the link

No. 41 January 2014 www.justice.gc.ca/eng/csj-sjc/harmonization/

The Bijural Revision Services Unit of the Legislative Services Branch of the Department of Justice is pleased to keep you posted on the most recent harmonization and bijuralism news.

Legislation

Recent Amendments Target the Definitions of "estate" and "trust"

Bill C-4, *A second act to implement certain provisions of the budget tabled in Parliament on March 21, 2013 and other measures* received Royal Assent on December 12th, becoming SC 2013, c 40. A lengthy act, our focus is on amendments to the definitions of "trust" and "estate" at subsection 248(1) of the *Income Tax Act*[1] which came into force as of Royal Assent.

The definition of "estate" is amended to include "for civil law, a succession." This amendment is bijural in nature. There is no amendment to the French version, as the French term "*succession*" is the appropriate rendering of both "estate" and "succession".

The definition of "trust" is amended to include "unless the context otherwise requires, an estate." This is to ensure that, as a general matter, provisions of the Act that apply to trusts, also apply to estates and successions.[2]

We offer two observations regarding these amendments.

First, the new definition of "estate" – which brings the civil law "succession" within the meaning of the common law term "estate" – is a departure from the general rule for bijural drafting. The general approach is to ensure that the appropriate civil law and common law terms are both reflected throughout the legislative text, in both official languages. Under this approach, the term "succession" would be added to each occurrence of the word "estate" and the amended the definition of "trust" would have referred to both estates and successions. Departures from the general approach are however justified where harmonizing each occurrence of a private law term would unnecessarily burden the legislative text or it is otherwise impractical to do so.

Our second observation is that while the Act purports to define "estate" and "trust," it does not strictly speaking do so. The terms "trust" and "estate" draw their meaning first and foremost from private law. The definitions in the Act do not set out or restate these private law meanings. The subsection 248(1) definitions of trust and estate serve only to expand the meaning of those terms for tax purposes.

[1] RSC 1985, c 1 (5th Supp), as amended, hereinafter the "Act". Unless otherwise stated, statutory references throughout are to the Act. These proposals – with explanatory notes - were previously included in draft legislative proposals released September 13, 2013.

[2] Although the September 13th explanatory notes do not so state, these measures seem to be a response to *Lipson v. The Queen*, 2013 TCC 20, see "Succession not a Trust for Tax Purposes" *The Link*, No. 40 (April 2013) 2-3.

Bijural Amendments Receive Royal Assent

Bill C-48 received Royal Assent on June 26, 2013, becoming SC 2013, c 34. Bijural amendments proposed in Part 4 harmonize the concepts of "joint and several liability / solidary liability", "tangible property / corporeal property", "intangible property / incorporeal property", "personal property / movable property", "real property / immovable property", and "interest / right." As well, the definition of "interest in real property" at subsection 248(4) is amended, and a separate concept of "real right in immovables" is added at subsection 248(4.1) to better envisage civil law rights in immovable property.

At Part 5, new rules are adopted (at subsections 248(30) *et seq*.) to ease common law rules as they apply for purposes of establishing whether a taxpayer has made a gift to a qualified donee, for tax deduction and credit purposes.[3]

CRA News

Administrative Guidance on the Taxation of French Usufruct

In an internal memorandum dated April 23, 2013, the CRA determined that section 43.1 applies to determine the tax consequences of a usufruct created under French law.

The situation involved a Canadian resident taxpayer who transferred an immovable property situated in France to her children through the French regime of "*donation-partage*" under which a usufruct is created in the donor's favour for the donor's lifetime.

The CRA concluded that the *donation-partage* resulted in a disposition of the property for Canadian tax purposes. The CRA noted that under subparagraph 69(1)(*b*)(ii), a donor of property is generally deemed to have received proceeds of disposition equal to the fair market value of the donated property, and that the deemed proceeds would be reduced to reflect the value of any retained interest or right, or any other charge against the property.

To determine the appropriate tax consequences of the disposition, the CRA adopted a two-step approach:

> *(our translation)*
>
> *1. Determining the characteristics of the foreign arrangement under foreign commercial law; and*
>
> *2. Comparing these characteristics with the categories of arrangements recognized under Canadian commercial law, considering the law of the relevant provincial jurisdiction, and the particular facts and circumstances, for the purposes of classifying the foreign arrangement in one of these categories.*

The CRA determined that the French *donation-partage* resembled both the Quebec civil law gift with retention of usufruct (addressed at subsection 248(3)) and the common law gift with retention of life interest (addressed at section 43.1).[4] The application of subsection 248(3) being limited to "usufructs governed by the laws of the Province of Quebec," the CRA relied on section 43.1 to determine the tax consequences of the *donation-partage*, finding that its position

> *(our translation)*
>
> *…conforms with the legislator's intention not to allow for a deferral of the accrued gain related to any life interest in real property, as well as the underlying tax policy requiring that the principle apply to all Canadian taxpayers, even where the arrangement is constituted in a foreign common law or civil law jurisdiction.*

[3] For more details, see "Bijural Amendments Back on Parliament's Agenda" and "Easing of Common Law Requirement for Gifts in Certain Circumstances" in *The Link*, No. 39 (January 2013) 1-2.

[4] Both provisions create an exception to the tax consequences resulting under subparagraph 69(1)(*b*)(ii).

Jurisprudence

Tax Authorities Obtain Revocation of Declaratory Judgment

When considering the impact of Canadian bijuralism on the application of federal tax legislation, it is important to consider not only specificities of legal concepts, institutions and terminology, but also remedies available to taxpayers.

In *A. v. B.*, 2013 QCCS 575, the Quebec Superior Court ordered the revocation of an April 4, 2011 declaratory judgment that rescinded a series of financial transactions in the 2005-2007 years. The purpose of the declaratory judgment was to avoid unintended tax consequences. It was obtained by the affected taxpayers without prior notice to tax authorities, granted the taxpayers anonymity, and was not published.[5]

In ordering the retraction of the consent judgment,[6] Justice Paquette recognized that the fisc was an interested party in the demand for consent judgment. She also did not disguise her dismay with the situation before her:

> *(our translation)*
>
> *[42]During the hearing before the Honourable Christiane Alary, the parties proceeded, for all practical purposes, ex parte. The absence of the tax authorities, having the greatest interest and whose interests were directly opposed to the parties' motion, was glaring.*
>
> *(...)*
>
> *[46]The parties then obtained their judgment on April 4, 2011, which granted the 25 conclusions requested, in accordance with the draft judgment submitted.*
>
> *[47] It is in this disgraceful context that the CRA and the ARQ were not in a position to prevent the judgment, obtained in secret.*
>
> *(...)*
>
> *[50] The judgment which the ARQ and the CRA seek to have revoked potentially deprives them of millions of dollars in tax claims. The parties cannot seriously argue that the judgment does not affect their interests. The interest of the ARQ and the CRA is obvious.*

Regarding the taxpayers' final argument that the tax authorities did not act with diligence in seeking retractions of the declaratory judgments, Madam Justice Paquette concluded as follows:

> *(our translation)*
>
> *[62] Moreover, in light of the shenanigans deployed in obtaining a judgment while keeping the tax authorities in ignorance, any opposition based on the lateness of the motions in revocation must be considered inadmissible.*

The *A. v. B.* decision was appealed to the Quebec Court of Appeal, but the appeal was discontinued on October 3, 2013.[7]

Case Update – Services environnementaux AES

On November 28, the Supreme Court of Canada dismissed the appeals in *Agence du revenu du Québec v. Services environnementaux AES inc.* and *Agence du revenu du Québec v. Riopel*.[8] An analysis of the decision will appear in the next issue.

Case Update – Envision Credit Union

The Supreme Court of Canada dismissed the appeal from the Federal Court of Appeal decision in *Envision Credit Union v. The Queen*,[9] confirming, *inter alia*, that the undepreciated capital cost of property of certain

[5] It is interesting to note that the request for the declaratory judgment in this matter was filed on March 15th, 2011, just thirteen days after the Quebec Court of Appeal ruled in *Services environnementaux AES inc.*, 2011 QCCA 394. See "Rectification Achieved Under the Rules of the Civil Code of Québec" *The Link*, No. 36 (July 2011) 4. On November 28th, the Supreme Court of Canada dismissed the appeal of the *Agence du revenu du Québec* in *AES*, 2013 SCC 65.

[6] In accordance with the rules at sections 489 *et seq.* of the Quebec *Code of Civil Procedure*, RSQ c C-25, as amended.

[7] CAQ 500-09-023398-134.

[8] 2013 SCC 65.

merged entities flowed through to Envision Credit Union, the entity resulting from the merger by operation of the Act. It was ultimately not necessary to refer to corporate law principles to arrive at this conclusion.

In the circumstances, meeting provincial requirements for the merger also satisfied the conditions at subsection 87(1), including the paragraph 87(1)(*a*) requirement that all property of the predecessor corporations become the property of new corporation. The Court rejected the taxpayer's argument that this interpretation rendered subsection 87(1) redundant. In the Court's view (para [38]), although current corporate requirements for amalgamation were such that the conditions at section 87(1) would be met, this might not always be the case nor does this result require a different interpretation of corporate law:

> *(…) The ITA exists to impose tax consequences based on corporate law; it does not exist to cause those corporate laws to be interpreted differently.*[10]

In *obiter*, the Court also rejected the tracing approach theory advanced by the Minister that had found favour in the Court of Appeal. The Supreme Court asserting that "[i]t is a basic rule of company law that shareholders do not own the assets of the company" and that exceptions to the rule, i.e. "look-through" rules, must be explicit.[11]

Case Update – Clearwater Seafoods Holdings Trust

The Federal Court of Appeal has referred back to the Tax Court of Canada the matter of the application of Rule 29 of the Tax Court of Canada Rules where the taxpayer in an appeal file has ceased to exist. According to Justice Sharlow: "[t]he appeal in the Tax Court is to be allowed to continue if there is a legal person or group of persons who may appropriately be named as the appellant in the place of the Taxpayer trust."[12]

[9] 2013 SCC 48, aff'g, on other grounds, 2011 FCA 32, and 2010 TCC 576. See "Relevance of Corporate Law Principles Confirmed" *The Link*, No. 38 (June 2012) 3-4.
[10] Para [38].
[11] Para [57].
[12] Para [15]. For a summary of the decision appealed from see: "Cautionary Tales for Taxpayers that Cease to Exist in Private Law" *The Link*, No. 40 (April 2013) 1-2.

Publications

Analyses of the Impact of Provincial Private Law on Federal Tax Law

Three articles in recent issues of the Canadian Tax Journal will be of interest to those concerned with Canadian bijuralism.

The **Honourable Robert Décary**'s article, "The Federal Court of Appeal to the Rescue of Civil Law" (2013) 61 (Supp.) *Canadian Tax Journal* 71-80, surveys key decisions of the Federal Court of Appeal in the last twenty years which have raised the stature of civil law in the practice of federal law.

Manon Thivierge's "Lawyers are from Mars, but Tax Lawyers Are from Venus" (2013) 61 (Supp.) *Canadian Tax Journal* 379-90 considers the defining feature of tax practice, which she describes (at 380) as: "the true complementarity between taxation statutes and other legislative frameworks."

In "Rectification of Tax Mistakes Versus Retroactive Tax Laws: Reconciling Competing Visions of the Rule of Law" (2013) 61:3 *Canadian Tax Journal* 563-598, **Professors Catherine Brown and Arthur Cockfield** review provincial trends and consider whether rectification might allow taxpayers to overcome unanticipated effects of retroactive tax legislation.

Website News

As of May 1st, we abandoned the familiar Bijurilex website and moved its content to the main website of the Department of Justice, under the title "Bijuralism and Harmonization" included in the module "Canada's System of Justice".

Our new location features updated content, an enhanced visual interface, and, most significantly, an improved search engine. The mission of our web presence, however, remains unchanged: To provide information about the implications and challenges of bijuralism as it relates to federal legislation.

You can still find past issues of *The Link* but it is now also possible to identify articles of interest through a keyword search.

Visit us at http://www.justice.gc.ca/eng/csj-sjc/harmonization/index.html.