CANADIAN TAX *focus*

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Pre-2017 ECP Crystallizations for CCPCs

For CCPCs, one negative aspect of the replacement of the present eligible capital property (ECP) regime with a new CCA class is that dispositions of this property after 2016 may generate investment income rather than active business income (ABI). As a result, taxpayers who are considering selling a business relatively soon after the new rules begin to apply may consider entering into a crystallization transaction before 2017 that locks in ABI treatment. A technical glitch that might have halted such planning has been fixed by revised draft legislation released on July 29, 2016.

Under the existing rules, a sale of ECP for which proceeds exceed cost (the associated eligible capital expenditure) effectively causes 50 percent of the difference to be taxed as ABI. However, under new rules that bring ECP into the CCA system and that generally take effect on January 1, 2017, this amount is a taxable capital gain (that is, investment income). Because CCPCs pay a higher effective corporate tax rate on investment income than on ABI (and only part of the excess is refundable on the payment of dividends), taxpayers may consider crystallization transactions.

Assume, for example, that Ms. A is the sole shareholder of Opco. She is approached by a buyer willing to purchase Opco's assets for $20 million, almost all of which is attributable to internally generated goodwill. Because the buyer is investigating other potential target companies, it is expected that the deal cannot be finalized before January 1, 2017. Therefore, Ms. A can have Opco transfer all of its assets, including goodwill, to a newly incorporated subsidiary, Subco. The transfer will be under section 85, with an elected amount of $20 million. The proceeds of disposition are thus $20 million and the ACB is zero; therefore, a gain of $10 million (1/2 × ($20 million − 0)) is recognized by Opco, and this gain is ABI (which is the goal of the transaction).

The technical issue with this transaction is to make sure that there is no capital gain to Subco in 2017 when the goodwill is sold to an outside buyer. Because Opco and Subco are related parties, variable A.1 in the definition of "cumulative eligible capital" (CEC) in subsection 14(5) provides for a grind to Subco's CEC balance. Thus, Subco's CEC balance at the end of 2016 will be $10 million ((3/4 × $20 million elected amount) less a grind of (1/2 × $10 million gain realized by Opco)). In the absence of special rules, this ground-down CEC balance will be used to determine future capital gains: the capital cost of the property included in new CCA class 14.1 on January 1, 2017 is essentially four-thirds of the CEC balance on December 31, 2016 (subsection 13(37)). Fortunately, the revised draft legislation provides the required upward adjustment in capital cost in proposed paragraph 13(41)(a) of the Act. (The earlier draft legislation released on March 22, 2016 did not include this provision: CRA document 2016-0641851E5, June 7, 2016.)

The paragraph prtovides that if the amount determined for A in the CEC definition in subsection 14(5) would have been increased immediately before 2017 if the property had been disposed of immediately before that time, the capital cost of the property is deemed to be increased by four-thirds of the amount of that increase. A $5 million increase in A (through a reversal of the grind) would have occurred if there had been a disposition of the ECP by Subco before 2017. Thus, the capital cost of the property included in new class 14.1 is $20 million ((4/3 × $10 million CEC balance on December 31, 2016) + (4/3 × $5 million grind)). Therefore, when the class 14.1 asset is sold for $20 million, there is no capital gain.

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Arm's-Length Rate Is Not the Limit for Interest Deductibility

In *ENMAX Energy Corporation v. Alberta* (2016 ABQB 334), the Alberta Court of Queen's Bench considered the meaning of "reasonable" for the purposes of interest deductibility under paragraph 20(1)(c) of the Income Tax Act. The court concluded that interest rates that exceed what an arm's-length person would pay may still be reasonable; arm's-length rates are relevant in informing the analysis but are not determinative.

In 2004, 2006, and 2007, ENMAX loaned funds to two of its subsidiaries, ENMAX Energy and ENMAX PSA, under unsecured subordinated debt obligations of approximately 10 years ("the notes").

Pursuant to the Alberta Electric Utilities Act (EUA) and its Payment in Lieu of Tax Regulation, government-owned entities, which were otherwise exempt from provincial and federal tax, were required to make payments in lieu of tax (PILOTs) equal to what would have been payable under the Income Tax Act and the Alberta Corporate Tax Act. ENMAX Energy and ENMAX PSA deducted interest on the notes in computing their PILOTs for the relevant taxation years, and the Alberta minister of finance reassessed on the basis that the rates of interest were unreasonable. The minister determined reasonable rates on the three notes to be 5.42 percent, 5.26 percent, and 5.24 percent rather than the rates charged of 11.5 percent, 10.3 percent, and 9.9 percent, respectively.

The minister argued that the interpretation of paragraph 20(1)(c), as applied within the EUA, must be considered in light of the provincial policy to deregulate the electrical utility industry. The ABQB rejected this argument and stated that paragraph 20(1)(c) has the same meaning and is informed by the same jurisprudence whether under the EUA or as part of the Income Tax Act for taxable entities.

The ABQB rejected the minister's arguments that the test for determining what is reasonable should include an arm's-length standard. One reason given was that this was not the SCC's holding in *Shell Canada* (1999 CanLII 647). Also, there is an absence of an arm's-length standard in paragraph 20(1)(c)—in contrast to other provisions of the Income Tax Act, such as subsection 247(2). Thus, the court held that an arm's-length rate is prima facie reasonable and may be a relevant factor, but it does not define what is reasonable, nor does it mean that paying more is necessarily unreasonable.

Regarding how the arm's-length rate should be determined, the ABQB, focusing on the actual legal obligation under which the indebtedness arose, rejected the idea that a higher credit rating should be given to the notes on the basis of implicit support from the parent corporation in their repayment: "It would be wrong . . . to allow consideration of implicit support to influence opinions about reasonable interest rates, regardless of whether bond purchasers might make such an assumption." Because in this case the parent was the lender, it would not be appropriate for the lender to count on support from itself.

The court also relied on *Gabco* ([1968] CTC 313 (Ex. Ct.)) to conclude that the interest rates were reasonable. According to *Gabco*, the minister or a court should not substitute its judgment for what is reasonable. Instead, it must determine whether no reasonable business person would have contracted to pay such an amount, having only the business considerations of the taxpayer in mind. The court reached its conclusion notwithstanding that the interest rates exceeded the rates that likely would have been paid in a similar arm's-length transaction, because (1) the notes were part of an idiosyncratic business strategy that established ENMAX as the principal funding source, and (2) the notes had a number of conditions, such as the level of debt, that would have made them difficult to sell on the market. The court also used these factors to reiterate that one should not put too much emphasis on the arm's-length standard.

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CRA's Bad News for Canadians Investing in US Real Estate

Two popular vehicles for investments in US real estate are limited liability limited partnerships (LLLPs) and limited liability partnerships (LLPs). However, the CRA's announcement at the May 26, 2016 International Fiscal Association (IFA) round table that it will consider many of these entities corporations for Canadian tax purposes has sharply increased their effective tax rate. As a result, restructuring that requires forgoing limited liability may be necessary. The restructuring will have to be done by 2018 in order to take advantage of administrative relief provided by the CRA.

For investments in US real estate, US legal counsel often recommend the use of disregarded limited liability corporations (LLCs), which offer both legal liability protection and flowthrough treatment for US tax purposes. However, for the reasons discussed below, LLCs are not tax-efficient for Canadian investors, because LLCs are treated as corporations from a Canadian tax perspective. As an alternative, Canadian investors have historically preferred to make use of US LLLPs or LLPs, which have typically been viewed as partnerships for Canadian purposes but still offer legal liability protection akin to that of an LLC.

The CRA had previously provided little specific guidance on how LLPs or LLLPs should be characterized for Canadian tax purposes. However, in addressing the tax treatment of Delaware limited partnerships and general partnerships, the CRA had stated that the attributes of entities formed under the Delaware Revised Uniform Partnership Act (DRUPA) or under the

Delaware Revised Uniform Limited Partnership Act (DRULPA) more closely resemble those of a partnership under Canada's common law than those of a Canadian corporation. Accordingly, the CRA indicated that entities governed by DRUPA or DRULPA would generally be treated as partnerships for Canadian tax purposes (see CRA document nos. 2000-0056715, November 28, 2000, and 2004-0104691E5, August 14, 2008, and *Income Tax Technical News* no. 34). Because the CRA's statement was broad enough to encompass both LLPs and LLLPs, Canadian taxpayers proceeded on this basis.

All structuring that uses LLPs and LLLPs is now disrupted by the CRA's announcement that, after much deliberation, it has concluded that Florida and Delaware LLPs and LLLPs should be treated as corporations for Canadian purposes—due in large part to the limited liability protection that they afford their members. This statement effectively puts Canadian investors in the same situation that they would have been in had they originally used disregarded LLCs instead. Unfortunately, the double taxation resulting from the use of LLCs or similar vehicles is substantial for individual and corporate Canadian investors.

Consider the effect on a Canadian individual earning rental income through an LLC (or an LLP or LLLP). For US tax purposes, he or she would be taxed at rates of up to 43.4 percent (including the 3.8 percent net investment income tax) on the rental income. Further, in Canada the entity is considered to be a corporation and a foreign affiliate pursuant to subsection 95(1) of the Act. Thus, the Canadian individual will be taxed in Canada on the income either as a dividend when the cash is ultimately distributed by the LLC or, if the LLC is also considered a controlled foreign affiliate, as FAPI under subsection 91(1) in the year in which the income is earned. In the latter case, no offsetting deduction for US taxes will be available under subsection 91(4) (because the definition of foreign accrual tax [FAT] in subsection 95(1) encompasses only taxes paid by the affiliate itself; the US tax does not qualify, since it is paid by the individual). Furthermore, the CRA takes the view that although a foreign tax credit (FTC) would be available under subsection 126(1) (see CRA document no. 2013-0480321C6, June 11, 2013), it would be limited to 15 percent. A deduction under subsection 20(11) would be available for the US tax in excess of 15 percent. For a taxpayer resident in Ontario, the effect of these rules is an overall effective tax rate in excess of 66 percent (before state tax implications, if any, are considered).

For a Canadian corporate investor, the results are far worse. In addition to US federal corporate tax at rates up to 34 percent, US branch tax could apply at a rate of 30 percent on after-tax profits (owing to the lack of treaty benefits available for the Canadian corporation pursuant to article IV(6)(b) of the Canada-US treaty). Furthermore, no FTC would be granted in Canada under subsection 126(1), because the tax is considered to be paid in respect of income from a share of a foreign affiliate. In addition, no FAT deduction would be available. Therefore, when one factors in refundable part I taxes levied on CCPCs, the overall effective tax rate on the rental income could exceed 100 percent.

The CRA has orally indicated an intention to provide partnership treatment for existing LLPs and LLLPs if, among other things, the LLP or LLLP is converted before 2018 into an entity recognized as a partnership for Canadian tax purposes—that is, an ordinary limited partnership. Such a step, while fairly straightforward, would force Canadian investors to forgo the legal liability protection that they had originally sought in the first place with the LLPs and LLLPs.

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The New Quebec Land Transfer Tax Act

Quebec's 2016-17 budget seeks to eliminate the most common techniques used to avoid the Quebec land transfer tax (the so-called "welcome tax"). It also adds two exemptions to modernize the regime. These proposed amendments to the Act Respecting Duties on Transfers of Immovables are effective for transfers occurring after budget day (March 17, 2016).

The LTT system dates back to 1976. It had never been substantially amended to correct some often-used loopholes, such as the use of unregistered transfers, nominee corporations acting as bare trusts or holding legal title with negligible FMV, and transactions designed to fall technically within an exemption. Municipalities were generally unable to stop these transactions because they were technically not disallowed.

Previously, an exemption was available in some circumstances if a transferor held 90 percent or more of the voting stock of a corporation at the time of the transfer. However, the exemption was clearly not intended to permit an arm's-length sale of an immovable property through a new intermediary corporation. As a consequence, the budget proposals now require that the 90 percent condition be maintained for at least 24 months following the transfer ("the disclosure mechanism"). Arm's-length persons that want to use this exemption will have to stay involved during this period. Furthermore, the budget restricts the exemption between two closely related legal persons so that only voting rights are considered (prior law also considered direct and indirect FMV).

Another loophole was that LTT was previously payable on the date that the transfer was registered at the Quebec Land Register. This provision was convenient for municipalities because they had easy access to registry information. However, practitioners often took the position that if the transfer was never registered, the LTT would never become payable. One common way to effect an unregistered transfer was to hold legal title to the property in a nominee corporation and then sell the nominee corporation's shares for a nominal amount (with no change in title to the underlying immovable); neither party would register a transfer because the legal title did not change. To capture such transfers of beneficial ownership, the budget provides that the date on which the LTT is payable is the date of the actual transfer of the property. This change codifies some Quebec court decisions, which held that one must consider the moment at which the transfer occurred and not the moment at which title was registered (for example, *Donnacona (Ville) c. Produits Forestiers Alliance inc.*, 2001 CanLII 20641 (QCCA); *Montréal (Ville) c. Fonds immobilier maximma*, 1998 CanLII 13008 (QCCA); and *Foresterie Noranda inc. c. Corporation municipale de Saint-Aimé du Lac des Îles*, 1998 CanLII 13012 (QCCA)).

If parties opt not to report their transfers under the new regime in the hope that they will not be caught, they will be subject to a new penalty duty equal to 150 percent of the LTT (previously, 125 percent of special duties) that would have otherwise been payable. This penalty is in lieu of the usual LTT and is subject to arrears interest.

In the case of an unregistered transfer, the budget introduces a new mechanism for parties to the transaction to report it to the relevant municipality. Only the City of Montreal forms (transfer of immovables and exemptions) appear to have been released so far, but the information in those forms is intended to be reported to any Quebec municipality in which the transfer takes place. The specific wording of the forms to be prepared by any city is not set out in the budget, but the disclosure must contain at least the information outlined here (see page A.83).

Revenu Québec and the municipalities are empowered under the budget proposals to exchange information pertaining to land transfers in order to assist the municipalities in collecting LTT. For instance, if a taxpayer declares a real property disposition in its tax return but does not report the transfer to the municipality, the penalty may be levied.

Finally, the budget introduces a new exemption for transfers between former de facto spouses, provided that the transfer is effected within 12 months of the breakdown of their union. In addition, exemptions will be granted retroactively to international government organizations that have entered into certain agreements in Quebec.

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La nouvelle loi québécoise sur les droits de mutation immobilière

Le budget québécois pour l'année 2016-2017 vise à éliminer l'utilisation de certaines techniques d'évitement des droits de mutation immobilière (communément appelé la « *taxe de bienvenue* » ou « DMI »). Il ajoute également deux exonérations afin de moderniser le régime. Ces amendements proposés à la Loi concernant les droits sur les mutations immobilières s'appliqueront à l'égard des transferts effectués après le jour du discours sur le budget (17 mars 2016).

Le système des DMI remonte à 1976 et n'avait jamais été modifié en profondeur afin de corriger certaines des échappatoires fiscales souvent utilisées, telles que l'utilisation de transferts non-inscrits, l'utilisation de sociétés prête-noms ou détenant le titre pour une JVM négligeable et les opérations techniquement conçues pour bénéficier d'une exonération. Les municipalités n'étaient généralement pas en mesure de prévenir ces opérations puisqu'elles n'étaient pas interdites.

L'une des échappatoires était l'existence d'une exonération dans certaines circonstances lorsque le cédant détenait au moins 90 pour cent des actions émises d'une société ayant droit de vote au moment du transfert. Toutefois, il est clair que l'exonération ne devrait pas être applicable dans un contexte de vente d'immeubles à une personne sans lien de dépendance par l'intermédiaire d'une nouvelle société. Par conséquent, le budget propose d'exiger le maintien de cette condition d'exonération de 90 pour cent pendant au moins 24 mois à la suite du transfert (le « mécanisme de divulgation »). Les personnes sans lien de dépendance désirant se prévaloir de cette exonération devront demeurer « impliquées » pendant cette période. De plus, le budget restreint l'exonération applicable à deux personnes morales étroitement liées en prenant en compte uniquement les droits de vote; les dispositions antérieures prenaient également en compte la JVM directe et indirecte.

Une autre échappatoire était que les DMI étaient dus à compter de l'inscription du transfert au registre foncier du Québec. Ceci était pratique pour les municipalités puisqu'elles avaient facilement accès aux renseignements figurant au registre. Néanmoins, certains praticiens étaient souvent d'avis que si le transfert n'était jamais inscrit, les DMI ne devenaient jamais exigibles. Une manière usuelle de conclure un transfert non inscrit (bien que contestable) était la détention du titre par une société prête-nom et la vente subséquente des actions de la société prête-nom pour un montant nominal (sans changement du titre sur le bien immobilier sous-jacent); aucune des parties n'inscrivait de transfert puisque le propriétaire inscrit ne changeait pas. Afin d'imposer ces transferts de propriété (effective), le budget prévoit dorénavant clairement que les DMI deviennent dus à la date du transfert (effectif) de l'immeuble. Ceci codifie certaines décisions judiciaires québécoises selon lesquelles il convient de prendre en compte le moment où le transfert est survenu et non le moment où le titre a été inscrit (par exemple : *Donnacona (Ville) c. Produits Forestiers Alliance inc.*, 2001 CanLII 20641 (QCCA); *Montréal (Ville) c. Fonds immobilier maximma*, 1998 CanLII 13008 (QCCA); et

Foresterie Noranda inc. c. Corporation municipale de Saint-Aimé du Lac des Îles, 1998 CanLII 13012 (QCCA)).

Si les parties ne déclarent pas leurs transferts en vertu du nouveau régime, elles seront soumises à un nouveau droit constituant une pénalité égal à 150 pour cent des DMI (antérieurement, 125 pour cent à titre de droit supplétif) qui auraient autrement été exigibles, et ce, à la place des DMI usuels et avec les intérêts sur les arriérés.

Dans le cas des transferts non-inscrits, un nouveau mécanisme de divulgation à la municipalité concernée est introduit. Seul le formulaire de la Ville de Montréal semble avoir été publié (transferts d'immeubles et exonération), mais les renseignements figurant sur ce formulaire sont ceux devant être divulgués à toute municipalité québécoise dans laquelle le transfert a lieu. L'utilisation du formulaire préparé par une ville n'est pas obligatoire, mais la divulgation doit comprendre au minimum les renseignements indiqués ici (voir pages A.85-86).

Les modifications proposées par le budget donnent à Revenu Québec et aux municipalités le pouvoir d'échanger des renseignements relativement aux transferts d'immeubles afin d'aider les municipalités à percevoir les DMI. Par exemple, un droit constituant une pénalité peut être imposé lorsqu'un contribuable déclare la disposition d'un bien immobilier sur sa déclaration de revenus, mais ne déclare pas le transfert à la municipalité.

Enfin, le budget introduit une nouvelle exonération pour les transferts entre ex-conjoints de fait, pourvu que le transfert soit effectué dans les 12 mois de la fin de leur union. De plus, des exonérations seront rétroactivement accordées aux organisations internationales gouvernementales qui ont conclu certaines ententes au Québec.

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The Canada Child Benefit and Child Custody

The Act recognizes three child custody categories for separated and divorced couples: (1) parent A with primary custody; (2) parent B with primary custody; and (3) shared custody. These categories generate large differences in Canada child benefit (CCB) payments—significantly larger than the differences in payments under the former Canada child tax benefit program (although the CCB parameters are not indexed to inflation). Parents need to decide which category applies and take steps to have it recognized in CCB payments. (Of course, custody arrangements also affect child support payments.)

For example, suppose that parent A and parent B have three children aged 3, 5, and 10. Parent A has adjusted income (defined in section 122.6) of $140,000; parent B has adjusted income of $50,000. The CCB entitlements for the year beginning July 1, 2016 for the three possible custody situations are shown in the accompanying table (see the calculator; top-up provincial benefits are not included).

Custody	Parent A	Parent B	Total
		dollars	
Parent A with primary custody	5,550	0	5,550
Parent B with primary custody	0	14,400	14,400
Shared custody	2,775	7,200	9,975

The large differences in total entitlements reflect differences in the CCB's income testing: (1) if parent A has primary custody, the entitlement is based on his or her adjusted income; (2) if parent B has primary custody, it is based on his or her adjusted income; and (3) if there is shared custody, each parent gets 50 percent of what he or she would have received if he or she had primary custody (subsection 122.61(1.1)). The custody category is presented to the CRA through the application for CCB benefits (form RC66, "Canada Child Benefits Application"): if one parent has primary custody, that parent alone files the form; in a shared-custody arrangement, both parents file. Of course, the CRA may request information to support the parents' chosen custody category.

Shared custody, in terms of the Act, exists when the two parents are "shared-custody parents" (defined in section 122.6). The determination rests mainly on whether the child resides with the two parents on an "equal or near equal basis." This status is not determined by the separation agreement; it is a question of taxpayer behaviour (*Nixon v. Nixon*, 2014 SKQB 264). In *Brady v. The Queen* (2012 TCC 240), three children resided 55 percent of the time with the mother and 45 percent of the time with the father; the court found that the parents were shared-custody parents. In *Reynolds v. The Queen* (2015 TCC 109), two children resided 49 percent of the time with the mother and 33 percent of the time with the father (the remainder was school time); the court found that the mother had primary custody. In *C.P.B. v. The Queen* (2013 TCC 118), however, the court paid little attention to time allocation and considered other matters; the parents were found to be shared-custody parents.

In opposite-sex marriages, the statutory presumption is that the female parent primarily fulfills the responsibility for the care and upbringing of the child (see paragraph (f) of the definition of "eligible individual" in section 122.6). This presumption may be rebutted by the male parent with sufficient evidence (*Cabot v. The Queen*, 1998 CanLII 477 (TCC)). Thus, the CRA's practice is not to request documentation when only the female parent has filed form RC66, but to request documentation when only the male parent has filed the form.

This statutory presumption is not a barrier to parents making the shared-custody choice, provided that both parents submit applications for the CCB (since, by virtue of paragraph (d) of regulation 6301, the presumption then does not apply).

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Exempt Surplus and TIEAs: A Bad Deal?

An article published by the CBC in June 2016 criticizes Canada's 2007 decision to extend exempt surplus treatment to certain business earnings from countries with which Canada has entered into a tax information exchange agreement (TIEA). The CBC cites data on direct investment abroad into TIEA countries, and it states that "billions [of dollars] in potential revenue [has been] lost." The CBC questions whether Canada should continue to sign TIEAs, since "instead of halting the flow of Canadian money offshore, they've hastened it." In my view, this analysis is flawed.

Until 2007, the exempt surplus system—under which dividends paid out of the active business earnings of a foreign affiliate are received in Canada tax-free—was limited to earnings derived from countries with which Canada had a tax treaty. In 2007, this treatment was expanded to include countries with TIEAs. The carrot was accompanied by a stick: the "non-qualifying country" concept was added to the FAPI rules, causing the business profits of a controlled foreign affiliate earned in a non-treaty, non-TIEA country to be taxed on a current basis, before any dividend was paid. If non-treaty countries wanted to pursue Canadian investment, they now had very strong incentives to enter into TIEAs with Canada.

There is no public information about how well TIEAs curtail tax evasion. Assuming that the Department of Finance had some reason to believe that there would be a positive effect, it is difficult to find fault with its decision to encourage candidate countries to enter into TIEAs by using the exempt surplus rules. Unlike the United States, Canada does not have the hard or soft power to compel other countries to enter into TIEAs; presumably, it would have been more difficult to convince countries to sign TIEAs if we had not been able to offer some potential benefit to them.

As for the data showing rising direct investment in TIEA countries, my experience is that these countries are not the ultimate destination of the investment. Instead, Canadian corporations are using their foreign affiliates in TIEA jurisdictions as conduits for investment in other, higher-tax jurisdictions. The use of TIEA-jurisdiction foreign affiliates may be permitting Canadian MNEs to erode the tax base of the countries in which capital is ultimately invested, but that is a very different problem from the one that the CBC is attempting to demonstrate. Indeed, if a reduction in foreign and Canadian tax costs makes Canadian MNEs more competitive internationally, lower MNE tax costs are in our collective best interest: MNEs are in fact our most efficient job creators, and they disproportionately create high-paying jobs.

To the extent that the TIEA country is the ultimate destination of the investment, there will be a revenue loss from the reduction in the tax burden on dividends received by the Canadian parent. However, this loss is likely to be small because it is likely that dividends would not be paid back to Canada in the absence of exempt surplus treatment. This result has been observed in the United States, where domestic corporations typically realize a US tax liability when their CFCs pay dividends. US corporations have responded to this disincentive, but not in the way that the US treasury would have liked: CFCs still carry on business in low-tax jurisdictions and make use of tax havens—and they simply refrain from paying dividends to their domestic corporation shareholders.

If a villain must be identified, as the CBC apparently believes is necessary, is it the fundamental basis of the exempt surplus system as a territorial tax system? The premise of such a system is that when Canadian companies invest abroad, only the local taxes in that country should apply; no additional tax should be imposed when the dividends are brought back to Canada. This practice creates a level playing field with MNEs from other countries investing in that country, if all such corporations are subject only to the local taxes. However, if that country has a low rate of corporate tax, the secondary effect of such a system is to create an incentive for Canadian companies to invest in the low-rate country rather than in Canada (assuming that the pre-tax rate of return is the same).

A possible solution to this problem is to limit exempt surplus treatment to high-tax countries. However, Canadian companies would then be at a competitive disadvantage in the low-tax countries compared with companies from countries that continued to offer territorial treatment. Also, to the extent that Canadian parent companies declined to repatriate foreign income from those countries, Canada might not reap additional revenue.

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Move to the UK and Earn Tax-Free Investment Income

The norm for personal income tax systems around the world is that residents of a country pay tax on their world income, although some countries provide special rules for those from abroad. For people moving to the United Kingdom from other countries (and for certain other individuals with some non-UK connection), investment income earned around the world can be non-taxable unless it is brought back to the United Kingdom. The UK revenue authority has just published a helpful guide on this subject. Reform proposals may end individuals' ability to continue this special treatment indefinitely.

UK tax law distinguishes between income and capital gains, and each is taxed separately. Therefore, the following discussion distinguishes between "income" and "gains."

UK residents are normally taxed on the arising basis of taxation, which means that world income and gains are taxable in the United Kingdom. However, a person who is resident in the United Kingdom but not domiciled there (a "non-dom") may choose between the arising basis of taxation and the remittance basis of taxation. Generally, an individual's domicile is the jurisdiction of permanent residence of his or her father at the time of the individual's birth.

On the remittance basis, the individual will pay tax on (1) any income and gains that arise or accrue in the United Kingdom, and (2) any foreign income and gains that are remitted (that is, brought) to the United Kingdom. Thus, a person who chooses the remittance basis of taxation does not pay tax on income and gains that are not remitted to the United Kingdom. Investment income, for example, can be kept offshore. (Of course, non-UK taxes may apply.)

However, a long-term UK resident who chooses to claim (that is, be taxed on) the remittance basis could be liable to pay the remittance basis charge (RBC). The RBC is essentially a flat amount that one pays for the privilege of accessing this special tax regime. There are three levels of the RBC: £30,000 for individuals who have been UK-resident in at least 7 out of the preceding 9 UK tax years; £60,000 for individuals who have been UK-resident in at least 12 out of the preceding 14 UK tax years; and £90,000 for individuals who have been UK-resident in at least 17 out of the preceding 20 UK tax years. (At the time of writing, £1.00 is worth Cdn$1.73.)

The breakeven point at which claiming the remittance basis becomes economically beneficial varies with the tax rate and the number of years that the person has been a UK resident. For example, a person paying tax at the 45 percent rate who has lived in the United Kingdom for 17 or more of the preceding 20 taxation years will find the remittance basis worthwhile if it allows him or her to avoid paying tax on £200,000 or more of income (£200,000 × 45% = £90,000). The choice to be taxed on the remittance basis is made separately for each tax year.

A 2015 government consultation paper includes proposals eliminating the ability to use the remittance basis for individuals who have been resident in the United Kingdom for at least 15 of the past 20 tax years. Also, individuals domiciled in the United Kingdom at birth and who subsequently acquire a foreign domicile will not be able to return to the United Kingdom as non-doms; they will revert to having a UK domicile for tax purposes whenever they are resident in the United Kingdom. Although these changes were to take effect on April 6, 2017, they have not been included in Finance Bill 2016, which is currently before Parliament.

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Escaping Penalties After Admitting False Statements

When taxpayers reduce or eliminate their tax liability by using obviously baseless tax-protester arguments, the government generally chooses to assess on the basis of the gross negligence penalties of subsection 163(2), since proof of intent is required for tax evasion (but see *R v. Klundert*, 2004 CanLII 21268 (ONCA)). Normally, the most economical and advisable response is simply to pay the penalty; however, in a few situations a taxpayer's appeal has been successful at the TCC.

The specific legal arguments made for the purported tax savings are not typically at issue in such appeals, since the parties have already agreed that the arguments have no merit. In *Torres v. The Queen* (2013 TCC 380), for example, some of the taxpayers said that they were led to believe that a social insurance number was a separate entity that could incur expenses that would be deductible to an individual even if the individual did not previously have any business activities. The claimed losses far exceeded the taxpayers' income, resulting in significant tax refunds for the current year and for previous years after loss carrybacks were claimed.

Gross negligence penalties under subsection 163(2) may be imposed when a taxpayer knowingly, or in circumstances amounting to gross negligence, has made or has participated in, assented to, or acquiesced in the making of a false statement in a return. The penalties generally amount to 50 percent of the tax avoided. In these loss-claim cases, the penalties are imposed not only on the taxpayer's T1 return, but also on the T1 adjustment request for a non-capital loss carryover deduction, regardless of whether a refund is ever issued to the taxpayer (*Morton*, 2014 TCC 72).

Many of the cases have involved Fiscal Arbitrators, a tax-preparation firm operating in Ontario. Certain individuals associated with the firm have been convicted of fraud in the preparation of income tax returns (see, for example, *R v. Watts*, 2015 ONSC 7375). There are a total of 27 TCC decisions referring to this firm. In addition, according to the current appeals docket on the TCC website, there are 381 related Fiscal Arbitrators appeals (for example, 2013-742(IT)G and 2013-1340(IT)I). At least 3 active appeals are at the FCA (*Maynard*, A-95-16, appealing 2016 TCC 21; *Wynter*, A-156-16, appealing 2016 TCC 103; and *Grier*, A-135-16, TCC decision unreported).

A clear majority of the Fiscal Arbitrators appeals have been dismissed by the TCC and, in most cases, the concept of wilful blindness was applied to uphold the subsection 163(2) gross negligence penalties. In finding wilful blindness, the TCC has considered the education and experience of the taxpayer and has reviewed a number of warning signs that strongly indicated a need for inquiry by the taxpayer before he or she filed the return, including the magnitude of the advantage claimed and the blatant false statement made in the return (*Torres*). The TCC has also rejected the argument that the government has a duty to warn taxpayers about these scams and that a failure to warn precluded the imposition of penalties (*Torres*).

Only eight of the Fiscal Arbitrators appeals have been successful at the TCC, and just four of those decisions have provided written reasons. In two cases (*Anderson*, 2016 TCC 93, and *Morrison*, 2016 TCC 99), the court found that the tax preparer had inserted pages into the return after the taxpayer had signed. In another case (*Brathwaite*, 2016 TCC 29), the return had not been put into evidence by the Crown. In yet another case (*Sam*, 2016 TCC 98), the taxpayer's long-time tax preparer had died; the taxpayer had not based her choice of the new preparer on the promise of a refund but rather on a referral. The court found that her acts and omissions were attributable to human failure and carelessness, not to negligence.

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SCC Upholds Solicitor-Client Privilege

In *Chambre des notaires* (2016 SCC 20) and *Thompson* (2016 SCC 21), released on the same day, the SCC affirmed the importance of solicitor-client privilege as it applies to CRA written requests ("requirements") to provide client information and a lawyer's accounting records: both requirements were found to be unconstitutional. As a result, any lawyer who receives a CRA letter requesting such information should inform affected clients of the letter and their rights under this doctrine.

Chambre des notaires concerned Quebec notaries who received requirements in the course of an audit, asking for specific data about their clients that could be used for tax collection or audit purposes. The SCC, emphasizing the quasi-constitutional status of solicitor-client privilege, found that the Act's requirement scheme contained a number of defects, including the provision that the CRA was not obliged to inform the clients of the letters sent to their lawyers. Thus, the requirements scheme violated section 8 of the Charter as an unreasonable intrusion on an individual's reasonable expectation of privacy, and could not be saved by the minimal-impairment-of-rights exception in section 1. The SCC made a similar finding about the Act's exclusion of protection for a lawyer's accounting records in its definition of solicitor-client privilege, noting that the term "accounting record of a lawyer" is not defined by the Act. These records may reveal privileged names, descriptions of the engagement between the lawyer and the client, and aspects of litigation strategy.

The companion case, *Thompson*, involved a lawyer who received a requirement from the CRA for his accounting records, including receivables, for the purposes of collecting on the lawyer's personal taxes owing. The SCC stated that having a court determine whether solicitor-client privilege attached to certain documents was insufficient to safeguard clients' rights. In other words, because a lawyer is not the client's alter ego (roughly, a second self), the client should be notified when a court considers making an order to require disclosure. The client should be given an opportunity to assert privilege over the information being demanded by the CRA and should be allowed to make submissions on its own behalf.

In obiter, the SCC opined in *Chambre des notaires* that the defects of the requirement scheme could "easily be mitigated" to respect solicitor-client privilege; it referred to a settlement agreement reached between the Quebec attorney general and the Chambre regarding similar requirement provisions found in the Quebec Tax Administration Act. The settlement provided, among other things, that before issuing a formal demand to a notary or lawyer, Revenu Québec had to attempt to obtain the requested documents from the public record, the taxpayer, other parties to the document, financial institutions, and the accountant who prepared the document. Even if the lawyer had sole possession of the document, Revenu Québec had to first request permission from the taxpayer before sending a formal demand. In turn, the formal demand had to specify the type of information requested and a rationale explaining why solicitor-client privilege did not apply. It remains to be seen whether the CRA will adopt a similar policy.

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Transfer-Pricing Penalties Now at Issue

Despite being enacted in 1998, the transfer-pricing penalty provisions in subsection 247(3) have been at issue before the TCC exactly once (*Marzen Artistic Aluminum Ltd.*, 2014 TCC 194, aff'd. 2016 FCA 34)—and no penalty was ultimately levied. Despite that unthreatening record, more attention should be paid to the possibility of these penalties.

The transfer-pricing rules outlined in section 247 apply, in general terms, to any transaction or series of transactions between a taxpayer and a non-resident person with whom the taxpayer is not dealing at arm's length. A penalty may be imposed if a transfer-pricing adjustment under subsection 247(2) exceeds a minimum amount of the lesser of $5 million and 10 percent of the taxpayer's gross revenues for the taxation year. The penalty amount is 10 percent of the actual adjustment.

The penalty is more significant than it might first appear. Because the minimum amount is tied to gross revenues, taxpayers with little revenue have far less room for error in setting their transfer prices. Additionally, penalties may be imposed even when there is no taxable income for a particular taxation year or when there are no increases in taxes payable because of the availability of losses, discretionary deductions, or credits. In contrast, US transfer-pricing documentation penalties apply only in situations with actual increases in taxes payable (IRC section 6662(e) and Treas. reg. section 1.6662-6).

Taxpayers for which a transfer-pricing adjustment is sufficient to generate a penalty when they use the calculation above will escape the penalty if they have made "reasonable efforts" to achieve a proper transfer price, which include but are not limited to satisfying certain contemporaneous documentation requirements in subsection 247(4). The local auditor does not determine whether reasonable efforts have been made: the question is subject to an automatic referral to the CRA's national Transfer Pricing Review Committee (TPRC). Taxpayers can make one written submission to the TPRC, but they have no right to appear in person to argue the case. Data released under access-to-information legislation indicate that as of August 2015, the TPRC had considered 508 penalty referrals, levying penalties in 232 (almost half) of these instances.

In *Marzen*, the TCC concluded that the taxpayer was deemed not to have made reasonable efforts because it failed to fulfill the documentation requirements of subparagraphs 247(4)(a)(v) and (vi). Ultimately, penalties were not applied because the revised adjustment fell below the minimum amount. *Marzen* presented an opportunity to provide clarification on what constitutes reasonable efforts for the purposes of subsection 247(3); however, owing to the facts of the case, the TCC did not go into detail beyond making a factual determination.

As more appeals involving penalties make their way to the TCC, it appears inevitable that the issue of what constitutes reasonable efforts will be addressed in more detail. Two recent notices of appeal filed with the TCC (court files 2016-77(IT)G and 2014-4179(IT)G) involve penalties of $70 million and $200 million, respectively. Given the quantum involved in these appeals and the lack of judicial guidance in the area, it will be interesting to see how the TCC will interpret the CRA's administrative positions if these appeals are litigated.

Penalty matters are automatically referred to the TPRC once an adjustment crosses the penalty threshold; therefore, taxpayers of all sizes must be prepared to demonstrate that they have complied with subsection 247(4) and made reasonable efforts to determine and use arm's-length transfer prices. Taxpayers should be proactive in preparing proper documentation in order to help avoid the application of penalties, and perhaps should take additional steps to ensure that reasonable efforts have been made.

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Quebec Opens the Door to Patent Boxes

The Quebec government's March 2016 budget announced the first patent box tax proposal in Canada: the deduction for innovative manufacturing corporations (DIMC). The aim is to support the innovation efforts of Quebec manufacturing companies and encourage them to keep intellectual property developed in Quebec in the province by providing a low 4 percent tax rate on eligible income, bringing the combined federal-provincial tax rate down to 19 percent. (In a similar vein, Saskatchewan announced on May 17, 2016 that it would consult with industry on reducing the tax rate applicable to the commercialization of patents and intellectual property.) Draft legislation is not expected until the fall.

The concern about existing tax incentives for research and development (R & D) is that they subsidize expenditures but leave the resulting income taxable at regular rates. (One exception is British Columbia, which offers a reduction in the tax rate for certain international revenue derived from patents.) Such incentives may cause intellectual property to be subsequently sent to other countries (such as Belgium, Luxembourg, and the Netherlands) offering tax regimes that are friendlier to income derived from the use of intellectual property.

The DIMC will be a deduction in computing taxable income for any eligible innovating manufacturing company, which is defined as a company where (1) 50 percent or more of its activities consist of manufacturing and processing activities, and (2) its paid-up capital (including affiliates) is at least $15 million. The DIMC will be available for fiscal years beginning after December 31, 2016, and it will apply only to patented intellectual property for which a patent application was filed after March 17, 2016, and for which the patent is valid for the entire fiscal year.

The new deduction will be a specified percentage (66.1 percent in 2017) of the value of qualified patented parts incorporated into qualified property that the company sold, leased, or rented, up to a ceiling of 50 percent of the net income derived from such property. The value of the qualified patented part corresponds to the portion of the net income derived from the sale, lease, or rental of the property into which the patented part is incorporated and which can be reasonably attributed to the gains that the patented part contributed to the income.

Some aspects of the budget proposal may be hard to implement in practice—for example, the requirement for a separate accounting of revenues and expenses relating to qualified property. Also, the value of a patented part may be difficult to establish and may risk being contested by tax authorities, particularly in a situation where several patented parts are incorporated into the property being sold, leased, or rented.

Another issue is that, unlike traditional patent box regimes, the DIMC will grant the tax incentive only if the patented part is integrated into a property that is sold, leased, or rented, and if this patented part originates from R & D efforts. Moreover, a special tax will apply to companies that have benefited from the DIMC in cases where a patent is not granted or is invalidated, or where a reassessment is issued that cancels a refundable tax credit for R & D that is covered in the calculation of the DIMC. This provision exposes companies that apply for the deduction to a risk of clawbacks.

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Le Québec ouvre la porte aux *patent boxes*

Le gouvernement du Québec a annoncé lors de son budget de mars 2016 la première législation fiscale au Canada de type *patent box* appelée « déduction pour société innovante » (DSI), afin de soutenir l'effort des sociétés manufacturières québécoises en matière d'innovation, et de favoriser la rétention des propriétés intellectuelles mises au point au Québec. Celles-ci verront leur revenu admissible imposé à un taux de 4 pour cent, ce qui ramènera à 19 pour cent le taux d'impôt combiné fédéral-provincial payable. (Dans une mesure similaire, le gouvernement de la Saskatchewan a annoncé le 17 mai 2016 qu'il entreprendrait des consultations avec l'industrie sur la réduction du taux d'impôt applicable à la commercialisation de brevets et de propriété intellectuelle.) Une première version du texte législatif n'est pas prévue avant l'automne.

La principale préoccupation concernant les incitatifs fiscaux actuels relatifs à la recherche et au développement (R & D) est qu'ils subventionnent les dépenses menant au développement de propriété intellectuelle, mais ne réduisent pas la charge fiscale du revenu découlant d'une telle propriété. (Une exception est celle de la Colombie-Britannique, qui offre actuellement une réduction du taux d'impôt pour certains revenus internationaux provenant de brevets.) De tels incitatifs peuvent favoriser un transfert de propriété intellectuelle vers des pays offrant un régime fiscal plus avantageux pour les revenus découlant de leur utilisation (telles que la Belgique, le Luxembourg ou les Pays-Bas).

La DSI prendra la forme d'une déduction dans le calcul du revenu imposable, dont pourra se prévaloir toute société manufacturière innovante admissible, c'est-à-dire une société 1) dont 50 pour cent ou plus de ses activités consistent en des activités de fabrication et transformation, et 2) dont le capital versé (incluant les sociétés associées) est d'au moins 15 millions de dollars. La DSI sera disponible aux sociétés dont l'exercice débute après le 31 décembre 2016, et sera applicable aux éléments brevetés dont la demande de brevet a été déposée après le 17 mars 2016, et dont le brevet est valide durant toute la durée de l'exercice.

Cette nouvelle déduction sera égale à un pourcentage déterminé (66,1 pour cent en 2017) de la valeur des éléments brevetés admissibles incorporés dans des biens admissibles vendus ou loués, jusqu'à concurrence d'un plafond correspondant à 50 pour cent des revenus nets tirés de la vente ou de la location de biens admissibles. La valeur d'un élément breveté admissible correspondra à la partie du revenu net découlant de la vente ou de la location du bien dans lequel l'élément breveté est incorporé et qui est raisonnablement attribuable à la plus-value que l'élément breveté ajoute au revenu.

Certaines conditions d'application de la mesure, telle qu'annoncée, risquent d'être difficiles à mettre en place en pratique, tel que la tenue d'une comptabilité séparée pour les revenus et dépenses relatifs à un bien admissible. De plus, la valeur d'un élément breveté, surtout dans un contexte où plusieurs éléments brevetés sont incorporés dans le bien vendu ou loué, risque également d'être difficile à établir, en plus d'être susceptible d'être contestée par les autorités fiscales.

Une autre problématique est qu'à la différence d'une *patent box* traditionnelle, la DSI n'accordera un incitatif fiscal que dans la mesure où l'élément breveté est intégré à un bien loué ou vendu, et où cet élément breveté découle d'efforts en R & D. De plus, un impôt spécial sera prévu pour les sociétés ayant bénéficié de la DSI lorsqu'un brevet n'est pas délivré, est invalidé, ou lorsque de nouvelles cotisations sont émises et annulent un crédit d'impôt remboursable pour la R & D pris en compte dans la détermination de la DSI, ce qui expose les sociétés demandant la déduction à un risque de recouvrement fiscal.

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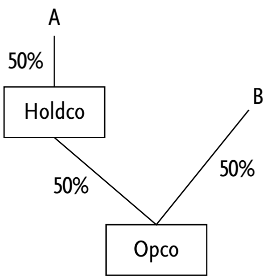
Multi-Level Farming Structures and the Capital Gains Exemption

Taxpayers selling a farming (or fishing) business will want to have the assets that are being sold qualify as "qualified farm or fishing property" (QFFP) so that the sale will be eligible for the capital gains exemption of $1 million in 2016 under subsections 110.6(2) and (2.2) (the farming exemption). Some multi-level structures will not be eligible for the farming exemption; the alternative is (1) to restructure to qualify and delay the sale by 24 months, or (2) to claim the more limited QSBC shares capital gains exemption under subsection 110.6(2.1) ($824,176 for the 2016 taxation year).

For shares to qualify as QFFP, the farming business must be carried on actively and continuously by the individual, his or her spouse, or his or her child; and the farming property must be used by any of those individuals, the corporation (whose shares are being disposed of), a related corporation, or a partnership in which the individual has an interest for 24 months. In addition, at the time of sale, all or substantially all of the fair market value of the properties must be attributable to the properties used in the farming business.

One problematic structure is that in which the farming business is carried on in Opco, which is owned 50 percent indirectly by taxpayer A and 50 percent directly by taxpayer B (an arm's-length party), as illustrated in figure 1.

Figure 1

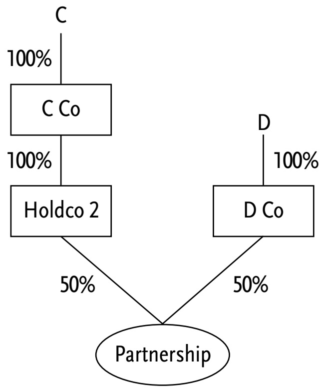


Taxpayer B will sell his or her shares in Opco, which will qualify as QFFP and thus will have access to the $1 million farming exemption. Taxpayer A will want to sell his or her shares in Holdco, but they will not qualify as QFFP because Holdco is not related to the corporation that is carrying on the farming business (Opco). Taxpayer A could claim the $824,176 exemption for QSBC shares. Alternatively, in order to claim the $1 million farming exemption, taxpayer A could first have taxpayer B sell his or her shares of Opco to Holdco for shares of Holdco (in order to make Opco and Holdco related). After this initial sale, however, taxpayer A would have to wait 24 months before selling his or her shares of Holdco; this restructure-and-wait strategy might not be acceptable to taxpayer B if it meant waiting 24 months before receiving the cash. Another issue is that Holdco might be considered to have had an acquisition of control, which would restrict the use of losses in the period prior to the sale of the business.

A second problematic ownership structure is that in which the farming business is carried on by a partnership owned 50 percent by Holdco 2 and 50 percent by D Co, as illustrated in figure 2. Holdco 2 is also owned by another holding company (C Co), which is owned by individual C. D Co is owned by individual D; individual C and individual D are arm's-length parties.

In order to qualify as QFFP, the D Co shares must be shares of the capital stock of a family farm or fishing corporation as defined in subsection 110.6(1). However, element (a)(i)(E) of the definition requires that individual D hold an interest in the partnership that is carrying on the farming business, which he or she does not. Nevertheless, the CRA has stated

Figure 2



that when a partnership carrying on a farming business has only one level of corporate partners, the corporate partner will be considered to carry on the business of the farm partnership (CRA document no. 2008-0299741I7, March 16, 2009). This statement qualifies the shares as QFFP under element (a)(i)(A) of the definition. Thus, by virtue of this administrative relief, the D Co shares are QFFP.

The C Co shares do not seem to be able to benefit from this relief because they are two levels above the partnership and therefore are not QFFP. Thus, again there is a choice between claiming the $824,176 exemption for QSBC shares and claiming the $1 million farming exemption provided to QFFP by restructuring and waiting 24 months before selling. In this case, the restructuring would require individual C to have at least a nominal direct interest in the partnership. This strategy might have an adverse effect on individual D, who, as a commercial matter, would probably also have to wait 24 months before being able to sell.

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FCA Reinstates Narrow View of De Facto Control

The potential expansion of de facto control in *McGillivray Restaurant Ltd.* (2014 TCC 357) (see "De Facto Control Broadened: More Than a Board of Directors Test," *Canadian Tax Focus*, February 2015) has been curtailed by *McGillivray Restaurant Ltd. v. The Queen* (2016 FCA 99). De facto control is confined to the "clear right and ability to effect a significant change in the board of directors or the powers of the board of directors or to influence in a very direct way the shareholders who would otherwise have the ability to elect the board of directors" (*Silicon Graphics*, 2002 FCA 260).

The appellant corporation operated a Keg restaurant in Winnipeg. It was controlled by Ruth Howard, who held 76 percent of its outstanding shares. Gordon Howard (Ruth's husband) owned the remaining shares and all of the shares of two other corporations that operated other Keg restaurants, provided management services, and leased premises to the appellant. The minister assessed on the basis that the corporations were associated and were therefore required to share the SBD. The minister did not rely on GAAR.

The separation of Mr. and Mrs. Howard's operating corporations, structured on the basis of professional advice, created no meaningful distinction between Mr. Howard's roles in each of them. Mr. Howard was heavily involved in the appellant's operations, serving as general manager of its restaurants. He negotiated contracts, made banking arrangements, and was the face of the Keg business in Winnipeg. Indeed, the franchise agreement permitting Mr. Howard's corporation and the appellant to operate Keg restaurants was partly conditioned on an assurance that he would manage and operate the business.

The trial judge found that Mr. Howard exercised de facto control of the appellant and it was therefore associated with Mr. Howard's other corporations. In so finding, Boyle J said that de facto control was more than an ability to elect the board of directors: he referred to cases that considered broader "manners of influence" over the "affairs and fortunes of the corporation" in question.

The FCA did not accept this line of reasoning, considering the question of de facto control thoroughly settled by *Silicon Graphics* and reinforced in *Transport Couture* (2004 FCA 23) and *Lyrtech* (2014 FCA 267). De facto control is "limited to the breadth of factors that can be considered in determining whether a person or group of persons has effective control, by means of an ability to elect the board of directors, of a corporation." When other cases contemplated a broader test, their reasons for judgment ultimately rested on those principles. Furthermore, the FCA affirmed that it would continue to follow its own previous decisions unless manifestly wrong, and any case that did not follow *Silicon Graphics* ought not to be followed. For greater certainty, the court explicitly rejected the proposition that de facto control had any basis in mere operational control.

Nonetheless, the taxpayer's appeal was dismissed. The trial judge had found that for business purposes—including the comfort of the franchisor under the franchise agreement—Mr. and Mrs. Howard had entered into an oral agreement that required Mrs. Howard to vote her shares to ensure that Mr. Howard remained the sole director of the appellant. The FCA found no palpable and overriding error that merited interfering with the TCC's factual finding. Consequently, there was an agreement under which the composition of the board of directors was under Mr. Howard's control. This control fell squarely within the type of de facto control contemplated in *Silicon Graphics*.

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Supreme Court Docket Update

Judgment Rendered

- *Canada (National Revenue) v. Thompson* (2016 SCC 21). The judgment was rendered on June 3, 2016. The appeal was allowed in favour of Duncan Thompson solely to set aside the FCA's order (2013 FCA 197). This case pertains to the issue of whether a lawyer subject to enforcement proceedings can claim solicitor-client privilege over his accounts receivable. In light of the SCC's conclusion in Canada (*Attorney General) v. Chambre des notaires du Québec* (2016 SCC 20), the request made by Thompson is now foreclosed. A webcast is available here. See also Sze Yee Ling and Nathan Wright, "SCC Upholds Solicitor-Client Privilege," elsewhere in this issue.
- *Canada (Attorney General) v. Chambre des notaires du Québec* (2016 SCC 20). The judgment was rendered on June 3, 2016. The appeal was dismissed with costs against the attorney general. Subsection 231.2(1) and section 231.7, together with the exception set out in the definition of "solicitor-client privilege" in subsection 232(1), were found unconstitutional vis-à-vis notaries and lawyers in Quebec on the basis that the provisions are contrary to the Canadian Charter of Rights and Freedoms. A webcast is available here. See also Sze Yee Ling and Nathan Wright, "SCC Upholds Solicitor-Client Privilege," elsewhere in this issue.

Awaiting Judgment

- *Jean Coutu Group (PJC) Inc. v. Attorney General of Canada* (from 2015 QCCA 838). The hearing was held on May 18, 2016. This case pertains to a motion for rectification and to what extent a taxpayer can retroactively revisit documentation giving effect to a series of transactions when unforeseen tax consequences have resulted following the SCC's decision in *Quebec (Agence du revenu) v. Services Environnementaux AES inc.* (2013 SCC 65). A short summary of the case is available here, and a webcast is also available.
- *Attorney General of Canada v. Fairmont Hotels Inc., et al.* (from 2015 ONCA 441). The hearing was held on May 18, 2016. This case pertains to a motion for rectification granted in favour of the taxpayer based on the test in *Attorney General of Canada v. Juliar* (2000 CanLII 16883

(ONCA)) and the taxpayer's continued tax intention. The Crown argued that the *Juliar* test was misapplied and that to allow rectification solely on the basis of the taxpayer's tax intention would be to sanction impermissible retroactive tax planning. A short summary of the case is available here, and a webcast is also available.

Leave Granted

- *Deloitte & Touche v. Livent Inc.* (from 2016 ONCA 11). Leave was granted on June 9, 2016. The date of the hearing is February 15, 2017. This case pertains to the professional liability of auditors and their duty of care owed to corporate clients. A short summary of the case is available here.

Leave Sought by the Department of Justice

None.

Leave Sought by the Taxpayer

- *1455257 Ontario Inc. v. Her Majesty The Queen* (from 2016 FCA 100). Leave was sought on May 27, 2016. This case pertains to whether a dissolved corporation has the capacity to initiate an appeal to the TCC from a reassessment issued against it.
- *Jacques Pellan v. Agence du revenu du Québec* (from 2016 QCCA 263). Leave was sought on April 8, 2016. This case pertains to the interpretation of section 8(b) of the Taxation Act (CQLR, c. I-3) with respect to the scope of the phrase "leaving Canada."
- *Jaamiah Al Uloom Al Islamiyyah Ontario v. Minister of National Revenue (Canada Revenue Agency)* (from 2016 FCA 49). Leave was sought on April 7, 2016. This case pertains to the status of a charity whose registration the minister of national revenue has revoked. A short summary of the case is available here.
- *Jean-Yves Archambault v. Agence du revenu du Québec, et al.* (from 2016 QCCA 76). Leave was sought on March 23, 2016. This case pertains to Revenu Québec's responsibility to a company and its main shareholder resulting from a tax audit.
- *Mac's Convenience Store Inc. v. Attorney General of Canada, et al.* (from 2015 QCCA 837). Leave was sought on December 18, 2015. This case pertains to a motion for rectification sought by the taxpayer that was denied on the basis that a taxpayer is obliged to pay tax arising from the transaction that it effected—not from the transaction that it would have preferred to have effected given the benefit of hindsight regarding unintended tax consequences. A short summary of the case is available here.

Leave Dismissed

- *Dan Mason v. Her Majesty The Queen* (from 2016 FCA 15). Leave was dismissed on June 30, 2016. This case pertains to the determination of the income of a taxpayer, as to whether the income is earned personally by the taxpayer or earned by corporations and trusts. A short summary of the case is available here.
- *James T. Grenon v. Her Majesty The Queen* (from 2016 FCA 4). Leave was dismissed on June 30, 2016. This case pertains to the deductibility of legal fees and costs incurred in contested proceedings to determine the amount of child support payments. A short summary of the case is available here.
- *Virginia Forsythe v. Her Majesty The Queen* (from 2015 FCA 258). Leave was dismissed on April 21, 2016. This case pertains to whether the taxpayer's employment income is property "situated on a reserve" so that it is exempt from taxation by operation of section 87(1)(b) of the Indian Act (RSC 1985, c. I-5). A short summary of the case is available here.

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Dossiers portés en appel devant la Cour suprême — Mise à jour

Jugement rendu

- *Canada (Revenu national) c. Thompson* (2016 CSC 21). Ce jugement a été rendu le 3 juin 2016. L'appel a été accueilli avec dépens en faveur de Duncan Thompson, mais seulement pour infirmer l'ordonnance de la CAF (2013 CAF 197). Cet arrêt se rapporte à la question de savoir si un avocat qui est visé par des procédures d'exécution peut invoquer le secret professionnel à l'égard de ses comptes à recevoir. Étant donné la conclusion de la CSC dans *Canada (Procureur général) c. Chambre des notaires du Québec* (2016 CSC 20), la demande de Thompson est désormais sans objet. Une diffusion Web de l'audience est disponible ici. Voir aussi le texte de Sze Yee Ling et Nathan Wright, « SCC Upholds Solicitor-Client Privilege », à ce sujet.
- *Canada (Procureur général) c. Chambre des notaires du Québec* (2016 CSC 20). Ce jugement a été rendu le 3 juin 2016. L'appel a été rejeté avec dépens contre le procureur général. Le paragraphe 231.2(1) et l'article 231.7 ainsi que la définition de « privilège des communications entre avocats et clients » au paragraphe 232(1) de la LIR ont été jugés inconstitutionnels, en ce qui concerne les avocats et notaires au Québec, puisqu'ils sont contraires à la Charte canadienne des droits et libertés. Une diffusion Web de l'audience est disponible ici. Voir aussi le texte de Sze Yee Ling et Nathan Wright, « SCC Upholds Solicitor-Client Privilege », à ce sujet.

En attente de jugement

- *Groupe Jean Coutu (PJC) inc. c. Procureur général du Canada, et al.* (de 2015 QCCA 838). L'appel a été entendu le 18 mai 2016 et le jugement est en délibéré. Ce dossier porte sur une demande de rectification et sur les balises appropriées à appliquer suite aux décisions de la Cour suprême du Canada en la matière dans *Québec (Agence du revenu) c. Services Environnementaux AES inc.* (2013 CSC 65). Un court sommaire du dossier est disponible ici et une diffusion Web de l'audience aussi disponible.
- *Procureur général du Canada c. Hôtels Fairmont Inc., et al.* (de 2015 ONCA 441). L'appel a été entendu le 18 mai 2016 et le jugement est en délibéré. Ce dossier porte sur une demande de rectification accueillie en faveur du contribuable compte tenu du test contenu dans la décision *Attorney General of Canada v. Juliar* (2000 CanLII 16883 (ONCA)) et de l'intention fiscale continue du contribuable. La Couronne a argumenté que le test de *Juliar* fut mal appliqué et que se baser uniquement sur l'intention fiscale du contribuable constitue de la planification fiscale rétroactive. Un court sommaire du dossier est disponible ici et une diffusion Web de l'audience aussi disponible.

Demande d'autorisation accueillie

- *Deloitte & Touche c. Livent Inc.* (de 2016 ONCA 11). Demande d'autorisation accueillie le 9 juin 2016. La date de l'audition a été fixée au 15 février 2017. Ce dossier porte sur la responsabilité professionnelle des vérificateurs et sur leur obligation de diligence envers l'entreprise pour qui ils agissent. Un court sommaire du dossier est disponible ici.

Demande d'autorisation déposée par le ministère de la Justice

Aucune.

Demande d'autorisation déposée par le contribuable

- *1455257 Ontario Inc. c. Sa Majesté la Reine* (de 2016 CAF 100). Demande d'autorisation déposée le 27 mai 2016. Ce dossier porte sur la question de savoir si une société dissoute peut intenter un appel devant la Cour canadienne de l'impôt à l'encontre d'une cotisation établie contre elle.
- *Jacques Pellan c. Agence du revenu du Québec* (de 2016 QCCA 263). Demande d'autorisation déposée le 8 avril 2016. Ce dossier porte sur l'interprétation du paragraphe 8b) de la Loi sur les impôts (RLRQ c. I-3) quant à l'expression « départ du Canada ».
- *Jaamiah Al Uloom Al Islamiyyah Ontario v. Minister of National Revenue (Canada Revenue Agency)* (de 2016 FCA 49). Demande d'autorisation déposée le 7 avril 2016. Ce dossier porte sur le statut d'un organisme de bienfaisance que le ministre du revenu national a révoqué. Un court sommaire du dossier est disponible ici.
- *Jean-Yves Archambault c. Agence du revenu du Québec, et al.* (de 2016 QCCA 76). Demande d'autorisation déposée le 23 mars 2016. Ce dossier porte sur la responsabilité de l'Agence du revenu du Québec envers une entreprise et son principal actionnaire découlant d'une vérification fiscale.
- *Dépanneurs Mac's c. Procureur général du Canada, et al.* (de 2015 QCCA 837). Demande d'autorisation déposée le 18 décembre 2015. Ce dossier porte sur une requête pour jugement déclaratoire (rectification) déposée par le contribuable et refusée par les instances inférieures au motif qu'un contribuable doit payer les impôts qui découlent de l'opération effectuée — et non pas celle, qu'avec du recul, il aurait préféré avoir effectuée compte tenu des conséquences fiscales inattendues de ladite opération. Un court sommaire du dossier est disponible ici.

Demande d'autorisation rejetée

- *Dan Mason c. Sa Majesté la Reine* (de 2016 FCA 15). Demande d'autorisation rejetée le 30 juin 2016. Ce dossier porte sur la détermination du revenu d'un contribuable, afin de savoir si son revenu est gagné par lui personnellement ou par des sociétés par actions et des fiducies. Un court sommaire du dossier est disponible ici.
- *James T. Grenon c. Sa Majesté la Reine* (de 2016 FCA 4). Demande d'autorisation rejetée le 30 juin 2016. Ce dossier porte sur la déductibilité des frais légaux et judiciaires encourus dans des procédures afin de déterminer le montant à payer de pension alimentaire pour enfants. Un court sommaire du dossier est disponible ici.
- *Virginia Forsythe c. Sa Majesté la Reine* (de 2015 CAF 258). Demande d'autorisation rejetée le 21 avril 2016. Ce dossier porte sur la question de savoir si le revenu d'emploi de la contribuable constituait des biens meubles « situés sur une réserve » au sens de l'alinéa 87(1)b) de la Loi sur les Indiens (LRC 1985, c. I-5) et étaient par conséquent exonérés d'impôt au titre de la Loi de l'impôt sur le revenu. Un court sommaire du dossier est disponible ici.

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