

Real Estate Donation Proposal

A 2015 federal budget proposal exempts the sale of real estate from income tax if the proceeds are donated within 30 days. (See new paragraph 38(a.4) and sections 38.3 and 38.4, released July 31, 2015.) A comment period that ended on September 30, 2015 may generate changes, but currently the proposal (1) does not address recaptured CCA arising on the sale and (2) yields a smaller donation deduction or credit than a direct donation does. The proposal also does not permit the donor to elect a reduction of sale proceeds to less than FMV, as he or she can do with a direct donation. All of these differences make the proposal problematic.

Under the proposal, a donation of the proceeds from the sale of real estate must be made to a registered charity or other qualified donee, and the exemption applies to the capital gain of an individual and a corporate donor. The property must be sold to a party at arm's length with the donor and with the qualified donee; the monetary proceeds must be donated as a gift of money within 30 days of the disposition. The exemption is calculated in proportion to the portion of proceeds donated.

The proposals apply to a disposition after calendar 2016, but anti-avoidance rules may apply. For example, the donor or a related party cannot directly or indirectly acquire the property within five years.

Recapture of CCA—the difference between the property's UCC and its FMV—on the sale or direct donation of depreciable real estate such as a building is triggered whether or not the proposed exemption or a direct donation applies. In effect, however, recapture may not be taxed in part or at all because of the donation deduction or credit that applies to a direct donation or to the donation of sale proceeds.

The proposal does not change the general rule on the extent of the donation deduction or credit: both the corporate deduction and the individual credit (paragraph 110.1(1)(a) and subsection 118.1(3), respectively) can be claimed in the year that the gift is made, or they can be carried forward five years. (The Quebec corporate carryforward is 20 years: see section 710 of the Quebec Taxation Act.) The deduction or credit is limited to 75 percent of the donor's net income; the same limit applies for a direct donation and under the proposal. However, for a direct donation of capital property only, the limit on the deduction or credit is increased by an additional 25 percent of the taxable capital gain and 25 percent of the recapture. Furthermore, the capital gain on the direct donation of ecologically sensitive real estate is not taxable (except for a direct donation to a private foundation; see paragraph 38(a.2)). The greater deduction and credit associated with such a direct donation is limited to 100 percent of net income (paragraph 110.1(1)(d) and subsection 118.1(3)). Therefore, in some situations, a direct donor may pay less tax.

The election to reduce proceeds to between ACB and FMV of the property is available for a direct donation by a corporation or an individual (subsections 110.1(3) and 118.1(6), respectively) for any real estate, including ecological property. But the election is not available under the proposal, which does not allow for the consequent generation of potential tax savings that flow from using a reduced proceeds amount to calculate the capital gain and recapture. (The election, however, does reduce the eligible amount of the gift and therefore reduces the direct donation deduction or credit accordingly.)

Therefore, when deciding whether to donate real estate directly or to donate under the proposal, one must carefully consider the best way to treat the capital gain and any recapture. The proposal does not always yield a greater tax saving than the existing deduction or credit for a direct donation. Furthermore, practical issues may arise because the proposal requires that sale proceeds must be donated: for example, the seller may receive a balance of sale, and thus some proceeds may not be available to donate within 30 days of the sale.

Daniel Frajman
Spiegel Sohmer Inc., Montreal