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Court File No.

IN THE SUPREME COURT OF CANADA
(ON APPEAL FROM THE FEDERAL COURT OF APPEAL)

B E T W E E N:

F. MAX E. MARÉCHAUX

Applicant (Appellant)

- and -

HER MAJESTY THE QUEEN

Respondent (Respondent)

APPLICATION FOR LEAVE TO APPEAL AND MOTION FOR EXTENSION OF TIME OF THE APPLICANT (APPELLANT), F. MAX E. MARÉCHAUX, VOLUME I OF II

BAKER & MCKENZIE
Barristers and Solicitors
Brookfield Place
181 Bay Street, Suite 2100
Toronto, Ontario M5J 2T3

Matthew J. Latella (39140R)
Tel: 416-865-6985
matthew.j.latella@bakermckenzie.com

Sal Borraccia (13414B)
Tel: (416) 865-6904
sal.borraccia@bakermckenzie.com

Telecopier: (416) 863-6275

Lawyers for the Applicant

GOWLING LAFLEUR HENDERSON
Barristers and Solicitors
2600 – 160 Elgin Street
Ottawa, Ontario
K1P 1C3

Henry S. Brown, Q.C.
Telephone: (613) 233-1781
Teleopier: (613) 563-9869

Ottawa agents for the lawyers for the Applicant

VOLUME I OF II

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TABLE OF CONTENTS

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NOTICE OF APPLICATION FOR LEAVE TO APPEAL

TAKE NOTICE that the Applicant, F. Max E. Maréchaux hereby applies for leave to appeal to the Court, pursuant to Section 40(1) of the *Supreme Court Act*, as amended, and Rule 25 of the Rules *of the Supreme Court of Canada*, from the Judgment of the Federal Court of Appeal in File Number A-494-09 made October 28, 2010 and for any further or other order that the Court may deem appropriate.

AND FURTHER TAKE NOTICE that this Application for leave is made on the following grounds:

1. The decisions of the Courts below in this matter directly affect the rights of tens of thousands of Canadians across the country who have donated billions of dollars worth of charitable gifts to numerous registered charities by way of so-called "leveraged donation" arrangements and countless others who will do so in the future;

2. The learned trial Judge and appellate Justices below have embarked upon a fundamental alteration of a test established approximately 20 years ago, in *Friedberg v. Canada* [1], in which

[1] [1991] F.C.J. No. 1255, aff'd on other grounds [1993] 4 S.C.R. 285; leave to appeal re: "gift" issue dismissed [1992]

the Federal Court of Appeal set out the definition of "gift"[2], as that word is used in the statutorily defined term, "total charitable gifts" in Section 118.1 of the *Income Tax Act* (the "*Act*");

3. Since *Friedberg* was decided, it has been repeatedly followed and applied with the result that tens of thousands of Canadian donors and the charities to which they donate have relied on that definition in making donations to registered charities by way of borrowed funds;

4. The departure from the *Friedberg* standard has been undertaken below without explanation or, seemingly, recognition that is the effect of the decision. The *Friedberg* test should be upheld and enforced in all respects and, absent the intervention of Parliament, not altered in the manner undertaken below;

5. The importance of altering the *Friedberg* definition of gift goes beyond leveraged donation arrangements, as it would impact on the legal implications of all of the charitable donations made by approximately 23 million Canadians, comprising 84% of the population aged 15 and over and gifts of $10 Billion (based on 2007 data);

6. If the *Friedberg* test is to be revisited in any material respect, the need for certainty and consistency in the law, and the attendant need for fairness to those seeking to follow the law, dictates that such an exercise should only be undertaken by this Honourable Court, particularly given the long-standing reliance of tens of thousands of Canadians and countless registered charities on the *Friedberg* test. This reliance is based in part on this Honourable Court's refusal

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[2] "Thus, a gift is a voluntary transfer of property owned by a donor to a donee, in return for which no benefit or consideration flows to the donor (see Heald, J. in *The Queen v. Zandstra* [74 DTC 6416] [1974] 2 F.C. 254, at p. 261.) The tax advantage which is received from gifts is not normally considered a "benefit" within this definition, for to do so would render the charitable donations deductions unavailable to many donors."

in *Friedberg* to grant leave regarding the portion of that case pertaining to the definition of "gift";

7. In particular, the *Act* should not be narrowed to exclude otherwise valid gifts where the donor may have received a benefit from a third party, as such a fundamental alteration of the "*in return for which*" portion of the *Friedberg* test should not be countenanced unless Parliament amends the clear wording of the Act to that effect;

8. Further, the *Act* should not be narrowed in this manner to exclude otherwise valid gifts where the alleged benefit to the donor was a loan from a third party, regardless of whether the interest terms of the loan are considered to be favourable;

9. The definition of "gift" in the *Act* should not be permitted to mean different things in different parts of Canada, as is currently the case, given that some Quebec jurisprudence under the *Act* draws on the definition of "gift" found in the Quebec *Civil Code*, whereas the rest of Canada derives its definition from the common law;

10. The wholesale rejection of the key component of the *Friedberg* definition of gift that permits a donor to receive a benefit in the form of a tax advantage, including an advantage that may be greater than the financial expenditure of the donor, should not be countenanced unless Parliament amends the clear wording of the *Act* to that effect.

11. In the decisions below and certain other decisions in this area, another central tenet of *Friedberg* has been cast aside and replaced by its very opposite: Friedberg's admonition that courts should avoid "*endless exercises to determine the true intentions behind certain transactions*" because,

"*in tax law, form matters*" is being ignored in favour of a confusing and inconsistent approach in which the donor's subjective state of mind has become a central consideration;

12. The decisions of the Courts below seek to alter the *Friedberg* test based on transactions or events by the registered charity after the donation was made, despite the fact taxpayers cannot be and are not, as a matter of law, held responsible for such matters, which are beyond their knowledge or control;

13. The effect of the decisions below would be to shift at least part of the government's responsibilities for regulating registered charities onto Canadian donors, despite the clear wording of the *Act* establishing that this burden rests with the government;

14. Further and in the alternative, the decision below to deny Mr. Maréchaux of any tax deduction whatsoever, even for the non-borrowed portion of his donation, constitutes a dangerous and punitive precedent and a fundamental departure from the existing law;

Dated at Toronto, Ontario this 26th day of January, 2011.

Signed by:

Counsel for the Applicant
BAKER & MCKENZIE
Barristers and Solicitors
Brookfield Place
181 Bay Street, Suite 2100
Toronto, Ontario
M5J 2T3

Matthew J. Latella
Telephone: (416) 865-6985
Sal Borraccia
Telephone: (416) 865-6904

Agent
GOWLING LAFLEUR HENDERSON
Barristers and Solicitors
2600 – 160 Elgin Street
Ottawa, Ontario
K1P 1C3

Henry S. Brown, Q.C.

Telephone: (613) 233-1781
Telecopier: (613) 563-9869

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Applicant (Appellant)

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Respondent (Respondent)

MEMORANDUM OF ARGUMENT OF THE APPLICANT (APPELLANT), F. MAX E.MARÉCHAUX

PART I – STATEMENT OF FACTS

OVERVIEW

1. In recent years, tens of thousands of Canadians have donated billions of dollars worth of charitable gifts to numerous registered charities by way of so-called "leveraged donation" arrangements. The Minister of National Revenue (the "Minister") has denied these donors, including the Applicant, Max Maréchaux, the tax credits that are otherwise allowed for such charitable donations as a result of the nature of the donation program. This test case centres on the proper definition of "gift", as that word is used in the term, "total charitable gifts" in section 118.1 of the *Income Tax Act* (the "*Act*")[1]. A resolution of this case would bring clarity and predictability for donors and the many charities who depend on their gifts in an area of Canadian tax law that is plagued by conflicting jurisprudence.

2. Mr. Maréchaux's donation was comprised of both his pre-existing funds and funds that he borrowed from a third party that is at arm's length from him and the duly registered charity. The Minister disallowed the entirety of Mr. Maréchaux's tax credit. The Minister seeks this result by effectively changing the law regarding charitable donations,

[1] *Income Tax Act*, R.S.C. 1985 5th Supp., as amended, s.118, Brief of Authorities, Vol I, Tab B1

without amending the *Act*. The change the Minister seeks both involves reading words into the *Act,* departing from long-standing jurisprudence and indeed moving beyond the language and intent of the Government's own proposed legislation. Additionally, this creates a dangerous and inequitable discordance between the manner in which the *Act* is to be interpreted in all of the common law jurisdictions in Canada, as compared to the manner in which it has been interpreted in Quebec, where some decisions look to the *Civil Code*'s definition of gift, which allows a donor to receive consideration, provided that the value of the gift exceeds the value of the consideration received in exchange.[2]

Factual Background

3. Mr. Maréchaux has been practicing as a real estate lawyer since 1976.[3] In his 2001 taxation year, he donated $100,000 (the "Donation") to The John McKellar Charitable Foundation (the "Foundation") and received a charitable donation receipt in that amount.[4]

4. In computing his tax payable for the 2001 taxation year, Mr. Maréchaux claimed the charitable tax credit resulting from the Donation. In a letter sent to Mr. Maréchaux on March 14, 2005, the Minister allowed the $20,000 of the Donation that had come from Mr. Maréchaux's own funds as a charitable gift and disallowed $80,000 of the Donation.[5] The Minister's position was stated to be based on the following reasons :

   (a) "The purported financing used by you for 80% of the claimed donation resulted in benefits received by you *in return for* making a contribution to the McKellar Foundation. It is CRA's view that a gift is a voluntary transfer of property without receiving consideration. There was no *donative intent* with respect to this

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[2] Article 1810, Civil Code of Quebec (1991, chapter 64) ("Civil Code"), Brief of Authorities, Vol. I, Tab B2; *Gagnon Estate* v. *MNR*, 1960 CarswellNat 143 at paras. 7-8, Brief of Authorities, Vol. I, Tab A1; *Aspinall* v. *MNR*, 1970 CarswellNat 179 at para. 9, Brief of Authorities, Vol. I, Tab A2

[3] Transcript of the evidence given at the Tax Court of Canada ("Trial Transcript") of M. Maréchaux, p. 1, lines 20-24, Application for Leave to Appeal ("Application Record"), Vol. I, Tab 12, p. 122

[4] Trial Transcript of M. Maréchaux, p. 14, lines 2-12; Application Record, Vol. I, Tab 13, p. 123; Trial Exhibit: AR-2, Tab 2, Application Record, Vol. I, Tab 14, p. 124; Trial Exhibit 4, Application Record, Vol. I, Tab 15, pps. 125-134; Amended Reasons for Judgment ("Amended Reasons"), para. 19, Application Record, Tab 8. p. 80

[5] Trial Transcript of M. Maréchaux, pps. 57-58, lines 7-25 and 1-18 Application Record, Vol. I, Tab 16, pps. 135-136; Trial Exhibit 6 – Letters from CRA dated April 11, 2005 and March 14, 2005, Application Record, Vol. I, Tab 17, pps. 137-143

contribution. It was made for the purposes of receiving a benefit, therefore it will be disallowed in its entirety." [emphasis added];

(b) "the purported financing obtained by you ...was in fact ultimately funded by amounts directed to the McKellar Foundation as the donated amounts.";

(c) "the terms and conditions of your purported financing ...indicate that it was not a bona fide loan."[6]

5. Four weeks later, by way of a letter dated April 11, 2005, the Minister reversed his own position regarding $20,000 of the Donation, thereby disallowing the credit for the entire amount of the deduction. The Minister cited no authority and provided no explanation for this *ad hoc* and punitive about-face. Rather, the brief letter simply increased the amount of the Donation that was disallowed, cited the same rationale as the previous letter and concluded: "*[w]e apologize for any inconvenience this may have caused*".[7]

6. The Canada Revenue Agency (the "CRA") sent Mr. Maréchaux a Notice of Reassessment dated August 5, 2005 for his 2001 taxation year, which reduced his tax credit in respect of the Donation to zero ("$0").[8]

7. Mr. Maréchaux learned of the Donation Program for Medical Science and Technology, known as the "Trinity Program", from his accountant, Judy Moore ("Ms. Moore"), who he had known for 25 years.[9] After determining that Ms. Moore had done her due diligence to satisfy herself that it was a *bona fide* donation program, Mr. Maréchaux then

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[6] Trial Exhibit 6: Letters from CRA dated April 11, 2005 and March 14, 2005, Application Record, Volume I, Tab 17, pps. 137-143

[7] Trial Exhibit 6: Letters from CRA dated April 11, 2005 and March 14, 2005, Application Record, Vol. I, Tab 17, pps. 137-143

[8] Trial Transcript of M. Maréchaux, p. 63, lines 14-25, Application Record, Volume I, Tab 18, p. 144; Trial Exhibit 14: Notice of Reassessment dated August 5, 2005, Application Record, Tab 19, pps. 145-149. On August 10, 2005, Mr. Maréchaux served a Notice of Objection ("Objection") to the Reassessment. After at least 90 days had elapsed following the service of Mr. Maréchaux's Objection, Mr. Maréchaux appealed to the Tax Court of Canada pursuant to paragraph 169(1)(b) of the *Act*. Appellant's Notice of Appeal to the Tax Court of Canada ["TCC Notice of Appeal"], para. 3, Application Record I, Tab 20, pps. 150-154

[9] Trial Transcript of M. Maréchaux, p.6, lines 19-25 and p. 7, lines 1-3; Application Record, Vol. I, Tab 21, pps. 155-156

confirmed that the charity to receive his donation was duly registered and he conducted his own further due diligence regarding the program before he decided to proceed.[10]

8. Mr. Maréchaux contributed $20,000 from his own resources and borrowed $80,000 from an entity at arms-length both from him and from the recipient of his donation. He also paid an amount equal to $10,000 to the lender for fees, insurance and a security deposit that was to be invested (the "Investment").[11] The $10,000 paid to the lender was allocated as follows: $8,000 to fund the Investment which was expected to accrete to $80,000 at the end of the twenty-year term; $1,200 as a fee for arranging the Loan; and $800 as a premium in respect of an insurance policy that insured the risk if the Investment did not accrete to $80,000 in 20 years (the "Insurance Policy").[12]

9. The Trinity Program was designed so that the donors could assign the Investment and the Insurance Policy to the lender in full satisfaction of the loan (the "Put Option").[13] However, the Put Option was not guaranteed under the Trinity Program, because it was possible that the Insurance Policy would not be obtained. In those circumstances, the Put Option would not be effective and Mr. Maréchaux would be required to repay any difference between the loan and the Investment at the end of the twenty-year term[14].

10. On January 16, 2002, Mr. Maréchaux exercised the Put Option by assigning the Insurance Policy and the Investment to Capital Structures as full payment of the Loan.[15]

11. The learned Trial Judge dismissed Mr. Maréchaux's appeal based on her conclusions that
1) the financing arrangement (consisting of the Loan "*coupled with the expectation of the Put Option*" constituted a significant benefit flowing to Mr. Maréchaux,[16];
2) the agreements establishing the financing arrangement "*do not clearly provide for an*

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[10] Trial Transcript of M. Maréchaux, p. 17, lines 10-13 and pps. 18-21, lines 1-25, p. 22, lines 1-19, Application Record, Vol. I, Tab 22, pps. 157-162; Trial Exhibit: AR-1, Application Record, Vol. I, Tab 23, pps. 163
[11] Amended Reasons, para. 19, Application Record, Vol. I, Tab 8, p. 80
[12] Partial Agreed Statement of Facts, para. 5, Application Record, Vol. I, Tab 24, p. 166
[13] Amended Reasons, para. 20, Application Record, Vol. I, Tab 8, p. 80
[14] Trial Transcript of M. Maréchaux, p. 30, lines 13-21; pps. 28-29, lines 11-25 and line 1, Application Record, Vol. II, Tab 25, pps. 359-361; Trial Exhibit: AR-2, Tab A, Application Record, Vol. II, Tab 26, pps. 362-369
[15] Amended Reasons, para. 19, Application Record, Vol. II, Tab 8, p. 80; Trial Exhibits: AR-2, Tabs 5, 5A, 5B, 5C, 5D and 5E, Application Record, Vol. I, Tab 27, pps. 370-389
[16] Amended Reasons, paras. 32-34, Application Record, Vol. I, Tab 8, p.85

effective Put Option";[17]

3) even without the Put Option, the loan provided a significant benefit;

4) the value of the alleged benefit "*appears to be somewhere in the neighbourhood of $70,000 ($80,000 received less outlays of $10,000), less a slight discount for the risk that the Put Option would not be effective*".

12. The Trial Judge did not explain how the mere "expectation" of an option that may or may not have been effective could constitute any part of a benefit that would vitiate a gift. Accordingly, she must be taken to have ultimately relied on the Loan itself constituting the sole benefit that vitiated Mr. Maréchaux's gift. However, her attempt to quantify the value of that purported benefit does not stand up to scrutiny, given that the Loan was required to be donated to charity and was to be repaid, in accordance with the agreements in place.

13. The Federal Court of Appeal upheld the Trial Judge's findings, supported by brief written Reasons that also failed to address the above concerns or to contemplate the other issues set out herein.

PART II – THE ISSUES

14. This test case raises the following issue of public importance that warrants the consideration of this Honourable Court:

What is the proper definition of "gift", as that word is used in the statutorily defined term, "total charitable gifts" in Section 118.1 of the *Income Tax Act*?

15. To properly define "gift" in the above context, the following three sub-issues regarding the potential benefits or consideration to a donor must be addressed:

> ***1) where does the law draw the line between the types of benefits that might have the effect of vitiating an otherwise valid gift and those that do not?***
>
> ***2) do benefits to a donor from a party at arm's length from the donee have the effect of vitiating an otherwise valid gift?***

[17] Amended Reasons, para. 23, Application Record, Vol. I, Tab 8, p. 83

3) to what extent is the donor's subjective state of mind regarding any potential benefit at the time of the donation relevant to determining the validity of a gift?

PART III – STATEMENT OF ARGUMENT

National and Public Importance

16. Canadian donors and charities, and their respective advisors, have relied on the applicable case law established approximately 20 years ago in *Friedberg v. Canada*[18] *("Friedberg")*, and the absence of any specific legislative prohibition against such arrangements in the *Act.* The within proceeding is the first known case to reach this Honourable Court involving an appeal by a donor against an assessment arising out of such an arrangement. This case explores the essence of charitable giving under the *Act.*[19].

17. In 2007, almost 23 million Canadians, 84% of the population aged 15 and over, made a financial donation to a charitable or other non-profit organization. Those gifts totalled $10 billion.[20] From 2003 to 2009, the CRA estimates that approximately 172,000 Canadians claimed tax credits for charitable contributions made through gifting arrangements such as leveraged donations. The total value of these donations exceeds $5.4 billion, which represents approximately 10 percent of all charitable donations in Canada during this period. Further, as of December 23, 2010, the CRA reports that it has reassessed over 130,000 taxpayers and denied over $4.5 billion in donation claims resulting from such donations.[21]

18. The increased audit and assessment activity of the Minister has closely corresponded with a decline in Canadians' participation in leveraged donation arrangements in recent years.

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[18] [1991] F.C.J. No. 1255, (FCA), aff'd on other grounds [1993] 4 S.C.R. 285; leave to appeal re: "gift" issue dismissed [1992] S.C.C.A. No. 190, Brief of Authorities, Vol. I, Tab A3

[19] Other recent cases dealing with similar issues illustrate the national importance of these issues such as *Coleman v. HMQ*, 2010, TCC 109 (CanLII), at paras. 1 and 2, Brief of Authorities, Vol. I, Tab A4, in which the trial judge was advised by counsel for the Appellant: "*The future of charitable giving in this country rests upon [your] shoulders*". Despite the fact counsel for the Minister in that case "*...attempted to alleviate that weighty burden by suggesting this case was no different from any other...*", the Judge in that case correctly concluded: "*This case explores the very nature of charitable giving*".

[20] Affidavit of Terrance S. Carter, sworn January 26, 2011, ("Carter Affidavit"), para.5, Application Record, Vol. I, Tab 3, p. 35

[21] Affidavit of David G. Duff, sworn January 18, 2011("Duff Affidavit"), paras 14 and 15, Exhibits "B" and "C", Application Record, Vol. I, Tab 2, pps. 10 and 27-33

Accordingly, less money is being given to charities.[22] If this were simply a function of the increased enforcement of clearly stipulated and understood legislation being uniformly interpreted across Canada, that would not be cause for as great a concern (although the fact that so many Canadians clearly did not appreciate the effect of the law would still be problematic). However, the legitimacy, or lack thereof, of the Minister's actions in assessing these donors is at the centre of the matters in issue in this case. For charities to be able to have stability in their donations and donors to have certainty regarding their tax treatment, this area of the law must be clarified.

19. If the Minister's reassessments are, in any way, more onerous than the law in this area, participation in these arrangements will have been artificially driven down by what amounts to illegitimate activity. On the other hand, if the Minister's actions are legal, all participants - the Minister, the donors, the charities - and those who advise each of these parties, will undoubtedly benefit from the certainty that a decision of this Honourable Court would bring. Absent such a decision, the law on gifts will remain in doubt.

20. The Minister's blanket default audit position when encountering any Canadian taxpayers who have participated in one of these arrangements is to deny any tax credit for any portion of the taxpayers' charitable donation.[23] This sort of pre-judgment is both improper and demonstrates the need for clearer parameters to be established for determining when such credit is to be given and when it is to be denied. This will benefit all parties, including the Minister.

What is the proper definition of "gift", as that word is used in the statutorily defined term, "total charitable gifts" in Section 118.1 of the *Income Tax Act* ?

1) where does the law draw the line between the types of benefits that might have the effect of vitiating an otherwise valid gift and those that do not?

21. The *Act* establishes a comprehensive system for charitable donations, which affects the rights and obligations of both donors and donees alike. Individuals and corporations who make gifts, and registered charities who receive them, rely upon both the wording of the *Act* and the interpretations of its words established in the common law.

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[22] Duff Affidavit, Exhibit "C", Application Record, Vol. I, Tab 2, pps. 29-33
[23] Carter Affidavit, Exhibit "D", Application Record, Volume I, Tab 3, pps. 52-53

22. Approximately 20 years ago, in *Friedberg*, the Federal Court of Appeal set out the definition of "gift", as that word is used in the context at issue:

> *"Thus, a gift is a voluntary transfer of property owned by a donor to a donee, in return for which no benefit or consideration flows to the donor (see Heald, J. in The Queen v. Zandstra [74 DTC 6416] [1974] 2 F.C. 254, at p.261 261.) The tax advantage which is received from gifts is not normally considered a "benefit" within this definition, for to do so would render the charitable donations deductions unavailable to many donors."*[24]

23. *Friedberg* has been repeatedly followed and applied since it was decided in 1991.[25] Tens of thousands of Canadians have relied on the above definition of gift in making donations to registered charities by way of borrowed funds. Now, without purporting to overturn *Friedberg*, the Courts below in this case have fundamentally ignored this definition and imposed different and additional criteria for the existence of a gift.

24. Specifically, the learned Justices below have effectively overturned three key aspects of the Federal Court of Appeal's definition, without acknowledging that is the effect of their decision: 1) they have decided that a benefit need not truly be "*in return for*" a gift, in order to render the gift invalid, in that the benefit may come from anyone, including someone at arm's length from the donee; 2) they have effectively concluded that a tax advantage which is received from gift *should*, in fact, be considered a "benefit" that vitiates a gift, if the benefit is significant enough; and 3) they have endorsed the idea that a donor's frame of mind, rather than the form of any transaction by which a donation is made, is to be determinative of the existence, or lack thereof, of a valid gift.

25. If the long-standing *Friedberg* definition that has been relied upon by so many is to be revisited in any material respect, the need for certainty and consistency in the law, and the attendant need for fairness to those seeking to follow the law, dictates that such an exercise should only be undertaken by this Honourable Court. This is particularly so given this Honourable Court's refusal in *Friedberg* to grant leave regarding the portion of that case pertaining to the definition of "gift", despite otherwise granting leave.

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[24] *Friedberg, supra note 18*, at p. 3, Brief of Authorities, Tab A3

[25] See e.g. *Chabot v. Canada* [2001] F.C.J. No. 1829 (FCA) at para 11, Brief of Authorities, Tab A5; *Doubinin v. Canada* [2005] F.C.J. No. 1535 (FCA), Brief of Authorities, Tab A6; *Lockie v. Canada* [2010] T.C.J. No. 96 (TCC) at para. 26, Brief of Authorities, Tab A7

26. Part of the uncertainty over the definition of "gift" in the *Act,* is the uncertainty over the scope of the term "benefit", as used in the *Friedberg* definition of gift. That test indicates that a donor's anticipation of the receipt of certain kinds of benefits will vitiate an otherwise valid gift. However, when making a charitable donation, one might anticipate a variety of different kinds of benefits, including:1) the benefit of a tax deduction; 2) the benefit of the satisfaction that stems from helping others; 3) the benefit of improving the community in which one lives, and; 4) the benefit of increasing one's stature and reputation within one's community, particularly if the gift is sufficiently large and publicly-made. Clearly, anticipating any or all of these types of benefit would not vitiate otherwise valid gifts.

27. What the Minister has truly attacked in this case is a key component of the *Friedberg* definition of gift that permits a donor to receive a benefit in the form of a tax advantage, including an advantage that may be greater than the financial expenditure of the donor.[26] Overturning that aspect of *Friedberg* should not be countenanced unless Parliament amends the clear wording of the *Act* to that effect.

28. Further, the decision of the Courts below to deny Mr. Maréchaux of any tax credit whatsoever, even for the $20,000 of his pre-existing funds that he donated, constitutes a deeply flawed and punitive precedent and a fundamental departure from the existing law.

29. Notably, proposed amendments to the *Act*[27] would only disallow the portion of a deduction that is in excess of the non-borrowed part of a donation. Specifically, in 2003, the Federal government tabled legislation to amend the *Act* by limiting taxpayers' existing rights pertaining to charitable gifts. However, the approach taken by the learned Justices below under the *Act* strips charitable donors of even more of their rights than would be the case under the proposed legislative restrictions. This is clearly an absurd result.

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[26] *Friedberg, supra note 18*, at p. 4; *Langlois v. Canada* [1998] T.C.J. No. 1049 (TCC), at para.159, aff'd [2000] F.C.J. No. 1806 (FCA), paras. 8-10, Brief of Authorities, Vol. I, Tab A8

[27] Bill C-10, *Income Tax Amendments Act*, 2006, 2nd Sess. 39th Parl., 2007, cl. 187(23) and cl. 139(2); Brief of Authorities, Vol. I, Tab B2 and B3. The government has failed to actually pass the amendments and, in any event, none of the proposed amendments would have affected the rights of Mr. Maréchaux in this case, as the matters in issue all pre-date the proposed effective dates for those potential amendments.

30. In addition, some cases under the current wording have held that donors who have received material benefits in exchange for charitable contributions have nonetheless made valid gifts, equal to the difference between the value contributed and the value received.[28]

31. Further, when distinguishing between the types of benefits, the receipt of which will have the effect of vitiating an otherwise valid gift and those that will not, that line must not be arbitrarily drawn. Rather, the line must be based on principles rooted in fairness and must be germane to the taxation context. Mr. Maréchaux contended that the term "taxable benefit", already well understood in the taxation context, provided an appropriate means of drawing that line. Defining "gift" for the purposes of section 118.1 in such a way as to exclude otherwise valid gifts where a "taxable benefit" is anticipated, while including gifts where the donor anticipated the receipt of a benefit that was not taxable (such as the 4 items listed in paragraph 26 above), would provide exactly the sort of principled line-drawing that would be clear, fair and rooted in the principles of the *Act*. It would also exclude the "benefit" of an interest-free loan that the courts below found to vitiate Mr. Maréchaux's gift.

32. In the Courts below, the Minister had to concede, based on *Cooper v. The Queen,* that an interest-free loan is generally not regarded as a "taxable benefit" for the purposes of income inclusion under the *Act*[29]. However, the Minister nonetheless maintained that, whether or not a benefit is a "taxable benefit" is "not relevant" to the determination of whether a gift has been made. The Minister did not explain the merits of that position. The Trial Judge cited *Cooper* for the conclusion that "an interest-free loan *generally could* be considered a benefit", without addressing the issue that the receipt of many types of benefit are neither taxable, nor vitiate a gift.[30] If one of the aims of the *Act*, as interpreted by the Courts, is to provide certainty and predictability to taxpayers and other stakeholders, such as registered charities, there is an obvious appeal to using a well-established principle like "taxable benefit" to draw this line. What's more, it makes sense

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[28] *Koetsier v. MNR*, 1973 CarswellNat 307 (TRB) at para. 14, Brief of Authorities, Vol. I, Tab A9; *Woolner v. Canada*, 1997 CarswellNat 2995 (TCC) at paras. 23, 26-29, 36, aff'd 1999 CarswellNat 1948, Brief of Authorities, Vol. I, Tab A10

[29] Minister's Memorandum of Argument before Federal Court of Appeal, p 15, footnote 43, Application Record, Vol. II, Tab 28, p. 390; *Cooper v. The Queen*, [1988] F.C.J. No. 931 (FCTD) at p. 16, Brief of Authorities, Tab A11

[30] Amended Reasons, paras. 27-9, Application Record, Vol. , Tab 8, p. 83

from a policy standpoint. After all, if a benefit is not taxable, query why its receipt should vitiate an otherwise valid gift?

33. The Applicant submits that the denial of a credit even for his own pre-existing funds is not only wrong in law, it is punitive, insofar as it denies any deduction for even the portion of the donation that came from the donor's annual income. There is simply no basis in the *Act* or the applicable jurisprudence for such an approach.

34. Furthermore, even the proposed draft legislation recognizes that the non-borrowed portion of a leverage donation of the sort made by Mr. Maréchaux would give rise to a credit.[31] The Minister's position in this case, thus far endorsed by the Courts below, takes the much more extreme position that somehow even a donor's hard-earned monies donated to a charity somehow cease to give rise to a credit when donated, if they happen to be donated along with funds that the donor borrowed. This is punitive and wholly unsupported by the plain wording of the *Act* and the jurisprudence applying it.

Post-Donation Transactions by Charities

35. The decisions of the learned Justices below are based, in part, on transactions by the registered charity or others after the donation was made.[32] By referencing such matters and allowing them to colour the analysis of when a charitable gift is made, the *Friedberg* definition is fundamentally altered and the taxpayer is unfairly punished. There are sound policy reasons that taxpayers are not held responsible for such matters, which are beyond their control and, generally, their knowledge.

36. A taxpayer ought not be punished for the actions taken or priorities set by the registered charity to which s/he donates. In any event, the registered charity that received Mr. Maréchaux's donation in this case went on to use the funds, in part, for the benefit of two other registered charities. All three charities involved have received some benefit from the Donation and those of other donors participating in the Trinity Program.[33] There is no

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[31] Bill C-10, *Income Tax Amendments Act*, 2006, 2nd Sess. 39th Parl., 2007, (as passed by the House of Commons 29 October 2007) ("Bill C-10"), cl. 187(23) and cl. 139(2), Brief of Authorities, Vol. I, Tabs B3 and B4

[32] Amended Reasons, paras. 15 (ASF 11-23, 25) and 24-25, Application Record, Vol. I, Tab 8, pps. 79 and 31, FCA Reasons, para. 1, Application Record, Vol. , Tabs 9, p. 90

[33] Partial Agreed Statement of Facts, para. 12, Exhibit 4; para. 15, Exhibit 8, para. 19, Exhibits 12 and 13,

finding that the transactions were a sham. Indeed, the learned Trial Judge found as a fact: "*...the bona fides of the financing arrangement provided to the appellant are not in dispute in this appeal.*[34]

37. The *Act* contains a comprehensive system for regulating registered charities, which includes the ability to strip such organizations of their charitable status in certain circumstances.[35] The CRA did not take any such action here. To the extent the decisions below rely on events that transpired involving the registered charity and/or other parties, but not Mr. Maréchaux, the effect of those decisions would be to shift at least part of the government's regulatory responsibilities in this regard onto Canadian donors, despite the clear wording of the *Act* establishing that this burden rests with the government.[36]

38. Donors must be entitled to rely upon the fact that a specific donee has been designated by the government as a registered charity and has issued a tax receipt, without having to somehow bear the burden to investigate the specific activities of that charitable organisation. It is no more appropriate for the government to attempt to allocate responsibility for policing the activities of a charitable foundation to a donor than it is to assign responsibility to the charitable organisation for investigating whether the source of any or all of the donations it receives may have been borrowed funds. However, the (perhaps unintended) implication of the decisions below is that the *Act* can be interpreted in this fashion. This is an absurd result.

39. The learned Trial Judge found as a fact: "*When the appellant agreed to participate in the Program, he was not aware of many of the transactions described above [in the Partial Agreed Statement of Facts]. In particular, the appellant did not have detailed information as to what the Donation would be used for after it was paid to the Foundation.*":[37] Indeed, taxpayers *cannot* be held responsible for knowing such things and the learned Justices below should have refrained from relying on such matters, explicitly or implicitly, in the context of an appeal by a taxpayer denied credit for a gift.

Application Record, Vol. I, Tab 24, p. 167, Vol II, pps. 271, 294-306, Vol I., p. 168 and Vol. II, pps. 325-340

[34] Amended Reasons, para. 44, Application Record, Vol. I, Tab 8, p. 86

[35] *Income Tax Act*, R.S.C. 1985 5th Supp., as amended, s. 149.1(f), 149.1(1), (2), (9), (14), (15) and s. 245 , Brief of Authorities Tabs B5 and B7

40. If a charitable organisation, registered by the government, is somehow engaged in activities that the government believes it should not be, the appropriate remedy is for the government to address that matter with the charity, up to and including the revocation of its charitable status. The Minister has consistently attempted to colour the *bona fides* of Mr. Maréchaux's charitable donation in this case by referencing the flow of funds *after* they were received by the Foundation, regardless of the fact that such activities were both beyond Mr. Maréchaux's control and were carried out unbeknownst to him. It is apparent from the decisions below that such facts, while perhaps not explicitly invoked as the rationale for the definition of gift, coloured the conclusions drawn therein.

Is an Interest-Free Loan a Benefit?

41. The decisions below are based on a fiction: that Mr. Maréchaux received the interest-free, unfettered use of borrowed funds for 20 years. In accordance with the undisputed documentation establishing the leveraged donation arrangement, he was *not* free to use the funds however he wished, as would typically be the case if one is considered to have the "benefit" of funds. Rather, he sought to and did, in fact, repay the Loan promptly.

42. Accordingly, the Minister is really concerned with a "benefit" of a different sort entirely: namely, a transaction the structure of which allows for a larger tax receipt than would otherwise be available, as that was the effect of the sole permitted use of the borrowed funds and the structure of the arrangement generally. The difficulty for the Minister in this situation is that the jurisprudence makes clear that that type of benefit is not of the kind that would typically vitiate a gift.[38]

43. To sum up: the *real* "benefit" at issue in this case is neither the interest-free loan that was for a dedicated purpose, nor the so-called "Put Option", which the trial judge said may not have ever been effective. Rather, the real benefit was the tax savings which is the same sort as was found not to vitiate the gift in *Friedberg*.

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[36] *Income Tax Act*, R.S.C. 1985 5th Supp., as amended, s. 168, Brief of Authorities Tab B6
[37] Amended Reasons, para. 17, Application for Leave to Appeal, Volume I, Tab 8, p. 79
[38] *Friedberg*, *supra* note 18, at pps. 3-4, Brief of Authorities, Tab A3

44. Another issue for this Honourable Court to resolve is whether the quantum of the alleged benefit received by a donor matters for the purposes of determining whether a valid gift exists. The Minister and the learned Justices below repeatedly and erroneously assert that Mr. Maréchaux received a benefit in the amount of $70,000. This assertion is simply incorrect because, even if Mr. Maréchaux was not required to donate the entirety of the interest free loan, (which he was), and the funds could somehow have been used for whatever purpose he wished, such a loan would still not constitute a $70,000 "benefit", as loans must be repaid. At most, it would constitute a benefit equal to the interest saved on the borrowed funds, were they to have been borrowed at market rates.[39]

45. Arguably, there could be some benefit related to the time value of money in such circumstances, although even that begs the question as to the role played by "market rates" when analyzing such a purported benefit. For example, would an otherwise valid gift cease to be so if it was partially made using funds borrowed at only slightly below market rates? What if there were some other advantageous term in the loan agreement besides the applicable interest rates?

46. Further, what if the loan to the donor was at market rates, but all of the other details regarding the "Put Option" still applied? In other words, a donor borrows funds and donates them to charity, but also invests funds with a third party and purchases an insurance policy that guards against the invested funds failing to grow over time at a sufficient rate as to pay off the loan. The growing investment would still be the donor's own funds, and it could even grow in excess of the guaranteed amount of growth, thereby completely eliminating any perceived monetary benefit of the insurance policy. Accordingly, it cannot be reliably predicted that there is any actual benefit to a so-called "put option", particularly one that the Trial Judge found to be unenforceable. Rather, all purported benefits to Mr. Maréchaux collapse into one perceived benefit: that of a higher tax receipt than would have been possible in the absence of the leveraged donation

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[39] There appears to be some uncertainty as to what the alleged benefit at issue was, as the expert witness at trial testified that it was the result of having an $80,000 *liability* extinguished for $10,000, Trial Transcript of H. Johnson, p. 525-6, lines 8-25 and 1-10, Application Record, Vol. II, Tab 29, pps. 391-392, while the learned Trial Judge indicated that it was a function of the net amount of the Loan itself, as if it was an *asset*, Amended Reasons, para. 34, Application Record, Vol. I, Tab 8, p. 85

arrangement. It is the receipt of this type of benefit that *Friedberg* has suggested does not vitiate an otherwise valid gift.

47. However, the Minister and the Courts below have not addressed this matter on those terms, preferring instead to focus on other, imagined benefits such as an interest-free loan, without addressing the fact the loaned funds were required to be given away. The analysis in the Courts below relies on a finding that the financing and the Donation "were inextricably tied together by the relevant agreements".[40] However, absent from this analysis is any recognition of the fact that such a finding means that the purported "benefit" of the financing was illusory since the borrowed funds were required to be donated in their entirety. In effect, the analysis below saddled Mr. Maréchaux with all of the negative implications of linking the financing to the Donation, but none of the favourable ones. Such a one-sided approach is fundamentally unsound if one is to truly ascertain the presence or absence of a benefit, its amount, if relevant, and whether the type of benefit is such as to vitiate an otherwise valid gift.

48. The Applicant respectfully submits that this Honourable Court must establish the point at which these lines are to be drawn. Otherwise, the Minister will do so and reassess countless taxpayers accordingly, despite the absence of language in the *Act* to support his actions. These are the issues that it is incumbent on this Honourable Court to clarify for the benefit of all Canadians who give to registered charities and of those charities as well.

The Unfairness of Inconsistent Application of Federal Legislation – The Quebec Context

49. The concept of a gift under the Quebec *Civil Code* is different from that under the common law in the rest of Canada.[41] Courts within Quebec appear divided over whether to draw on the *Civil Code* definition of "gift" or the common law definition applied in the rest of Canada.[42] However, as the *Act* is federal legislation that uses the concept of gift (but does not define it), query whether this Honourable Court should permit varying

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[40] Trial Reasons, para. 33, Application Record, Vol. I Tab 9

[41] See *Civil Code*, Articles 1806, 1810, Brief of Authorities, Tab B1

[42] Duff Affidavit, paras. 11-12, Application Record, Vol. I, Tab 2, pps. 9-10; *Littler v. The Queen*, 1978 Carswell Nat 185 (FCA) at paras. 11 and 12, Brief of Authorities, Tab A12; *Gervais v. The Queen*, 1984 CarswellNat 273 (FCTD) at para 12, Brief of Authorities, Tab A13; *Langlois*, *supra* note 27, Brief of Authorities, Tab A8

standards in different parts of the country? To have a more rigorous test in one part of the country could encourage leveraged donation arrangements in one province alone, with its population having more advantageous tax treatment than all other Canadians.

50. Parliament has, thus far, chosen not to define "gift", as that term is used in s.118.1 of the *Act*, nor the range of "benefits" the receipt of which by a donor could vitiate an otherwise valid gift. Nor has Parliament signalled in the *Act* that it intended for the definition of "gift" to be interpreted differently in Quebec than it is in the rest of the country. Section 8.1 of the *Interpretation Act* suggests that "*a province's rules, principles or concepts forming part of the law of property and civil rights*" are to be considered, if "*it is necessary to refer to*" them in order to interpret an enactment.[43] However, some Courts have characterized the common law definition of gift as being based on the "ordinary" meaning of the term.[44] This begs the question whether "*it is necessary to refer to...the law of property and civil rights*" in order to interpret this part of the *Act*. If not, there is a debate whether s. 8.1 of the *Interpretation Act* applies, which should be resolved. [45]

51. Further, this Honourable Court has held that "*Parliament has, in effect, incorporated the common law definition of charity into the ITA*" and the "*conception of charity*" in the ITA is "*uniform federal law across the country.*"[46]As there is considerable uncertainty as to whether the same reasoning applies to the equally important and related term, "gift", it falls to this Honourable Court to decide the matter.

2) do benefits to a donor from a party at arm's length from the donee have the effect of vitiating an otherwise valid gift?

52. An important policy issue raised in this case is whether the *Act* is to be interpreted in such a way that *any* benefit flowing to a donor vitiates a gift, even if it comes from a non-party that is operating at arm's length from the donee. *Friedberg* established that the "benefit" of a tax receipt from a third party (the government) should not generally have this impact.

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[43] *Interpretation Act*, R.S.C 1985, c. I-21, Brief of Authorities, Tab B8
[44] *R. v. McBurney*, [1985] F.C J. No. 821 (FCA) at p. 6, leave to appeal dismissed [1985] S.C.C.A. No. 50 [SCC], Brief of Authorities, Tab A14
[45] D. Duff, *"The Federal Income Tax Act and Private Law in Canada: Complementarity, Dissociation, and Canadian Bijuralism"* (2003), 51:1 Canadian Tax Journal 1-132 at pp. 54-55, Brief of Authorities, Tab B9
[46] *Vancouver Society of Immigrant and Visible Minority Women v. M.N.R.*, [1999] 1 S.C.R. 10, at paras 28 and 143, Brief of Authorities, Tab A15

53. *Friedberg* also spoke of a benefit that is received "*in return for*" a gift. Accordingly, by its very wording, the *Friedberg* definition of gift recognizes that benefits received *from the donee* are materially different from the myriad benefits that one might receive from third parties at arm's length from the donee. The learned Trial judge did not address this fundamental point.

54. The learned Justices of the Federal Court of Appeal in the within matter very briefly disposed of the issue by incorrectly suggesting that counsel cited no authority to support the point and, in any event, they saw no principled reason for disregarding the benefit simply because it was provided by a third party.[47] What appears to have been missed is the fact that there was indeed authority cited for this point: *Friedberg* itself. *Friedberg's* "*in return for which*" language simply cannot be properly construed to encompass a benefit received from an arm's length third party.

55. Furthermore, there is a very clear "*principled reason*" for not casting the "*in return for which*" portion of the *Friedberg* definition of gift aside: by expanding the definition beyond benefits flowing from donee to donor, the essence of the benefit is fundamentally altered. Suddenly, we are no longer looking at an exchange between two parties involving something akin to "consideration". Rather, the clarity and predictability of this area of the law would be effectively eliminated, in the same way that the removal of the doctrine of privity would affect contract law.

56. In any event, only this Honourable Court should decide whether or not the clear "*in return for which*" language of the *Friedberg* definition should be upheld or discarded. Having conflicting Federal Court of Appeal decisions on this point is a recipe for ongoing uncertainty in this area of the law, particularly when the panel below purported to follow *Friedberg*, while clearly doing otherwise.

57. On the facts of this case, there was no finding that the third party was not operating at arm's length from the recipient of the gift and, absent such a finding, such a fundamental alteration of the "*in return for which*" portion of the *Friedberg* test should not be

[47] Reasons for Judgment of the Federal Court of Appeal ("FCA Reasons"), para. 7, Application Record, Vol. I, Tab 9, p. 92

countenanced unless Parliament amends the clear wording of the *Act* to that effect. In particular, the *Act* should not be narrowed in this manner to exclude otherwise valid gifts where the alleged benefit to the donor was a loan from a third party, regardless of whether the interest terms of the loan are considered to be favourable.

3) to what extent is the donor's subjective state of mind regarding any potential benefit at the time of the donation relevant to determining the validity of a gift?

58. In *Friedberg*, the Federal Court of Appeal explained an important tenet of tax law generally and the law pertaining to gifts in particular, at pg. 3 of its reasons:

> *In tax law, form matters. A mere subjective intention, here as elsewhere in the tax field, is not by itself sufficient to alter the characterization of a transaction for tax purposes. If a taxpayer arranges his affairs in certain formal ways, enormous tax advantages can be obtained, even though the main reason for these arrangements may be to save tax (see The Queen v. Irving Oil 91 D.T.C. 5106, per Mahoney J.A.) If a taxpayer fails to take the correct formal steps, however, tax may have to be paid. If this were not so, Revenue Canada and the courts would be engaged in endless exercises to determine the true intentions behind certain transactions. Taxpayers and the Crown would seek to restructure dealings after the fact so as to take advantage of the tax law or to make taxpayers pay tax that they might otherwise not have to pay. While evidence of intention may be used by the Courts on occasion to clarify dealings, it is rarely determinative. In sum, evidence of subjective intention cannot be used to 'correct' documents which clearly point in a particular direction.*

59. *Friedberg* clearly established that "*the main reason*" for a donation "*may be to save tax*", but that, since "*form matters*", the focus must be on the legal rights and obligations that flow from the actual documents, rather than a Quixotic quest for "*the true intentions behind certain transactions*". However, in later cases, not only have such considerations of a donor's state of mind become the focus, the Courts cannot agree on the language to be used to describe this nebulous variable. Consequently, the standard is set in decidedly different places when the Courts have attempted to engage in the "*endless exercises*" that Justice Linden warned about.

60. For example, in this case, the Trial Judge purported to set the bar thus: a donor must demonstrate "*a gift [was given] in <u>expectation</u> of no return*"[48], seemingly regardless of

[48] <u>Amended</u> Reasons, at para.49, Application Record, Vol. I, Tab 8, p. 87

the donor's stated "intention" or "motivation". However, that is inconsistent with *Friedberg* and other Federal Court of Appeal decisions following it, such as *Langlois*, which concluded that, so long as the donor intends to give the gift in question to the designated recipient, the "*necessary intent*" exists, as "*...it does not matter that the appellant's principal motivation was to obtain a tax advantage.*"[49] Other cases have suggested that the donor must have "*the requisite intent*" to make a gift, which can, nonetheless, co-exist with a "*hope*" for the receipt of a monetary benefit, but not an actual "*expectation*" of one.[50] Still others have disallowed a gift if the donor's "*sole motivation*" was to save tax, seemingly regardless of the donor's intent or expectation.[51] However, what "motivates" a person is distinct from what they "intend", and different still from what they may "expect".[52] "Expectation" suggests some sort of an assessment of the likelihood something will occur, which may or may not exist when one "hopes" or "intends" that it will do so. Nor is not clear whether such an assessment is to be subjective or objective. Accordingly, there is conceptual confusion among the Courts.

61. In any event, in this case, the Trial Judge spoke of "*the expectation of the Put Option*", regarding what Mr. Maréchaux was taken to have "expected" when he made his donation. However, she could not go further than that, as she also held that the Put Option may not be effective. The Court of Appeal stated that the Trial Judge held Mr. Maréchaux "*expect[ed] to receive...an interest-free loan*".[53] It is respectfully submitted that the fact the Put Option may not have been effective means that the purported benefit of the Loan must be the sole issue raised and, for the reasons explained above, the Loan, by itself and in the context of the requirement to donate the loaned funds, does not constitute a benefit that would vitiate an otherwise valid gift.

62. Furthermore, while the lower Courts purport to follow *Friedberg*, it is being denuded by this emphasis on the donor's state of mind, at the expense of the sort of transactional

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[49] *Langlois, supra* note 27, at para.159 of TCC decision, aff'd by FCA, Brief of Authorities, Tab A8
[50] *Doubinin, supra* note 26, paras. 8-10, Brief of Authorities, Tab A6
[51] *Dutil v. Canada* [1991] T.C.J. No. 654, at para.25, Brief of Authorities, Tab A16
[52] As has been recognized in other areas of the law, "motive" and "intent" are not the same. *Lewis v. The Queen*, [1979] 2 S.C.R. 821, at p. 831, Brief of Authorities, Tab A17
[53] Amended Reasons, at para.33, Application Record, Vol. I, Tab 8, p. 85, FCA Reasons, at paras. 3, Application Record, Vol. I, Tab 9, p. 85 The FCA went on to say that he had "good reason to believe that [the Put Option] would be effective" at para.11.

form that Justice Linden rightly pointed out "matters" in tax law. This kind of stealth overturning of long-standing and sound appellate authority is contrary to the doctrine of *stare decisis* and results in uncertainty in the law. The Courts have somehow moved from the "reason" for a donation being essentially irrelevant in *Friedberg,* to it being highly relevant, and there purportedly being a *requirement* for a particular intention. If such a fundamental change is to be made, it should only be made by this Honourable Court.

63. In *Doubinin*, the Federal Court of Appeal held that, where there was "*no guarantee*" a donor would receive a benefit and it was a "*mere possibility*", the donor had the "*requisite intent*" to make a charitable gift. While the concept of "requisite intent" is inconsistent with the tenets of *Friedberg*, the absence of a guarantee that the perceived benefit would be received (as was the case with the "Put Option" here) resulted in the gift being valid (unlike the decisions below). Accordingly, the conceptual confusion across decisions of the Federal Court of Appeal is evidenced by the fact that *Doubinin* is at once more onerous than *Friedberg* (by raising the spectre of a "requisite intent"), yet more permissive than the decision below in the within matter, which reached the opposite conclusion, despite essentially the same finding re: the contingent nature of the "benefit. This sort of confusion calls out for the intervention of this Honourable Court.

64. The imprecision of language used to describe a donor's state of mind has given rise to an unacceptable level of inconsistency and conceptual confusion characterized by the wide array of terms used by courts to describe precisely that which *Friedberg* admonished against. It is vitally important for all involved that this situation be remedied.

PART IV – SUBMISSIONS AS TO COSTS

65. This application for leave to appeal raises issues of public importance within the meaning of subsection 40(1) of the *Supreme Court Act*. For this reason, the Applicant requests that it be awarded costs in any event of the cause.

PART V – ORDER SOUGHT

66. Mr. Maréchaux respectfully requests:

a) an Order that leave to appeal be granted with costs, in any event of the cause.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 26th day of January, 2011.

BAKER & McKENZIE
181 Bay Street
P.O. Box 874
Suite 2100
Toronto, Ontario M5J 2T3

Matthew J. Latella (39140R)
416-865-6985

Salvador Borraccia (13414B)
416-865-6904
Fax: (416) 863-6275

Solicitors for the Applicant (Appellant),
F. Max E. Maréchaux

PART VI – TABLE OF AUTHORITIES

TAB A	DOCUMENT	VOL. #	PARA.
1.	*Gagnon Estate* v. *MNR*, 1960 Carswell Nat 143 at paras. 7-8,, Brief of Authorities, Tab A1	I	2
2.	*Aspinall* v. *MNR*, 1970 Carswell Nat 179 at para. 9, Brief of Authorities, Tab A2	I	2
3.	*Friedberg v. Canada* [1991] F.C.J. No. 1255, (FCA), aff'd on other grounds [1993] 4 S.C.R. 285; leave to appeal re: "gift" issue dismissed [1992] S.C.C.A. No. 190, , Brief of Authorities, Tab A3	I	16
4.	*Coleman v. HMQ*, 2010, TCC 109 (CanLII), at para. 1, Brief of Authorities, Tab A4	I	4
5.	*Chabot v. Canada* [2001] F.C.J. No. 1829 (FCA), Brief of Authorities, Tab A5	I	23
6.	*Doubinin v. Canada* [2005] F.C.J. No. 1535 (FCA), Brief of Authorities, Tab A6	I	23
7.	*Lockie v. Canada* [2010] T.C.J. No. 96 (TCC), Brief of Authorities, Tab A7	I	23
8.	*Langlois v. Canada* [1998] T.C.J. No. 1049 (TCC), at para.159, aff'd [2000] F.C.J. No. 1806 (FCA), paras. 8-10, Brief of Authorities, Tab A8	I	27
9.	*Koetsier v. MNR*, 1973 Carswell Nat 307 (TRB) at para. 14, Brief of Authorities, Tab A9	I	30
10.	*Woolner v. Canada*, 1997 Carswell Nat 2995 (TCC) at paras. 23, 26-29, 36, aff'd 1999 Carswell Nat 1948,, Brief of Authorities, Tab A10	I	30
11.	*Cooper v. The Queen*, [1988] F.C.J. No. 931 (FCTD), at p. 16, Brief of Authorities, Tab A11	I	32
12.	*Littler v. The Queen*, 1978 Carswell Nat 185 (FCA) at paras. 11 and 12; Brief of Authorities, Tab A12	I	49

TAB A	DOCUMENT	VOL. #	PARA.
13.	*Gervais v. The Queen*, 85 DTC 5004 (FCTD), ; Brief of Authorities, Tab A13	I	49
14.	*R. v. McBurney*, [1985] F.C J. No. 821 (FCA) at p. 6, leave to appeal dismissed [1985] S.C.C.A. No. 50 [SCC]; Brief of Authorities, Tab A14	I	50
15.	*Vancouver Society of Immigrant and Visible Minority Women v. M.N.R.*, [1999] 1 S.C.R. 10, at paras 28 and 143, Brief of Authorities, Tab A15	I	49
16.	*Dutil v. Canada* [1991] T.C.J. No. 654, at para.25, Brief of Authorities, Tab A16	I	60
17.	*Lewis v. The Queen*, [1979] 2 S.C.R. 821, at 831, Brief of Authorities, Tab A17	I	60