

Date: 20090429

Docket: T-1899-07

Citation: 2009 FC 434

Ottawa, Ontario, April 29, 2009

PRESENT: The Honourable Madam Justice Simpson

BETWEEN:

**ROBERT M.O. MORRIS and
NEVILLE LEROY SMITH
TRUSTEES OF THE RCI TRUST**

Applicants

and

MINISTER OF NATIONAL REVENUE

Respondent

REASONS FOR JUDGMENT AND JUDGMENT

[1] The Applicants are the Trustees of the RCI Trust. They say that the tax treaty between Canada and Barbados exempts the trust from paying capital gains tax in Canada on the disposition of the shares of RCI Environment Inc. because the RCI Trust is resident in Barbados.

BACKGROUND

[2] The *Agreement between Canada and Barbados for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion With Respect to Taxes on Income and on Capital* was enacted in Canada by the *Canada-Barbados Income Tax Agreement Act*, 1980 S.C. 1980-81-82-83, c. 44, Schedule IX (the Treaty).

[3] The Treaty applies to “persons” who are residents of one or both of the contracting states and in Article III, paragraph 1(c), the term “person” is defined to include a trust. The term resident is defined in Article IV, paragraph 1, in the following terms:

1. For the purposes of this Agreement, the term “resident of a Contracting State” means any person who, under the law of that State, is liable to taxation therein by reason of his domicile, residence, place of management or any other criterion of a similar nature. The terms “resident of Canada” and “resident of Barbados” shall be construed accordingly.

1. Au sens du présent Accord, l’expression « résident d’un État contractant » désigne toute personne qui, en vertu de la législation dudit État, est assujettie à l’impôt dans cet État en raison de son domicile, de sa résidence, de son siège de direction ou de tout autre critère de nature analogue, et les expressions « résident du Canada » et « résident de la Barbade » ont le sens correspondant.

[4] Paragraph 3 of Article IV also deals with residency. It states:

3. Where by reason of the provisions of paragraph 1, a person other than an individual is a resident of both Contracting States, then the competent authorities of the Contracting States shall by mutual agreement endeavour to settle the question and to determine the mode of application of this Agreement to such person.

3. Lorsque, selon la disposition du paragraphe 1, une personne autre qu’une personne physique est considérée comme résident de chacun des États contractants, les autorités compétentes des États contractants s’efforceront d’un commun accord de trancher la question et de déterminer les modalités d’application du présent Accord à ladite personne.

[5] The Applicants say that the RCI Trust is only resident in Barbados and that Article IV, paragraph 3, has no application in this case. They rely on the following facts:

1. The Trust was settled under the laws of Barbados;
2. The trustees are citizens of and are residents of Barbados;
3. The Trust's business office is in Barbados and it has one employee;
4. The Trust files tax returns in Barbados;
5. The Trust's accountants are in Barbados.

[6] The disposition of taxable Canadian property which generated the gains at issue in this case followed rather convoluted trust and corporate transactions which appear to have been undertaken by a Quebec businessman by the name of Lucien Rémillard for the purpose of estate and related tax planning.

[7] The plan appears to have been initiated on February 28, 1995 when North West Investments settled a trust in the Cayman Islands called the North West Trust (the Cayman Trust). The party behind North West Investments is unknown but the beneficiaries of the Cayman Trust are the children and remoter issue of Lucien Rémillard, together with their spouses, widows and widowers and their remoter issue. Lucien Rémillard's children are Maxime and Julien Rémillard. They are both residents of Canada (the Rémillard Children).

[8] Two years later, in 1997, two companies were formed under the *Canada Business Corporations Act*, R.S., 1985, c. C-44, s. 1; 1994, c. 24, s. 1(F) (CBCA). They were RCI

Environment Inc. and Centre de Transbordement et de Valorisation Nord-Sud Inc. These waste disposal management companies (the Waste Companies) were wholly owned by a Montreal lawyer named Paul Biron in trust for a trust to be settled under the law of Barbados. He held one hundred shares in each company and each share was valued at \$1 for a total of \$200. Lucien Rémillard was the sole director of each company.

[9] On July 9, 2002, North West Investments settled a second trust – this time in Barbados. It is called the RCI Trust (the Barbados Trust). Its beneficiary is the Cayman Trust.

[10] On the same day (July 9, 2002), Maître Biron conveyed the shares of the Waste Companies to the Barbados Trust for \$200.

[11] On January 31, 2006, the Waste Companies were amalgamated under the CBCA (the Amalgamation) and continued as RCI Environment Inc. (RCI). On Amalgamation, the two hundred outstanding shares of the Waste Companies were cancelled and two hundred shares of RCI were issued and valued at \$200.

[12] On May 5, 2006, the Barbados Trust agreed to sell its two hundred shares of RCI for \$145,000,000. The effective date of the sale was May 31, 2006 and the purchase price is to be paid by December 31, 2011. The purchaser is a company called Les Investissements Historia Inc. (Historia). It is incorporated under the CBCA and one of its shareholders and its sole officer and

director is Lucien Rémillard. This share purchase agreement of May 31, 2006 will be referred to as the “Transaction”.

[13] To summarize, the facts in evidence disclose that Lucien Rémillard was the sole director of the Waste Companies and is the sole director of RCI and Historia.

[14] The Information Circular which applied to section 116 of the *Income Tax Act*, S.C. 1985, c. 1 (5th Supp.) (the Act), at the time of the Transaction bore the number 72-17R5 and was entitled “Procedures concerning the disposition of taxable Canadian property by non-residents of Canada – Section 116” (the Circular).

[15] Paragraph 1 of the Circular provided the following general information:

1. Under Section 116, non-resident vendors (from now on referred to as vendors) who dispose of certain taxable Canadian property (see item 2 below) have to notify the Canada Revenue Agency (CRA) about the disposition either before they dispose of the property or within ten days after the disposition. When the CRA has received either an amount to cover the tax on any gain the vendor may realize upon the disposition of property, or appropriate security for the tax, the CRA will issue a certificate of compliance to the vendor. A copy of the certificate is also sent to the purchaser. If the purchaser does not receive such certificate, the purchaser is required to remit a specified amount to the Receiver General for Canada and is entitled to deduct the amount from the purchase price. Any payments or security provided by the vendor and/or purchaser will be credited to the vendor’s account. A final settlement of tax will be made when the vendor’s income tax return for the year is assessed.

[16] Paragraph 7 of the Circular provided detail about the required documentation and showed that payment or security must be received before a certificate would issue.

7. A vendor should use the appropriate authorized form to notify the CRA about a section 116 disposition. The forms outline the procedures to follow for reporting the transaction, calculating the gain or loss, income, recapture or terminal loss, and making the required payment on account of tax. The vendor must also provide all required information and documentation as described in the “Supporting Document List” attached to the authorized form. This information is essential to the issuance of the certificate in a timely manner. The notification form must be signed by the vendor. [...]

[17] However, paragraph 25 of the Circular dealt with tax treaty exemptions in slightly different terms in that it appears that a request for an exemption did not require payment of the gain or security therefor.

25. Section 116 does not provide for treaty exempt status. However, the CRA allows vendors to claim an exemption under a specific tax treaty at the time they file the notification of disposition. Vendors must state the applicable Article (paragraph) of the particular treaty that Canada has with their country of residence. To expedite the processing of the exemption, the necessary documentation to support the claim should be submitted along with the request. The documentation must be based on the particular tax treaty under which the exemption is claimed, and would include items such as proof of residency, or proof that the gain has been or will be reported in the vendor’s country of residence. Tax officials in some countries may supply the necessary certification required to claim the exemption. Refer to the Supporting Document List in the instructions to forms T2062 and T2062A for a complete list of the required documentation. [my emphasis]

[18] Paragraph 28 of the Circular also dealt with tax treaty exemptions and it said:

28. The granting of exemptions at the time of notification of disposition is discretionary. The vendor must provide documents to support the proceeds of disposition and the adjusted cost base of the property. The certificate of compliance will indicate that the disposition is treaty exempt. However, the certificate of compliance will be issued only when all other outstanding debts of the vendor with the CRA has been satisfied. [my emphasis]

[19] It therefore appears from the Circular that the certificate of compliance (the Certificate) was intended to be the vehicle which notified vendors that an exemption was granted.

[20] The Circular also made it clear that, when a treaty exemption was sought, the proceeds of disposition and adjusted cost base of the property were to be established.

[21] Paragraphs 39 and 40 of the Circular describe the issuance of the Certificate:

39. The CRA will issue the certificate of compliance at the earliest possible date once the necessary information and supporting documentation have been received and validated, and acceptable payment or security has been received.

40. A copy of the certificate of compliance will be issued to both the vendor and the purchaser. The certificate protects the purchaser from any further tax liability in respect of the particular notice filed for that particular disposition. The vendor's final tax liability in respect of the particular notice will be determined when the vendor files a tax return, as is required under the Act, for the year the disposition took place.

THE SECTION 116 REQUEST

[22] By letter dated May 4, 2006 from solicitors in Markham, Ontario (the Letter), the Barbados Trust advised Revenue Canada of the Transaction and enclosed Form T-2062 which constituted a request by the Barbados Trust for a Certificate for the Transaction under section 116 of the Act.

[23] The Letter did not clearly seek an exemption from the capital gains tax based on the Treaty. However, it mentioned that the vendor was the Barbados Trust and documents were included which showed that the Barbados Trust was claiming an exemption under a tax convention.

[24] As well, the form itself showed that although the gain was \$145,000,000 less \$200, the taxable capital gain was \$0. No payment or security was included with the Letter and neither has since been provided. If tax had been reported as payable, the amount would have been 25% of \$144,999,800 or \$36,249,950.

THE APPLICANTS' POSITION

[25] The Applicants' initial submission is that section 116 does not apply to the shares of RCI. They say the shares are treaty exempt property because they are being sold by the Barbados Trust which is resident in Barbados. The Applicants, in the alternative, say that the Barbados Trust has fulfilled all the requirements of section 116 of the Act and is forthwith entitled to a Certificate showing exempt status under the Treaty. In particular, the Applicants deny that the Respondent has any discretion when a treaty exemption is sought and say that the statement to that effect in the Circular is wrong.

THE RESPONDENT'S POSITION

[26] The Respondent says that the issuance of a Certificate confirming a treaty exemption is a matter of ministerial discretion and that the onus is on the Barbados Trust to satisfy the Minister of National Revenue that the Treaty applies to the Transaction.

[27] The Respondent also says that this may be a case of dual residency and that Article IV, paragraph 3, of the Treaty may apply. Even though the Respondent acknowledges that the Barbados Trust is a resident of Barbados, the Respondent suggests that the Transaction may not be at arms length. Section 94 of the Act may deem the Barbados Trust to be a resident of Canada because its beneficiaries once removed, namely the Rémillard Children, are Canadian residents.

[28] The Respondent is also concerned that it has no evidence to support the sale price of \$145,000,000 as the fair market value of the RCI shares at the time of the Transaction. Although the Applicants suggested that the Respondent contact Capital Environment Resources Inc. to confirm that it had been negotiating with the Barbados Trust to purchase the RCI shares for a comparable sum, there is no evidence about whether that contact was made. Finally, the Respondent is concerned about: the \$200 valuation of the estimated adjusted cost base for the RCI shares in the Applicants' section 116 Certificate application; the identity of Maître Biron's client; and the fact that no tax was paid on the disposition in 2000 when Maître Biron conveyed the shares of the Waste Companies to the Barbados Trust for \$200.

[29] The Respondent has contacted Maître Biron but he has refused to volunteer any information about his retainer or his client.

[30] The Respondent says that because it has not received all the information it requires to deal with these issues it is entitled to take the position that it is not satisfied that the Treaty applies and that it can, in its discretion, refuse to issue the Certificate until it is so satisfied.

[31] The Applicants reply that they were not appointed as trustees until 2002 and have no information about Maître Biron's client or the value of the shares of the Waste Companies when they were incorporated in 1997.

[32] The Applicants also note that by September 12, 2007, they had sent the Respondent all the relevant documentation required by the Circular's supporting document list. They say that the Respondent is already auditing the Barbados Trust and, according to a letter of June 11, 2007 from Mr. Marc Lemyre, the Respondent also now appears to be auditing the Transaction. The Applicants note that during the audits, the Respondent will be entitled to secure the outstanding information from knowledgeable parties.

DISCUSSION

[33] Section 116 of the Act predates the Treaty. Section 94 of the Act, an anti-avoidance provision dealing with deemed residence, also predates the Treaty.

[34] If those sections of the Act had been intended to apply notwithstanding the Treaty, I would have expected the Treaty to deal expressly with the interaction between its provisions and the requirement for a Certificate and the possibility of deemed residence.

[35] In the absence of such provisions, I have concluded that the Treaty is paramount and that decisions about residence and treaty exempt property are to be based solely on the language of the Treaty.

[36] Against this background the issues are:

1. Where is the Barbados Trust resident?
2. What is the taxing authority?
3. What is the import of section 116 and the Circular?
4. What, if any, is an appropriate remedy for the Applicants?

1. Residence

[37] The Respondent acknowledges that the Barbados Trust is *prima facie* a resident of Barbados. Based on the facts described above, it meets the physical criteria associated with actual residence of the kind described in Article IV, paragraph 1, of the Treaty which speaks of “domicile”, “place of management” and “criterion of a similar nature”. In my view, similar criteria

would include other aspects of actual physical presence and not more esoteric concepts such as deemed residence.

[38] The question is whether Article 3 of the Treaty allows me to conclude that the Barbados Trust is also a resident of Canada. In my view, such a conclusion is not open to me on the facts of this case because Article IV, paragraph 3, limits the assessment to the provisions of paragraph 1 of the Treaty. This means that a finding of dual residence must be based on actual physical factors and there are no such factors linking the Barbados Trust to Canada. Accordingly, the Barbados Trust is only resident in Barbados.

2. The Taxing Authority

[39] Article XIV of the Treaty deals with gains from the alienation of property. Paragraph 4 provides that:

4. Gains from the alienation of any property, other than those mentioned in paragraphs 1, 2 and 3 may be taxed only in the Contracting State of which the alienator is a resident

4. Les gains provenant de l'aliénation de tous biens autres que ceux qui sont mentionnés aux paragraphes 1, 2 et 3 ne sont imposables que dans l'État contractant dont le cédant est un résident.

[40] The Respondent made no submissions to the effect that paragraphs 1, 2 or 3 applied. Accordingly, Barbados is the taxing authority. It did not tax capital gains at the time of the Transaction.

3. Section 116 and the Circular

[41] In my view, when no tax is owing because of a tax treaty, the Respondent should not use section 116 of the Act to accomplish enforcement and collection objectives, however worthy. It appears that, using the Circular, the Respondent has purported to extend its powers under section 116 beyond those contemplated by the section. Section 116 of the Act makes no reference to exemptions under tax treaties.

[42] I am supported in this view by the fact that pending amendments to the Act introduced in 2007 make it clear that section 116 does not apply to treaty exempt property.

4. Remedy

[43] In my view, the Applicants are entitled to a binding ruling from the Respondent about whether the RCI shares are treaty exempt property, accepting that the Barbados Trust is a resident only of Barbados.

JUDGMENT

THIS COURT ORDERS AND ADJUDGES that on or before June 30, 2009, the Respondent is to provide the Applicants with a written decision in accordance with these reasons, indicating whether or not the RCI shares are treaty exempt property under the Treaty.

“Sandra J. Simpson”

Judge

FEDERAL COURT
SOLICITORS OF RECORD

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