the link

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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.

International

OECD Commentary on the Meaning of "beneficial owner"

On July 15th, the OECD Council approved the *2014 Update to the OECD Model Tax Convention* (the "2014 Update"). The changes include new guidance on the meaning of "beneficial owner" in relation to dividend, interest and royalty income.

Among the challenges of interpreting "beneficial owner" in a tax treaty context is the issue of whether a domestic or an international meaning should be adopted.[1] This issue has been considered in a number of tax cases, notably in the Canadian decisions *The Queen v Prévost Car Inc.* 2009 FCA 57 and *Velcro Canada Inc. v The Queen*, 2012 TCC 57.[2] Reliance on a domestic law meaning can be problematic. It creates the potential for a multiplicity of interpretations across the treaty network and presents a real difficulty in jurisdictions having no domestic law concept of "beneficial owner." In the Canadian bijural context, these difficulties are compounded. While the concept of beneficial owner has meaning in the common law provinces and territories, it is unknown to the civil law of Quebec.

The 2014 Update is clear: "beneficial owner" must be interpreted independently of the domestic law of a particular country. Paragraph 12.1 of the Commentary to Article 10 (Dividends) now states (changes are indicated in boldface):

> ***12.1 Since the term "beneficial owner" was added to address potential difficulties arising from the use of words "paid to…a resident" in paragraph 1, it was intended to be interpreted in this context and not to refer to any technical meaning that it could have had under the domestic law of a specific country (in fact, when it was added to the paragraph, the term did not have a precise meaning in the law of many countries).*** *The term "beneficial owner" is* ***therefore*** *not used in a narrow technical sense* ***(such as the meaning that it has under the trust law of many common law countries****), rather, it should be understood in its context,* ***in particular in relation to the words "paid …to a resident",*** *and in light of the object and purposes of the convention, including avoiding double taxation and the prevention of fiscal evasion and avoidance.*[3]

It is noteworthy that amended paragraph 12.1 does not include a sentence that appeared in the 2011 draft version of paragraph 12.1 and that referred to possible continued relevance of domestic law meaning.[4]

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[1] "The OECD and the TCC Consider the Meaning of 'beneficial owner'" *The Link*, No. 36 (July 2011) 1-2.

[2] For summaries of these decisions, see, respectively, "Court of Appeal Rules in *Prévost Car Inc.*" *The Link*, No. 30 (April 2009) 1, and "Recipient of Royalties Held to be Beneficial Owner" *The Link*, No. 38 (June 2012) 2-3.

[3] The same changes appear at paragraph 9.1 of the Commentary to Article 11(Interest).

[4] The now deleted sentence was included in *Clarification of the Meaning of "Beneficial Owner" in the OECD Model Tax Convention*: *Discussion Draft* (Paris: OECD, April 29, 2011) at 3. The deleted sentence read as follows: "This does not mean, however, that the domestic law meaning of "beneficial owner" is automatically irrelevant for the interpretation

Other clarifications on the meaning of "beneficial owner" found in the revised Commentary to Article 10 include the following:

- in the case of a recipient who is an agent or nominee, "the direct recipient of the dividend is not the "beneficial owner" because that recipient's right to use and enjoy the dividend is constrained by a contractual or legal obligation to pass on the payment received to another person." (paragraph 12.4);
- even if the recipient of a dividend is the "beneficial owner," the limitation of tax provided for by paragraph 2 of Article 10 will be denied in cases of abuse of that provision or improper use of the Convention (paragraph 12.5);[5]
- the meaning "beneficial owner" in the context of Article 10, must be distinguished from the meaning given to the term in the context of other instruments (paragraph 12.6).[6]

of that term in the context of the Article: that domestic law meaning is applicable to the extent that it is consistent with the general guidance included in this Commentary." The 2014 Update (at 2) notes that "commentators generally supported the deletion of the sentence referring to domestic law."

[5] The introduction to the 2014 Update also advises that "It should be noted that the changes related to the meaning of "beneficial owner" that are included in the 2014 Update do not prejudge in any way the outcome of the work on Action 6 (Prevent Treaty Abuse) of the Action Plan on Base Erosion and Profit Shifting" (at 2). Interesting to note in this connection that *Finance Canada News Release 2014-113* (dated August 29, 2014) states "After engaging in consultations on a proposed anti-treaty shopping measure, the Government will instead await further work by the Organisation for Economic Co-operation and Development and the Group of 20 (G-20) in relation to their Base Erosion and Profit Shifting initiative."

[6] The same changes are introduced to the Commentary to Articles 11 (Interest) and 12 (Royalties).

Jurisprudence

Rectification: Tax-Driven Evolution in the Civil Law

In *Agence du revenu du Québec v. Services environnementaux AES inc.* and *Agence du revenu du Québec v. Riopel*, 2013 SCC 65, the Supreme Court of Canada dismissed the Quebec revenue agency's appeals of two decisions[7] that allowed taxpayers to correct documentation to avoid unanticipated tax consequences.

Writing for the Court, Justice Lebel noted that the evidence presented by the taxpayers in support of their motions for rectification was uncontested (para [26]) and summarized the legal basis for rectification in Quebec as follows:

> *[52] In the final analysis, the court's intervention was based on the fundamental rules of contract law, which is premised on a principle of consensualism and in which a fundamental distinction exists between the exchange of consents and the written expression of that exchange. Quebec's law of evidence in civil matters reinforces this distinction between internal will — or true intention — and declared will. … The private writing is also a form of expression of a common intention. If such a writing contains an error, particularly one that can, as here, be attributed to the taxpayer's professional advisor, the court must, once the error is proved in accordance with the rules of evidence in civil matters, note the error and ensure that it is remedied. In the civil law, the tax authorities do not have an acquired right to benefit from an error made by the parties to a contract after the parties have corrected the error by mutual consent.*

The Supreme Court also cautioned taxpayers:

> *[54] … Taxpayers should not view this recognition of the primacy of the parties' internal will — or common intention — as an invitation to engage in bold tax planning on the assumption that it will always be possible for them to redo their contracts retroactively*

[7] 2011 QCCA 394 and 2011 QCCA 954.

> *should that planning fail. A taxpayer's intention to reduce his or her tax liability would not on its own constitute the object of an obligation within the meaning of art. 1373 C.C.Q., since it would not be sufficiently determinate or determinable. Nor would it even constitute the object of a contract within the meaning of art. 1412 C.C.Q. Absent a more precise and more clearly defined object, no contract would be formed.*

In its judgment, the Court also highlighted certain realities of Canada's bijural landscape. First, on the role of courts when dealing with private law issues that intersect with federal tax legislation, Justice Lebel wrote:

> *[43] … the specific avenues established by Parliament for tax appeals cannot be circumvented …This means that a court dealing with a challenge relating to civil aspects of a transaction with tax implications does not have the authority to rule on notices of assessment that were issued or notices of objection that were filed in respect of that transaction. The validity and effects of the notices in question must instead be determined, if necessary, by the courts that have been assigned jurisdiction over such matters. It would also be up to those courts to consider the consequences of judgments rendered by the civil courts with respect to the transactions that led to the issuance of the notices of assessment.*

It is interesting to note that the Alberta Court of Queen's Bench recently asserted its right to interpret the *Income Tax Act* (Canada).[8] As well, courts have sometimes refused to address private law issues germane to federal tax disputes.[9]

Second, Justice Lebel succinctly described the position of tax authorities (both federal and provincial) at the intersection between tax law and provincial private law. Justice Lebel wrote:

> *[45] … Under the civil law itself, the agencies can also prove that simulation existed and demonstrate the true nature of transactions they allege to be shams. In addition, tax legislation may recharacterize contractual or economic transactions for its own purposes by overriding the legal categories established by the common law and the civil law. With the exception of such situations, however, tax law applies to transactions governed by, and the nature and legal consequences of which are determined by reference to, the common law or the civil law.*

AES is an important decision, as much for Quebec civil law as for the application of federal legislation. Writing before the release of the Supreme Court's judgment, one author anticipated that "Whichever way the court elects to go, its decision should become one of the landmarks of the interaction between the practice of tax law and other legislative frameworks."[10] On the strength of the Supreme Court's ruling in *AES*, the appeal of another Quebec rectification case, *Mac's Convenience Stores inc. v. Couche-Tard*, is moving forward.[11] The hearing is set for March 24, 2015.

The Supreme Court of Canada: "a federal and bijural institution"

In the decision *Reference re Supreme Court Act*, 2014 SCC 21, the Supreme Court highlighted the importance of Canadian bijuralism and the influence that bijuralism has – has always had - on the composition of Canada's highest court.

On the initial guarantee that two of five justices would be from Quebec,

> *[55] Government and opposition members alike saw the two seats (one third) for Quebec judges as a means of ensuring not only the functioning, but also the legitimacy of the*

[8] RSC 1985, c 1 (5th Supp), as amended (hereinafter the "Act"). The Alberta decision is *Graymar Equipment (2008) Inc. v AGC*, 2014 ABQB 154.

[9] See *Sheila Holmes Spousal Trust v Canada (Attorney General)*, 2013 ABQB 489 and *Stephkan Holdings Inc. v Canada Revenue Agency*, 2013 QCCS 643. In both cases, the courts found that the taxpayer's motions were attempts to circumvent the tax appeals process and the exclusive jurisdiction of the Tax Court of Canada.

[10] Manon Thivierge, "Lawyers are from Mars, but Tax Lawyers Are from Venus" (2013) 61 (Supp.) *Canadian Tax Journal* 379-90 at 383.

[11] 2012 QCCS 2745. The appeal (CAQ 500-09-022851-125) had been in abeyance pending the decision of the Supreme Court in *AES*. An unofficial English translation of the Superior Court judgment is available at: http://soquij.qc.ca/fr/services-aux-citoyens/english-translation. For a summary of the Superior Court's decision see: "Provincial Superior Courts Confronted by Rectification Requests" *The Link*, No 39 (January 2013) at 3.

> *Supreme Court as a federal and bijural institution.*

On the evolution in the Court's powers and its role in private law matters,

> *[85] With the abolition of appeals to the Judicial Committee of the Privy Council, … The Court assumed a vital role as an institution forming part of the federal system. It became the final arbiter of division of powers disputes, and became the final word on matters of public law and provincial civil law. Drawing on the expertise of its judges from Canada's two legal traditions, the Court ensured that the common law and the civil law would evolve side by side, while each maintained its distinctive character. The Court thus became central to the functioning of legal systems within each province and, more broadly, to the development of a unified and coherent Canadian legal system.*

In finding that matters concerning the composition of the Court benefited from constitutional protection, the Court observed:

> *[93] … the Court's composition has been long recognized as crucial to its ability to function effectively and with sufficient institutional legitimacy as the final court of appeal for Canada. As explained above, the central bargain that led to the creation of the Supreme Court in the first place was the guarantee that a significant proportion of the judges would be drawn from institutions linked to Quebec civil law and culture. The objective of ensuring representation from Quebec's distinct juridical tradition remains no less compelling today, and implicates the competence, legitimacy, and integrity of the Court.*
>
> …
>
> *[104] Changes to the composition of the Supreme Court must comply with s. 41(d) of the Constitution Act, 1982. Sections 4(1), 5 and 6 of the Supreme Court Act codify the composition of and eligibility requirements for appointment to the Supreme Court of Canada as they existed in 1982. Of particular relevance is s. 6, which reflects the Court's bijural character and represents the key to the historic bargain that created the Court in the first place. As we discussed above, the guarantee that one third of the Court's judges would be chosen from Quebec ensured that civil law expertise and that Quebec's legal traditions would be represented on the Court and that the confidence of Quebec in the Court would be enhanced.*

Even Justice Moldaver, in dissent, stated "The coexistence of two distinct legal systems in Canada — the civil law system in Quebec and the common law system elsewhere — is a unique and defining characteristic of our country" (at para [113]).

CRA News

Partnership Assets Attributed to Partners for Treaty Purposes

Article XIII of the Canada-Singapore Income Tax Convention provides that "[g]ains from the alienation of shares of a company, or of an interest in a partnership or a trust, the property of which consists principally of immovable property as defined in paragraph 2 of Article VI, may be taxed in the Contracting State in which such immovable property is situated."

In a recent opinion,[12] the Canada Revenue Agency (the "CRA") considered the tax treatment of capital gains realized by a Singapore resident on the disposition of shares of a Canadian resident corporation ("Canco"). Canco's assets consisted of interests in two partnerships established under the laws of Quebec. The property of the partnerships consisted of immovable property situated in Canada.

The CRA determined that the better view is that partnerships are not distinct legal persons for purpose of the Convention and that partnership patrimony can be assimilated to the patrimony of the partners. As such, the property of Canco was found to consist principally of immovable property situated in Canada, and the gain from the disposition of the Canco shares was held to be taxable in Canada.

[12] Agence du revenu du Canada, *Document 2013-0516151I7*, le 14 avril 2014, Direction des décisions en impôt.

Legislation

Corrections to the Civil Code of Québec Affect 1,580 Articles in the English Version

By Information Notes dated May 1, 2014, 1,580 articles of the English version of the Civil Code of Québec "were corrected for purposes of terminological uniformity, quality of language, and minor corrections with a view to reconciling the French and English versions."[13] The French version also saw some changes.

These changes were made pursuant to Minister of Justice's authority to provide for updating of laws and regulations included in the Compilation of Québec Laws and Regulations. In particular, the basis of the current updates was to "correct obvious errors of reference, data-entry and transcription, and errors of a similar nature."[14]

An updated version of the Civil Code is available on the *Publications Québec* web site. The May 1st changes can be identified by the mention "I.N. 2014-05-01" in the English version and by "N.I. 2014-05-01" in the French version.

New BC Wills, Estates and Succession Act

The *Wills, Estates and Succession Act*, RSBC 2009, c 13 came into effect on March 31, 2014. On its adoption in 2013, the legislation was described as

> *...modernizing B.C.'s current laws - which have provisions dating back to the 1800s - on inheritance and succession planning. By streamlining seven outdated acts into one single act, the new law will make estate planning easier for the general public to understand.*[15]

New Quebec Code of Civil Procedure

A new Code of Civil Procedure was adopted by the Quebec National Assembly in February,[16] and, since May 23rd, 2014, is available in the Compilation of Québec Laws and Regulations at chapter c C-25.01. It is expected that all of the provisions of the new Code will be in force by autumn 2015.

Compilation of Quebec Laws and Regulations

The *Policy Concerning the Compilation of Québec Laws and Regulations*[17] came into force on April 1st, 2014, replacing the policy dated January 3, 2013. It makes for interesting reading and includes detailed rules for the citation of Quebec laws and regulations. Regarding the Civil Code of Québec, the Policy points out that the Code and the *Act respecting the implementation of the reform of the Civil Code* have no alphanumeric designation in the Compilation.[18]

Quebec Registration Requirement for Commercial Trusts

Effective July 1, 2014, trusts operating a commercial enterprise in Quebec must register with the *Régistraire des entreprises*, unless the trust is administered by a registered registrant.[19] Business trusts, investment trusts, and real estate investment trusts are among those envisaged by the new requirement. See: http://www.registreentreprises.gouv.qc.ca/en/actualites/2014/2014-05-26.aspx.

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[13] http://www2.publicationsduquebec.gouv.qc.ca/documents/catalogue/pdf/politique_en.pdf

[14] *Ibid.* See also sections 2 and section 3(2) of the *Act respecting the Compilation of Québec Laws and Regulations*, CQLR, c R-2.2.0.0.2.

[15] http://www.newsroom.gov.bc.ca/2013/03/date-set-for-modernized-wills-and-estate-law.html

[16] LQ 2014, c 1 (former Bill 28).

[17] http://www2.publicationsduquebec.gouv.qc.ca/documents/catalogue/pdf/politique_en.pdf

[18] *Ibid* at 2.

[19] Subsection 21(8) of the *Act respecting the Legal Publicity of Enterprises*, CLRQ, c P-44.1.