Significant Tax Changes Affecting The Canadian Resource And Energy Sector

Budget 2014 contained two changes of particular interest to the Canadian resource and energy sectors. First, as expected, Budget 2014 proposes to extend the "super flow-through share" program for another year in order to continue to promote the exploration and development of mineral resources in Canada. Second, in keeping with similar changes in recent budgets, Budget 2014 proposes to enhance the capital cost allowance ("**CCA**") treatment of certain environmentally-friendly equipment and technologies to encourage Canadian businesses to adopt such technologies.

Extension of Super Flow-through Share Program

Budget 2014 proposes to extend the "super flow-through share" program for an additional year. The super flow-through share program was initially introduced in October 2000 in response to a severe downturn in mineral exploration in Canada. The program had expired at the end of 2005, but was re-introduced in the 2006 Budget in respect of flow-through shares issued pursuant to agreements made after May 1, 2006 and on or before March 31, 2007. The program was extended for additional one-year periods in each of the 2007 to 2013 Budgets.

Canada's flow-through and super flow-through share programs provide tax incentives to promote the exploration and development of mineral resources in Canada, particularly by encouraging new equity investment in junior mining companies. Under Canada's flow-through share program, a company is permitted to renounce or "flow-through" certain expenses associated with its Canadian exploration activities to investors. In turn, investors can generally deduct such expenses in calculating their own taxable income.

The super flow-through share program provides an additional benefit to those who invest in flow-through shares. Under this program, an investor may claim a 15% tax credit in respect of certain grassroots exploration expenses incurred by the issuer of the shares in Canada and renounced to the flow-through shareholder. The tax credit may be applied to reduce certain federal income taxes otherwise payable by the investor.

Grassroots mining expenditures include expenses incurred in conducting certain mining exploration activities for the purpose of determining the existence, location, extent or quality of a mineral resource.

Budget 2014 proposes to extend the super flow-through share program to apply in respect of flow-through share agreements entered into on or before March 31, 2015. Under a "look-back" rule, funds raised under the terms of the program in the first three months of 2015 may be used to support eligible exploration up to the end of 2015.

Environmentally-Friendly Equipment And Technologies

A preferential set of rules govern the CCA that may be claimed in respect of certain clean energy generation and conservation equipment. In particular, CCA is generally permitted to be claimed at accelerated rates under CCA Class 43.2 in respect of eligible equipment that generates or conserves energy by (i) harnessing a renewable energy source (e.g., wind, solar), (ii) using fuel from waste (e.g., landfill gas, lumber waste), or (iii) making efficient use of fossil fuels. CCA may generally be claimed in respect of property in CCA Class 43.2 at a rate of 50% per year on a declining-balance basis.

Currently, Class 43.2 includes equipment that uses wave or tidal energy to produce electricity. Budget 2014 proposes to expand Class 43.2 to include water-current energy equipment used primarily for the purpose of converting the kinetic energy of flowing water into electricity without the use of a physical barrier (such as a dam) or flow diversion. In addition to the water-current energy equipment itself, eligible property would also include support structures, submerged cables, transmission equipment, and control, conditioning and battery storage equipment relating to such equipment.

Budget 2014 also proposes to expand the scope of waste gasification technology included in Class 43.2. At present, Class 43.2 includes equipment used to convert organic or fossil based materials ("**eligible waste**") into gaseous fuel ("**producer gas**") that is used in eligible cogeneration and thermal energy facilities. Under the proposals contained in Budget 2014, Class 43.2 would be amended to include property used to gasify eligible waste for other uses, such as the sale of producer gas for domestic or commercial use. Eligible property would include equipment used primarily to produce producer gas, as well as related piping and storage equipment, feeding equipment, ash-handling equipment and equipment to remove non-combustibles and contaminants from the producer gas. Under these rules, accelerated CCA would only be available if, at the time the property first becomes available for use, it complies with all applicable Canadian environmental laws.

These changes will apply to property acquired on or after February 11, 2014 that had not been used or acquired for use before this date.

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a cautionary note

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