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AUTHOR Friedlander, Lara G.
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Please note that the following document, although believed to be correct at the time of issue, may not represent the current position of the CRA. Prenez note que ce document, bien qu'exact au moment émis, peut ne pas représenter la position actuelle de l'ARC.

PRINCIPAL ISSUES: Whether interest would be deemed to accrue on a non-interest bearing loan?

POSITION: It may.

REASONS: 69(1)(a) may deem the holder to acquire the loan at a cost that is less than the principal amount.

XXXXXXXXXX

2014-053265

L. Friedlander

July 28, 2014

Dear XXXXXXXXXXXX:

Re: Loan to Charitable Foundation

This is in response to your email of May 21, 2014 concerning certain issues relating to a non-interest bearing loan to a charitable foundation.

Canco is a taxable Canadian corporation for purposes of subsections 89(1) and 248(1) of the Income Tax Act (the "Act"). Canco is related to the Foundation, a new corporation resident in Canada for purposes of the Act that engages in charitable activities. The Foundation is a "registered charity" as defined in subsection 248(1) of the Act.

Canco loans \$XXXXXXXXXX (the "Loan") to the Foundation. The Loan has a term of XXXXXXXXXXXX years and must be repaid for \$XXXXXXXXXX (i.e., the Loan was not issued at a discount). The Loan

does not carry a stipulated rate of interest. We assume that the Loan is held on capital account by Canco.

You have asked whether there would be any tax consequence for advancing money without charging interest to the Foundation and if Canco should charge interest at a prescribed rate to the Foundation. If so, you have asked what the prescribed rate is that should be charged. You have also asked whether a written agreement is necessary between Canco and the Foundation.

Our Comments

Written confirmation of the tax implications inherent in particular transactions is given by this Directorate only where the transactions are proposed and are the subject matter of an advance income tax ruling request submitted in the manner set out in Information Circular 70-6R5, Advance Income Tax Rulings, dated May 17, 2002. Also, where the particular transactions are completed, the inquiry should be addressed to the relevant Tax Services Office. Nonetheless, we have provided some general comments below.

You indicate that the Loan does not carry a stipulated rate of interest. A debt obligation that does not carry a stipulated rate of interest is a prescribed debt obligation under paragraph 7000(1)(a) of the Income Tax Regulations (the "Regulations"). Accordingly, pursuant to subsection 12(9) of the Act, Canco may be required to accrue interest on the Loan.

Whether any accrual will be required will depend on paragraph 7000(2)(a) of the Regulations. This paragraph would generally require Canco to compute deemed interest at a rate that would result in the present value of the maximum of all payments under the Loan being equal to the cost of the Loan to Canco. Where the amount payable on maturity of the Loan is equal to the cost of the Loan to Canco, paragraph 7000(2)(a) of the Regulations should not deem any interest to accrue. Where the cost of the Loan is less than the amount payable at maturity, there will be a deemed accrual under paragraph 7000(2)(a) of the Regulations.

However, because the Loan was made between two non-arm's length parties, paragraph 69(1)(a) of the Act may apply to reduce the cost of the Loan to Canco. If the Loan is not repayable at the demand of Canco, it is possible that the fair market value of the Loan could be less than the amount advanced by Canco under the Loan. If that is the case, then paragraph 69(1)(a) of the Act could deem Canco to have acquired the Loan at a cost equal to the fair market value of the Loan, triggering the deemed accrual under paragraph 7000(2)(a) of the Regulations referenced above. A reduction in the cost of the Loan under paragraph 69(1)(a) of the Act would also have consequences for the calculation of any eventual gain or loss of Canco on the disposition of the Loan, subject to the potential application of subsection 52(1) of the Act in respect of any deemed accrual under subsection 12(9) of the Act.

We do not have sufficient information to provide more definitive comments. We note that there are a number of other provisions that could be applicable to Canco or to other members of the Canco group, including benefit provisions such as subsection 15(1) of the Act. We also have not considered any aspects of the Loan that might relate to Canco's application for status as a registered charity. We trust that these comments will be of assistance.

Yours truly,

G. Moore

www.globalphilanthropy.ca

For Director
International Division
Income Tax Rulings Directorate
Legislative Policy and Regulatory Affairs Branch