusive, was 7% per annum.

Appendix B

66(12.6) If a person gave consideration under an agreement to a corporation for the issue of a flow-through share of the corporation and, in the period that begins on the day on which the agreement was made and ends 24 months after the end of the month that includes that day, the corporation incurred Canadian exploration expenses (other than an expense deemed by subsection 66.1(9) to be a Canadian exploration expense of the corporation), the corporation may, after it complies with subsection (12.68) in respect of the share and before March of the first calendar year that begins after the period, renounce, effective on the day on which the renunciation is made or on an earlier day set out in the form prescribed for the purpose of subsection (12.7), to the person in respect of the share the amount, if any, by which the portion of those expenses that was incurred on or before the effective date of the renunciation (which portion is in this subsection referred to as the “specified expenses”) exceeds the total of

- (a) the assistance that the corporation has received, is entitled to receive or can reasonably be expected to receive at any time, and that can reasonably be related to the specified expenses or to Canadian exploration activities to which the specified expenses relate (other than assistance that can reasonably be related to expenses referred to in paragraph 66(12.6)(b) or 66(12.6)(b.1)),
- (b) all specified expenses that are prescribed Canadian exploration and development overhead expenses of the corporation,
- (b.1) all specified expenses each of which is a cost of, or for the use of, seismic data
 - (i) that had been acquired (otherwise than as a consequence of performing work that resulted in the creation of the data) by any other person before the cost was incurred,
 - (ii) in respect of which a right to use had been acquired by any other person before the cost was incurred, or
 - (iii) all or substantially all of which resulted from work performed more than one year before the cost was incurred, and
- (c) the total of amounts that are renounced on or before the date on which the renunciation is made by any other renunciation under this subsection 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 under this subsection or subsection 66(12.601) or 66(12.62) in respect of the share on or before the day on which the renunciation is made, or
- (e) exceeding the amount, if any, by which the cumulative Canadian exploration expense of the corporation on the effective date of the renunciation computed before taking into account any

amounts renounced under this subsection on the date on which the renunciation is made, exceeds the total of all amounts renounced under this subsection in respect of any other share

- (i) on the date on which the renunciation is made, and
- (ii) effective on or before the effective date of the renunciation.

Effect of renunciation

(12.61) Subject to subsections 66(12.69) to 66(12.702), where under subsection 66(12.6) or 66(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.

Expenses in the first 60 days of year [or throughout next calendar year]

66(12.66) Where

- (a) a corporation that issues a flow-through share to a person under an agreement incurs, in a particular calendar year, Canadian exploration expenses or Canadian development expenses,
 - (a.1) the agreement was made in the preceding calendar year,
 - (b) the expenses
 - (i) are described in paragraph (a), (d), (f) or (g.1) of the definition Canadian exploration expense in subsection 66.1(6) or paragraph (a) or (b) of the definition Canadian development expense in subsection 66.2(5),
 - (ii) would be described in paragraph (h) of the definition Canadian exploration expense in subsection 66.1(6) if the reference to “paragraphs (a) to (d) and (f) to (g.4)” in that paragraph were read as “paragraphs (a), (d), (f) and (g.1)”, or
 - (iii) would be described in paragraph (f) of the definition Canadian development expense in subsection 66.2(5) if the words “any of paragraphs 66(12.66)(a) to (e)” were read as “paragraph 66(12.66)(a) or (b)”,
- (c) before the end of that preceding year the person paid the consideration in money for the share to be issued,

- (d) the corporation and the person deal with each other at arm's length throughout the particular year, and
- (e) in January, February or March of the particular year, the corporation renounces an amount in respect of the expenses to the person in respect of the share in accordance with subsection 66(12.6) or 66(12.601) and the effective date of the renunciation is the last day of that preceding year,

the corporation is, for the purpose of subsection (12.6), or of subsection (12.601) and paragraph (12.602)(b), as the case may be, deemed to have incurred the expenses on the last day of that preceding year.

66(12.73) Where an amount that a corporation purports to renounce to a person under subsection 66(12.6), 66(12.601) or 66(12.62) exceeds the amount that it can renounce to the person under that subsection,

- (a) the corporation shall file a statement with the Minister in prescribed form where
 - (i) the Minister sends a notice in writing to the corporation demanding the statement, or
 - (ii) the excess arose as a consequence of a renunciation purported to be made in a calendar year under subsection 66(12.6) or 66(12.601) because of the application of subsection 66(12.66) and, at the end of the year, the corporation knew or ought to have known of all or part of the excess;
- (b) where subparagraph 66(12.73)(a)(i) applies, the statement shall be filed not later than 30 days after the Minister sends a notice in writing to the corporation demanding the statement;
- (c) where subparagraph 66(12.73)(a)(ii) applies, the statement shall be filed before March of the calendar year following the calendar year in which the purported renunciation was made;
- (d) except for the purpose of Part XII.6, any amount that is purported to have been so renounced to any person is deemed, after the statement is filed with the Minister, to have always been reduced by the portion of the excess identified in the statement in respect of that purported renunciation; and
- (e) where a corporation fails in the statement to apply the excess fully to reduce one or more purported renunciations, the Minister may at any time reduce the total amount purported to be renounced by the corporation to one or more persons by the amount of the unapplied excess in which case, except for the purpose of Part XII.6, the amount purported to have been so renounced to a person is deemed, after that time, always to have been reduced by the portion of the unapplied excess allocated by the Minister in respect of that person.

Definitions

66(15) In this section,

flow-through share means a share (other than a prescribed share) of the capital stock of a principal-business corporation, or a right (other than a prescribed right) to acquire a share of the capital stock of a principal-business corporation, issued to a person under an agreement in writing made between the person and the corporation under which the corporation, for consideration that does not include property to be exchanged or transferred by the person under the agreement in circumstances to which any of sections 51, 85, 85.1, 86 and 87 applies, agrees

- (a) to incur, in the period that begins on the day on which the agreement was made and ends 24 months after the month that includes that day, Canadian exploration expenses or Canadian development expenses in an amount not less than the consideration for which the share or right is to be issued, and
- (b) to renounce, in prescribed form and before March of the first calendar year that begins after that period, to the person in respect of the share or right, an amount in respect of the Canadian exploration expenses or Canadian development expenses so incurred by it not exceeding the consideration received by the corporation for the share or right; (action accréditive)

PART XII.6 Tax on Flow-through Shares

Tax imposed

Section 211.91 reads:

- 211.91 (1) Every corporation shall pay a tax under this Part in respect of each month (other than January) in a calendar year equal to the amount determined by the formula

$$(A + B/2 - C - D/2) \times (E/12 + F/10)$$

where

A

is the total of all amounts each of which is an amount that the corporation purported to renounce in the year under subsection 66(12.6) or 66(12.601) because of the application

- 211.91 (1) Toute société doit payer en vertu de la présente partie pour chaque mois, sauf janvier, d'une année civile un impôt égal au résultat du calcul suivant :

$$(A + B/2 - C - D/2) \times (E/12 + F/10)$$

où :

A

représente le total des montants représentant chacun un montant auquel elle a censément renoncé au cours de

of subsection 66(12.66) (other than an amount purported to be renounced in respect of expenses incurred or to be incurred in connection with production or potential production in a province where a tax, similar to the tax provided under this Part, is payable by the corporation under the laws of the province as a consequence of the failure to incur the expenses that were purported to be renounced); (emphasis added)

B

is the total of all amounts each of which is an amount that the corporation purported to renounce in the year under subsection 66(12.6) or 66(12.601) because of the application of subsection 66(12.66) and that is not included in the value of A;

C

is the total of all expenses described in paragraph 66(12.66)(b) that are

- o (a) made or incurred by the end of the month by the corporation, and
- o (b) in respect of the purported renunciations in respect of which an amount is included in the value of A;

l'année en vertu des paragraphes 66(12.6) ou (12.601) par l'effet du paragraphe 66(12.66), à l'exception d'un montant auquel il a censément été renoncé au titre de frais engagés ou à engager relativement à la production réelle ou éventuelle dans une province où un impôt, semblable à celui prévu par la présente partie, est payable par la société aux termes des lois provinciales par suite du défaut d'engager les frais auxquels il a censément été renoncé;(emphasis adjoute)

B

le total des montants représentant chacun un montant auquel elle a censément renoncé au cours de l'année en vertu des paragraphes 66(12.6) ou (12.601) par l'effet du paragraphe 66(12.66) et qui n'est pas inclus dans la valeur de l'élément A;

C

le total des frais visés à l'alinéa 66(12.66)b) qui, à la fois :

- o a) sont engagés ou effectués par la société au plus tard à la fin du mois,
- o b) se rapportent aux renoncations censément effectuées et relativement auxquelles un montant est inclus dans la valeur de l'élément A;

D

is the total of all expenses described in paragraph 66(12.66)(b) that are

- o (a) made or incurred by the end of the month by the corporation, and
- o (b) in respect of the purported renunciations in respect of which an amount is included in the value of B;

E

is the rate of interest prescribed for the purpose of subsection 164(3) for the month; and

F

is

- o (a) one, where the month is December, and
- o (b) nil, in any other case.
- Return and payment of tax

(2) A corporation liable to tax under this Part in respect of one or more months in a calendar year shall, before March of the following calendar year,

- o (a) file with the Minister a return for the year under this Part in prescribed form containing an estimate of the tax payable under this

D

le total des frais visés à l'alinéa 66(12.66)b qui, à la fois :

- o a) sont engagés ou effectués par la société au plus tard à la fin du mois,
- o b) se rapportent aux renoncations censément effectuées et relativement auxquelles un montant est inclus dans la valeur de l'élément B;

E

le taux d'intérêt prescrit pour le mois pour l'application du paragraphe 164(3);

F

:

- o a) un, si le mois en question est décembre,
- o b) zéro, dans les autres cas.
- Déclaration et paiement de l'impôt

(2) La société redevable de l'impôt prévu par la présente partie pour un ou plusieurs mois d'une année civile doit, avant mars de l'année civile subséquente :

- o a) présenter au ministre, sur le formulaire prescrit, une déclaration pour l'année en vertu de la présente partie contenant une estimation de son impôt payable en vertu

Part by it in respect of each month in the year; and

de cette partie pour chaque mois de l'année;

o b) verser cet impôt au receveur général.

o (b) pay to the Receiver General the amount of tax payable under this Part by it in respect of each month in the year.

•Dispositions applicables

(3) Les paragraphes 150(2) et (3), les articles 152, 158 et 159, les paragraphes 161(1) et (11), les articles 162 à 167 et la section j de la partie I s'appliquent à la présente partie, avec les adaptations nécessaires.

• Provisions applicable to Part

(3) Subsections 150(2) and 150(3), sections 152, 158 and 159, subsections 161(1) and 161(11), sections 162 to 167 and Division J of Part I apply to this Part, with any modifications that the circumstances require.

Interest

Flow-through share renunciations

161(6.2) Where the tax payable under this Part by a taxpayer for a taxation year is more than it otherwise would be because of a consequence for the year described in paragraph (b) of the definition specified future tax consequence in subsection 248(1) in respect of an amount purported to be renounced in a calendar year, for the purposes of the provisions of this Act (other than this subsection) relating to interest payable under this Act, an amount equal to the additional tax payable is deemed

• (a) to have been paid on the taxpayer's balance-due day for the taxation year on account of the taxpayer's tax payable under this Part for the year; and

• (b) to have been refunded on April 30 of the following calendar year to the taxpayer on account of the taxpayer's tax payable under this Part for the taxation year.

Section 248

specified future tax consequence for a taxation year means

- **(a)** the consequence of the deduction or exclusion of an amount referred to in paragraph 161(7)(a),

- **(b)** the consequence of a reduction under subsection 66(12.73) of a particular amount purported to be renounced by a corporation after the beginning of the year to a person or partnership under subsection 66(12.6) or 66(12.601) because of the application of subsection 66(12.66), determined as if the purported renunciation would, but for subsection 66(12.73), have been effective only where
 - (i)** the purported renunciation occurred in January, February or March of a calendar year,

 - (ii)** the effective date of the purported renunciation was the last day of the preceding calendar year,

 - (iii)** the corporation agreed in that preceding calendar year to issue a flow-through share to the person or partnership,

 - (iv)** the particular amount does not exceed the amount, if any, by which the consideration for which the share is to be issued exceeds the total of all other amounts purported by the corporation to have been renounced under subsection 66(12.6) or 66(12.601) in respect of that consideration,

 - (v)** paragraphs 66(12.66)(c) and 66(12.66)(d) are satisfied with respect to the purported renunciation, and

 - (vi)** the form prescribed for the purpose of subsection 66(12.7) in respect of the purported renunciation is filed with the Minister before May of the calendar year, and

- **(c)** the consequence of an adjustment or a reduction described in subsection 161(6.1); (conséquence fiscale future déterminée)

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