Federal Court of Appeal

Cour d'appel fédérale

Date: 20200212

Docket: A-315-18

Citation: 2020 FCA 43

CORAM: **WEBB J.A.**
NEAR J.A.
LOCKE J.A.

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

and

ALTA ENERGY LUXEMBOURG S.A.R.L.

Respondent

Heard at Toronto, Ontario, on November 12, 2019.

Judgment delivered at Ottawa, Ontario, on February 12, 2020.

REASONS FOR JUDGMENT BY: WEBB J.A.

CONCURRED IN BY: NEAR J.A.
LOCKE J.A.

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REASONS FOR JUDGMENT

WEBB J.A.

[1] This is an appeal from a Judgment of the Tax Court of Canada dated August 22, 2018 (2018 TCC 152) that allowed the appeal of Alta Energy Luxembourg S.A.R.L. (Alta Luxembourg) from an assessment made under the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) (the Act), for its 2013 taxation year. Alta Luxembourg claimed that the large taxable capital gain that it realized as a result of the disposition of the shares of Alta Energy Partners Canada Ltd. (Alta Canada) was not taxable in Canada. The exemption from tax was based on the provisions

of the *Convention between the Government of Canada and the Government of the Grand Duchy of Luxembourg for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and on Capital* (the Luxembourg Convention). The Minister of National Revenue (Minister) did not agree that the provisions of the Luxembourg Convention applied. In the alternative, the Minister invoked the provisions of the general anti-avoidance rule (the GAAR) to tax that taxable capital gain in Canada. The Tax Court found that the provisions of the Luxembourg Convention did apply and that the GAAR did not apply. Therefore, the appeal of Alta Luxembourg was allowed.

[2] For the reasons that follow, I would dismiss this appeal.

I. Background

[3] The parties filed an extensive Statement of Agreed Facts with the Tax Court. For the purposes of this appeal, it is not necessary to recite all of the facts upon which there was an agreement. It is only necessary to highlight a few of the facts.

[4] On June 13, 2011, Alta Canada was incorporated under the laws of Alberta. This company was a wholly owned subsidiary of Alta Energy Partners, LLC (a Delaware limited liability company). In turn, the shares of this company were owned by two groups – one with the expertise for exploring for oil and natural gas, and the other with the capital that would be needed to conduct such exploration work.

[5] The Tax Court Judge found that Alta Canada carried on an unconventional shale oil business in the Duvernay shale oil formation situated in Northern Alberta. Alta Canada acquired various petroleum and natural gas licenses during the period from 2011 to 2013. In the Statement of Agreed Facts, it was noted that, as of March 28, 2013, Alta Canada's net acreage position in the Kaybob Duvernay was 67,891 acres.

[6] During 2012 and 2013, Alta Canada drilled four vertical wells and two horizontal wells. It appears that five of these six wells were drilled after Alta Luxembourg was formed and had acquired the shares of Alta Canada. Alta Canada was also a non-operator in two additional wells.

[7] At some point in 2011, the persons who indirectly owned the shares of Alta Canada were informed that the structure that had been adopted was not an ideal structure from a tax perspective because the exploration work was being done on properties in Canada. By late 2011, it was expected that the value of Alta Canada could increase substantially in the next few years.

[8] A restructuring was undertaken in 2012. As part of the restructuring, Alta Luxembourg was formed under the laws of Luxembourg and the shares of Alta Canada were transferred to it. The parties recognized that this transfer of shares was a taxable transaction. However, the Canada Revenue Agency agreed that the fair market value of the shares of Alta Canada at that time was equal to the adjusted cost base of these shares. Therefore, no capital gain was realized on the transfer of the shares of Alta Canada to Alta Luxembourg.

[9] Following the restructuring, all of the shares of Alta Luxembourg were held by Alta Energy Canada Partnership. This partnership was formed under the laws of Alberta. The partners were the shareholders of Alta Energy Partners, LLC. In effect, the result of the restructuring was to replace Alta Energy Partners, LLC with Alta Luxembourg and Alta Energy Canada Partnership.

[10] In 2013, the shares of Alta Canada were sold for approximately $680 million. The resulting capital gain was in excess of $380 million.

II. Relevant Provisions of the Act

[11] Subsection 2(3) of the Act provides that a non-resident, who has disposed of any taxable Canadian property, will be required to pay tax under the Act on that person's taxable income as determined in accordance with Division D of the Act.

[12] Division D includes section 115. Paragraph 115(1)(b), in particular, provides that:

115 (1) For the purposes of this Act, the taxable income earned in Canada for a taxation year of a person who at no time in the year is resident in Canada is the amount, if any, by which the amount that would be the non-resident person's income for the year under section 3 if	115 (1) Pour l'application de la présente loi, le revenu imposable gagné au Canada pour une année d'imposition d'une personne qui ne réside au Canada à aucun moment de l'année correspond à l'excédent éventuel du montant qui représenterait son revenu pour l'année selon l'article 3:
…	[…]
(b) the only taxable capital gains and allowable capital losses	b) si les seuls gains en capital imposables et les seules pertes en

referred to in paragraph 3(b) were taxable capital gains and allowable capital losses from dispositions, other than dispositions deemed under subsection 218.3(2), of taxable Canadian properties (other than treaty-protected properties), and …	capital déductibles visés à l'alinéa 3b) étaient de semblables gains et de semblables pertes provenant de la disposition (sauf la disposition réputée effectuée selon le paragraphe 218.3(2)) de biens canadiens imposables (sauf des biens protégés par traité);

[13] Taxable Canadian property is defined in subsection 248(1) of the Act. It is not necessary to include this definition, as there is no dispute that the shares of Alta Canada were taxable Canadian property. Their value was derived from Canadian resource properties (as defined in subsection 66(15) of the Act).

[14] Treaty-protected property is also defined in subsection 248(1) of the Act:

"treaty-protected property" of a taxpayer at any time means property any income or gain from the disposition of which by the taxpayer at that time would, because of a tax treaty with another country, be exempt from tax under Part I;	**« bien protégé par traité »** À un moment donné, bien d'un contribuable dont la disposition par lui à ce moment donne naissance à un revenu ou à un gain qui serait exonéré, par l'effet d'un traité fiscal, de l'impôt prévu à la partie I.

[15] Sections 38, 39 and 40 of the Act address how a taxpayer's taxable capital gain is to be calculated. Since there is no dispute with respect to the amount of the taxable capital gain, it is not necessary to recite these provisions.

[16] As a result, if:

(a) a person is resident in another country;

(b) that person disposes of taxable Canadian property and realizes a taxable capital gain;

(c) there is a treaty between Canada and the country where the person is resident; and

(d) under that treaty the gain on the disposition of the property is exempt from taxation in Canada;

the property will be a treaty-protected property for the purposes of the Act and the gain realized on the disposition of such property will not be subject to tax under the Act.

[17] In this case, the Crown is arguing that the GAAR applies. Since Alta Luxembourg concedes that there was a tax benefit and an avoidance transaction, the relevant provision is subsection 245(4) of the Act:

(4) Subsection (2) applies to a transaction only if it may reasonably be considered that the transaction	(4) Le paragraphe (2) ne s'applique qu'à l'opération dont il est raisonnable de considérer, selon le cas :
(a) would, if this Act were read without reference to this section, result directly or indirectly in a misuse of the provisions of any one or more of	a) qu'elle entraînerait, directement ou indirectement, s'il n'était pas tenu compte du présent article, un abus dans l'application des dispositions d'un ou de plusieurs des textes suivants :
(i) this Act,	(i) la présente loi,
(ii) the *Income Tax Regulations*,	(ii) le *Règlement de l'impôt sur le revenu*,
(iii) the *Income Tax Application Rules*,	(iii) les *Règles concernant l'application de l'impôt sur le revenu*,
(iv) a tax treaty, or	(iv) un traité fiscal,
(v) any other enactment that is relevant in computing tax or any	(v) tout autre texte législatif qui est utile soit pour le calcul d'un

other amount payable by or refundable to a person under this Act or in determining any amount that is relevant for the purposes of that computation; or

impôt ou de toute autre somme exigible ou remboursable sous le régime de la présente loi, soit pour la détermination de toute somme à prendre en compte dans ce calcul;

(b) would result directly or indirectly in an abuse having regard to those provisions, other than this section, read as a whole.

b) qu'elle entraînerait, directement ou indirectement, un abus dans l'application de ces dispositions compte non tenu du présent article lues dans leur ensemble.

III. Relevant Provisions of the Luxembourg Convention

[18] The relevant articles of the Luxembourg Convention are Articles 1, 4(1), 13(4) and 13(5):

Article 1

This Convention shall apply to persons who are residents of one or both of the Contracting States.

Article 4(1)

1. For the purposes of this Convention, the term "resident of a Contracting State" means any person who, under the laws of that State, is liable to tax therein by reason of that person's domicile, residence, place of management or any other criterion of a similar nature. This term also includes a Contracting State or a political subdivision or local authority thereof or any agency or instrumentality of any such State, subdivision or authority. This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State.

Articles 13(4) and (5)

4. Gains derived by a resident of a Contracting State from the alienation of:

a. shares (other than shares listed on an approved stock exchange in the other Contracting State) forming part of a substantial interest in the capital stock of a company the value of which shares is derived principally from immovable property situated in that other State; or

b. an interest in a partnership, trust or estate, the value of which is derived principally from immovable property situated in that other State,

may be taxed in that other State. For the purposes of this paragraph, the term "immovable property" does not include property (other than rental property) in which the business of the company, partnership, trust or estate was carried on; and a substantial interest exists when the resident and persons related thereto own 10 per cent or more of the shares of any class or the capital stock of a company.

5. Gains from the alienation of any property, other than that referred to in paragraphs 1 to 4 shall be taxable only in the Contracting State of which the alienator is a resident.

[19] The exemption from taxation in Canada, which is in issue in this case, arises as a result of the combination of Articles 13(4) and (5). Article 13(4) sets out the general rule for the right of Canada to tax a resident of Luxembourg on the gain arising from the alienation of shares or an interest in a partnership, trust or estate. Only the provisions as they relate to shares are relevant for this appeal. Article 13(4) does not apply to gains realized from the sale of shares that are listed on an approved stock exchange in Canada. Therefore, as a general rule, Canada has only reserved the right to tax gains arising on the alienation of shares of a private company (or shares not listed on an approved stock exchange in Canada).

[20] Two further restrictions on Canada's right to tax such gains are also present in this Article 13(4). The shares must form part of a substantial interest in the corporation and the value of the shares must be derived principally from immovable property situated in Canada. A resident of Luxembourg will have a substantial interest in the corporation if that resident and any person who is related to that resident own collectively at least 10% of the shares of any class of the corporation. If the resident of Luxembourg does not have a substantial interest in the

corporation, Canada has not reserved the right to tax any gain arising from the alienation of such shares under this Article.

[21] As a result, the general rule is that if a resident of Luxembourg owns 10% or more of the shares of a private company that owns real property in Canada (such that the value of its shares is principally derived from such real property), Canada has reserved the right to tax the gain arising from the sale of the shares of that company. Article 13(4), however, also provides a significant exception to this rule (which is the exception that is relevant in this case). Immovable property does not include property (other than rental property) in which the business of the corporation is carried on.

[22] The relevant net effect of Article 13(4), for the purposes of this appeal, is that Canada has surrendered its right to tax gains derived by a resident of Luxembourg from the sale of shares of a private corporation if the value of such shares is derived principally from immovable property (other than rental property) situated in Canada in which the business of the corporation is carried on.

[23] Since Article 13(4) would not apply to allow Canada to tax the gain on the disposition of such shares, Article 13(5) would apply and the gain could only be taxed in Luxembourg. For ease of reference, the applicable exemption will sometimes be referred to herein as the exemption in Article 13(4). Since the gain on such shares would be exempt from taxation in Canada under the Luxembourg Convention, such shares would be treaty-protected property for the purposes of the Act.

IV. Decision of the Tax Court

[24] The Crown, at the Tax Court hearing, raised two issues:

(a) whether the shares of Alta Canada qualified as treaty-protected property as a result of the application of Articles 13(4) and (5) of the Luxembourg Convention; and

(b) if the shares did qualify as treaty-protected property, whether the GAAR would apply to deny the tax benefit of only taxing the gain realized on the disposition of these shares in Luxembourg.

[25] The Tax Court Judge found that the shares of Alta Canada were treaty-protected property as a result of the application of Articles 13(4) and (5) of the Luxembourg Convention. In this appeal, the Crown does not challenge this finding.

[26] The Tax Court Judge also found that the GAAR did not apply because there was no abuse of the Act or the Luxembourg Convention. In this appeal, the Crown challenges this finding.

V. Issue and Standard of Review

[27] As noted above, Alta Luxembourg concedes that there was a tax benefit and an avoidance transaction. Therefore, in this appeal, the only issue is whether the transactions resulted in an abuse of the provisions of the Act or the Luxembourg Convention for the purposes of the application of the GAAR. As noted by this Court in *Canada v. Oxford Properties Group Inc.*, 2018 FCA 30, [2018] 4 F.C.R. 3 (*Oxford Properties*):

> [39] The inquiry as to whether there has been an abuse gives rise to a question of mixed fact and law and is therefore subject to the standard of palpable and overriding error (*Trustco* at para. 44; *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235 (S.C.C.) at para. 37 [*Housen*]). However, the abuse analysis proceeds in two stages. The first stage requires the determination of the object, spirit and purpose of the provisions giving rise to the tax benefit while the second turns on whether the provisions, so construed, were frustrated by the tax benefit achieved (*Trustco* at para. 44). The object, spirit and purpose of a provision is discerned by way of statutory interpretation (*Copthorne* at para. 70). This gives rise to a question of law and is an extricable part of the analysis. It is therefore subject to the standard of correctness (*Trustco* at para. 44; *Housen* at paras. 8, 37).

VI. Analysis

[28] Under the Act, taxable capital gains realized by non-residents of Canada as a result of a disposition of a taxable Canadian property will be subject to tax in Canada, unless the property is a treaty-protected property. If Canada has agreed in a treaty with another country that any gain arising from the disposition of a property will be exempt from tax under Part I of the Act, then such property will be a treaty-protected property. In this case, an exemption from such tax in Canada has been included in the Luxembourg Convention.

[29] The particular exemption that is in issue in this appeal is not in all of the treaties negotiated by Canada with other countries. In particular, as noted by the Crown, it is not included in the *Convention Between Canada and the United States of America With Respect to Taxes on Income and on Capital* (the Canada-U.S. Tax Treaty). The Crown appeared to be implying that because this exemption was not in all of the treaties that Canada has signed, the exemption in the Luxembourg Convention should be restricted.

[30] However, the presence of this provision in the Luxembourg Convention – and not in all treaties that Canada has signed – must mean that the result under the Luxembourg Convention in relation to the gain to which the exemption applies would not be the same as it would be under any other treaty where this exemption was not included, such as the Canada-U.S. Tax Treaty. The provisions of the Luxembourg Convention must be examined to determine their object, spirit and purpose. The Canada-U.S. Tax Treaty, which does not include this exemption, is of little assistance in determining the rationale for this provision in the Luxembourg Convention.

[31] Although the Crown raised the issue of whether there was an abuse of paragraph 115(1)(b) of the Act, the focus of the hearing was on whether there was an abuse of the relevant provisions of the Luxembourg Convention. The carve-out for treaty-protected property in paragraph 115(1)(b) of the Act simply reflects what Canada had agreed to do under the Luxembourg Convention, i.e. to not tax the gain realized on the dispositions of certain properties. Therefore, in my view, the proper focus for the GAAR analysis, in this case, is on the provisions of the Luxembourg Convention. If there is no abuse of the Luxembourg Convention, there would be no abuse of paragraph 115(1)(b) of the Act.

[32] As noted in *Oxford Properties*, the first step in the analysis is to determine the object, spirit and purpose of the provisions giving rise to the tax benefit. In this particular case, the tax benefit in question is the exemption from tax in Canada on the taxable capital gain realized on the disposition of the shares of Alta Canada. Articles 13(4) and (5) of the Luxembourg Convention describe the property that would be exempt from taxation in Canada (and hence would qualify as treaty-protected property for the purposes of the Act).

[33] In *Canada Trustco Mortgage Co. v. Canada*, 2005 SCC 54, [2005] 2 S.C.R. 601 (*Trustco)*, the Supreme Court of Canada noted that:

> 64 By contrast, the inquiry into abusive tax avoidance under s. 245(4) involves a textual, contextual and purposive analysis of the provisions on which the tax benefit is based. We see no reason to maintain the distinction between a theoretical and practical perspective on the burden of proof, adopted by the majority of the Federal Court of Appeal in *OSFC* [*OSFC Holdings Ltd. v. Canada*, 2001 FCA 260, [2002] F.C. 288]. The Federal Court of Appeal held that there is no burden on either party at the stage of interpreting the provisions at issue, since this is a question of law, which is ultimately for the court to decide. It went on to state at para. 68 that "from a practical perspective, ... [t]he Minister should set out the policy with reference to the provisions of the Act or extrinsic aids upon which he relies".
>
> 65 For practical purposes, the last statement is the important one. The taxpayer, once he or she has shown compliance with the wording of a provision, should not be required to disprove that he or she has thereby violated the object, spirit or purpose of the provision. It is for the Minister who seeks to rely on the GAAR to identify the object, spirit or purpose of the provisions that are claimed to have been frustrated or defeated, when the provisions of the Act are interpreted in a textual, contextual and purposive manner. The Minister is in a better position than the taxpayer to make submissions on legislative intent with a view to interpreting the provisions harmoniously within the broader statutory scheme that is relevant to the transaction at issue.
>
> (emphasis added)

[34] In this case, the Crown concedes that Alta Luxembourg has complied with the wording of Articles 1, 4, 13(4) and (5) of the Luxembourg Convention. Therefore, it falls to the Crown to identify the object, spirit or purpose of the provisions that, according to the Crown, have been frustrated or defeated.

[35] The Crown dedicated 19 paragraphs of its memorandum to the “Underlying Rationale: Articles 1, 4 and 13(4) of the [Luxembourg] Convention”. However, most of the paragraphs

contain only references to general principles, a review of the text of the relevant provisions of the Luxembourg Convention, and references to general commentary or decisions that do not address the rationale for the provisions in issue in this case.

[36] As part of these submissions, the Crown includes references to the commentaries related to certain Model Tax Conventions prepared by the Organization for Economic Co-operation and Development (the OECD). It is not clear whether those commentaries are related to the 1998 Model Tax Convention or some other model convention. In any event, the only model conventions included in the joint book of authorities are dated 1998 or later. The first convention between Canada and Luxembourg was adopted by the *Canada-Luxembourg Income Tax Convention Act*, *1989*, S.C. 1989, c. 20, s 3. This version of the convention also included the exemption in issue in this case, although the wording was slightly different. The commentaries, to which the Crown referred, relate to an OECD Model Tax Convention that was created after the particular exemption in issue was included in the first convention between Canada and Luxembourg. These commentaries were written for a model convention that was not adopted by Canada and Luxembourg. These commentaries are of little assistance in determining the rationale for the exemption that is in issue in this case.

[37] Paragraph 91 of the Crown's memorandum is the closest that the Crown comes to identifying the rationale for the provisions. However, it is worded in the negative and it is a general statement of what the Crown asserts was *not* the intent of these provisions.

[38] In paragraph 91 of its memorandum, the Crown submits that:

> 91. Articles 1, 4 and 13(4) of the Convention, together, are intended to grant a particular treaty benefit to Luxembourg investors whose investments in specific taxable Canadian property gives rise to gains for them, in Luxembourg. Those provisions are not intended to benefit entities who do not have the potential to realize income in Luxembourg, nor have any commercial or economic ties therewith. Such situations are wholly dissimilar to the relationships or transactions that are contemplated by those provisions of the Convention.

[39] There are three key aspects of this short paragraph that need to be addressed:

(a) the change in the identity of who will qualify for the exemption from “residents” to “investors”;

(b) the statement that the provisions “are not intended to benefit entities who do not have the potential to realize income in Luxembourg”, which would add a qualification that the “entity” must have the potential to earn income in Luxembourg; and

(c) the statement that the provisions “are not intended to benefit entities who do not have … any commercial or economic ties” with Luxembourg, which would add a requirement for commercial or economic ties to Luxembourg.

A. *Investor v. Resident*

[40] The opening words of Article 13(4) of the Luxembourg Convention are clear: “Gains derived by a *resident* of a Contracting State…” (emphasis added). The exemption is provided to Luxembourg *residents*, not investors. Article 1 also makes it clear that the Luxembourg Convention applies to “persons who are *residents* of one or both of the Contracting States” (emphasis added). The Crown does not provide any explanation for why “investor” was substituted for “resident”.

[41] The Tax Court Judge, however, did include, in his description of the rationale for the relevant provisions of the Luxembourg Convention, a reference to an “investment”. The Tax Court Judge found that:

> [100] …The rationale underlying the carve-out is to exempt residents of Luxembourg from Canadian taxation where there is an investment in immovable property used in a business. The significant investments of the Appellant to de-risk the Duvernay shale constitute an investment in immovable property used in a business. Therefore, I conclude that the GAAR does not apply to preclude the Appellant from claiming the exemption provided for under Article 13(5) of the Treaty.

[42] In this statement, the Tax Court Judge did not identify the source or the amount of the investment that would be required in order for the exemption to be applicable. This statement also reflects his comments in paragraph 43: “the Excluded Property exception appears to have been intended, *inter alia*, to encourage investments by Luxembourg residents in Immovable Property acquired to be used in a company's business”.

[43] The comments in paragraph 43 immediately follow a quoted excerpt from a document that the Tax Court Judge identified as being dated January 31, 1991, but which, presumably, is the document bearing the dates of January 23, 1991, and February 28, 1991. In any event, the document refers to the various treaties that Canada had signed which include the exemption in issue in this case. The document was prepared in response to a number of requests that the government had received “for technical interpretations concerning what is meant by ‘property, other than rental property, in which the business of the company was carried on’ (hereinafter called ‘Excluded Property’) in the context of resource industries” (page 1 of E9011711 – “Capital Gain Exemption”).

[44] The one position from this document that was quoted by the Tax Court Judge (at paragraph 42 of his reasons) is the last position that is set out therein:

> 6. Immovable property (e.g. real estate) that is not used or held for use in the company's business but is held as an investment for capital gain is not Excluded Property.
>
> (emphasis in original)

[45] This statement – that property that is held as an investment (on which the company expects to make a capital gain) will not be excluded property – does not necessarily lead to the conclusion that, in order for a shareholder of a corporation to be eligible to claim the exemption from taxation in Canada, such person must invest in that corporation. This statement simply relates to the reason why a particular property is being held by the corporation. It is not a statement related to the source of any funds that were used to buy that asset.

[46] Even if, as noted by the Tax Court Judge in paragraph 43 of his reasons, one of the objectives for the exemption was to encourage investment in Canada, it does not seem to me that this should be elevated to the status of a requirement that must be met to claim the exemption from tax in Canada. While the GAAR can change the tax consequences from what they would otherwise be, the GAAR cannot be used, in this case, to justify adding a requirement for investment that is not present in the Luxembourg Convention.

[47] Articles 13(4) and (5) of the Luxembourg Convention provide that a person who has sold shares of a private Canadian corporation that comprise part of a substantial interest (i.e. 10% or

more) of the shares of any class of that corporation will not be subject to tax in Canada on the gain realized on such disposition, if the following conditions are satisfied:

(a) the person is a resident of Luxembourg; and

(b) the value of those shares is derived principally from immovable property (other than rental property) in which the business of the corporation is carried on.

[48] There is no requirement that the person invest any particular amount in the corporation. As noted above, if the person and any related persons own less than 10% of the shares, the gain would not be taxable in Canada, regardless of what assets are held by the corporation.
The threshold for ownership of shares (at which point the assets held by the corporation are relevant) is only 10% of the shares of any class. This raises the question of whether the object, spirit and purpose of the exemption from taxation in Canada would necessarily be linked to a mandatory requirement that a minority shareholder (owning only 10% of the shares) resident in Luxembourg provide funds to a corporation that is carrying on business in Canada which is thousands of kilometres away.

[49] It does not seem to me that claiming the exemption from tax in Canada, on the gain realized on a sale of shares of a particular company, is predicated on the resident of Luxembourg having made any particular investment in that company. To add a requirement that the resident of Luxembourg must have made an investment in the relevant company, would then require speculation on the amount and the source of such investment that would be necessary for the person to be eligible for the exemption from tax in Canada. The requirements of the Luxembourg Convention are simply that the person claiming the exemption (who holds a substantial interest)

is a resident of Luxembourg, and that the company (whose shares were sold) satisfies the asset test as set out in Article 13(4). There are no further requirements.

[50] The lack of a requirement for the resident of Luxembourg to invest in the particular company can also be illustrated by considering an example outside the GAAR context. For example, assume that an individual, who is a resident of Luxembourg, inherits 10% of the shares of a private company. Assume that the value of that company is derived principally from immovable property (other than rental property) situated in Canada in which the business of the company is carried on. On what basis would the individual not qualify for the exemption from tax on any capital gain realized on any subsequent disposition of those shares, regardless of whether that individual actually invests any money in the company?

[51] As noted by the Supreme Court of Canada in *Copthorne Holdings Ltd. v. Canada*, 2011 SCC 63, [2011] 3 S.C.R. 721 (*Copthorne*):

> [69] In order to determine whether a transaction is an abuse or misuse of the Act, a court must first determine the "object, spirit or purpose of the provisions … that are relied on for the tax benefit, having regard to the scheme of the Act, the relevant provisions and permissible extrinsic aids" (*Trustco*, at para. 55). The object, spirit or purpose of the provisions has been referred to as the "legislative rationale that underlies specific or interrelated provisions of the Act" (V. Krishna, *The Fundamentals of Income Tax Law* (2009), at p. 818).
>
> [70] The object, spirit or purpose can be identified by applying the same interpretive approach employed by this Court in all questions of statutory interpretation — a "unified textual, contextual and purposive approach" (*Trustco*, at para. 47; *Lipson v. Canada*, 2009 SCC 1, [2009] 1 S.C.R. 3, at para. 26). While the approach is the same as in all statutory interpretation, the analysis seeks to determine a different aspect of the statute than in other cases. In a traditional statutory interpretation approach the court applies the textual, contextual and purposive analysis to determine what the words of the statute mean. In a GAAR analysis the textual, contextual and purposive analysis is employed to determine

> the object, spirit or purpose of a provision. Here the meaning of the words of the statute may be clear enough. The search is for the rationale that underlies the words that may not be captured by the bare meaning of the words themselves. However, determining the rationale of the relevant provisions of the Act should not be conflated with a value judgment of what is right or wrong nor with theories about what tax law ought to be or ought to do.

[52] Whether searching for the rationale that underlies the words in a GAAR case, or for the meaning of the words in a case where the GAAR is not invoked, the same interpretative approach is applied – a "unified textual, contextual and purposive approach". In applying this approach in this case, the GAAR cannot be used to add a requirement for investment that would have to be satisfied if the GAAR applied, but which would not have to be satisfied if the GAAR did not apply. If, in applying the GAAR, an additional requirement is inferred that the resident of Luxembourg must invest in the corporation in order to qualify for the exemption, this could lead to the result that it would be an abuse of the Luxembourg Convention, if the person did not invest in the particular corporation. This would result in a significant change in the requirements that the resident of Luxembourg would have to satisfy. In my view, the addition of this requirement is not warranted. There is nothing to suggest that the underlying rationale for the exemption is that it would only be available to a resident of Luxembourg who invests in the particular corporation in which such resident holds shares.

[53] Article 13(4) applies to the residents of each contracting state. If a person is a resident of Luxembourg as defined in Article 4, then that person is also a resident for the purposes of Article 13(4). The Crown does not dispute that Alta Luxembourg was a resident of Luxembourg for the purposes of the Luxembourg Convention. This is sufficient to satisfy this requirement as set out in Article 13(4), without any necessity to determine what, if any, amounts Alta Luxembourg

invested in Alta Canada. Of course, if Alta Luxembourg had not made the significant investments that it did in Alta Canada, it probably would not have realized the large gain that is referred to in paragraph 10 above.

B. *Potential to Earn Income*

[54] The comments of the Crown, in relation to the potential to realize income in Luxembourg, appear to be related to the Profit Participating Facility Agreement that Alta Luxembourg entered into with Alta Energy Canada Partnership, which held all of the shares of Alta Luxembourg. Under this agreement, Alta Luxembourg borrowed significant sums of money from the partnership. Clause 4.1 of this agreement provided that the interest on the outstanding debt "shall be composed of a profit sharing interest (the Variable Interest) and an ordinary interest (the Fixed Interest)". The Variable Interest was determined under Clause 4.2.1 and was 100 per cent of the Adjusted Net Profit minus the Fixed Interest and certain other amounts.

[55] There is no dispute that the amount of the capital gain in issue in this case, for the purposes of the Act, is in excess of $380 million (and therefore this interest was not deductible in computing this gain). It is, however, not clear whether, in determining the income that would be subject to tax in Luxembourg, the gain realized on the sale of the shares of Alta Canada would be included in computing the net profit of Alta Luxembourg and whether this Variable Interest would be deductible. Assuming that such gain would be included in determining the net profit of Alta Luxembourg and that the full amount for the Variable Interest would be allowed as a deduction in computing the income that would be subject to tax in Luxembourg, the result of

these provisions appears to be that Alta Luxembourg would not have any taxable income in Luxembourg. This would presumably mean that no income tax would be payable in Luxembourg.

[56] This concern that the net effect of the Profit Participating Facility Agreement would result in Alta Luxembourg never realizing taxable income in Luxembourg, is also reflected in the concluding paragraph in the section of the Crown's memorandum that addresses the "Underlying rationale: Articles 1, 4 and 13(4) of the [Luxembourg] Convention". This concluding paragraph states:

> 94. The facts remain of utmost importance in a GAAR analysis. The GAAR framework, particularly the second part of the abuse enquiry, ensures a line can be drawn between acceptable tax planning and abusive tax avoidance. In this case, the fact it was impossible for the Respondent, set up in Luxembourg in contemplation of the realization of a gain, to realize any income in Luxembourg resulted in the abuse of the provisions of the Convention. The GAAR is expected, as stated by the OECD, to "play an important role in preventing treaty benefits from being granted in inappropriate circumstances", such as in the present case.

[57] However, whether the result of the Profit Participating Facility Agreement is that Alta Luxembourg will not have any taxable income in Luxembourg is a matter for the Luxembourg tax authorities (subject, in the event of a dispute, to any review or appeal process that may be available in Luxembourg). It is not a matter that is before this Court. In any event, this paragraph appears to ignore the two-step process in the abuse analysis, as described in *Oxford Properties*. The first step of the process is to identify the object, spirit, and purpose of the relevant provisions. The second step is to determine whether the transactions resulted in an abuse of these provisions. Paragraph 94 of the Crown's memorandum states the conclusion that there is an abuse of the provisions without identifying the underlying rationale or object, spirit and purpose

of the provisions in question. The caution expressed by the Supreme Court of Canada in *Copthorne* is relevant:

> [70] … However, determining the rationale of the relevant provisions of the Act should not be conflated with a value judgment of what is right or wrong nor with theories about what tax law ought to be or ought to do.

[58] The definition of "resident" in Article 4 provides that a person "who, under the laws of that State, is liable to tax therein by reason of that person's domicile, residence, place of management or any other criterion of a similar nature" will be a resident. A person is a resident if that person is liable to tax for the reasons as stated in Article 4. The level or amount of tax is not relevant. To add or infer a condition that a resident will only be a resident of Luxembourg for the purposes of the Luxembourg Convention if a certain amount of tax is paid, would alter the definition from the words as chosen. Whether Luxembourg will impose any income tax on Alta Luxembourg is a matter for the Luxembourg tax authorities (subject, in the event of a dispute, to any review or appeal process that may be available in Luxembourg).

[59] The Crown has not challenged the finding that the provisions of the Luxembourg Convention apply to Alta Luxembourg (subject only to the application of the GAAR). Therefore, it is not challenging the finding that Alta Luxembourg satisfies the definition of a resident of Luxembourg for the purposes of this Convention. By attempting to include, as a rationale for the provisions, the requirement that a person can only access the exemption if that person actually pays tax, the Crown is either:

(a) attempting to create two classes of residents – those who actually pay taxes and those who do not; or

(b) attempting to argue that Alta Luxembourg is not a resident of Luxembourg.

[60] Neither alternative is appropriate. If the Crown is attempting to create two classes of residents, this would deny the benefit of Article 13(4) based on something other than the qualification of the person as a resident under Article 4. I do not agree with this proposition. The Luxembourg Convention is clear that the benefit is available to a resident of Luxembourg, not to only certain residents who satisfy some other condition that is not part of the definition of a resident in Article 4.

[61] If this is an attempt to argue that Alta Luxembourg is not a resident of Luxembourg for the purposes of the Luxembourg Convention, then the Crown cannot now make that argument. The Crown has not challenged the finding that Alta Luxembourg is a resident of Luxembourg for the purposes of the Luxembourg Convention. By conceding that Alta Luxembourg is a resident of Luxembourg for the purposes of the Luxembourg Convention, the Crown is conceding that Alta Luxembourg was liable for tax in Luxembourg. The Crown cannot now indirectly argue that Alta Luxembourg was not liable for tax in Luxembourg.

[62] There is no basis to find that the rationale for the definition of “resident” would suggest that any criteria other than the criteria included in the definition of resident in Article 4, should be used to determine if a person is a resident of Luxembourg for the purposes of the Luxembourg Convention.

C. *Commercial or Economic Ties*

[63] The implied characterization by the Crown, in paragraph 91 of its memorandum, that the underlying purpose for the exemption is to benefit only persons who have some commercial or economic ties to Luxembourg, is similar to the submissions made in *Garron Family Trust v. The Queen*, 2009 TCC 450, [2010] 2 C.T.C. 2346. Justice Woods, as she then was, dismissed these arguments:

> [380] The Minister also submits that the *Treaty* exemption was not intended to apply to the Trusts because they had very little connection with Barbados. It was noted that the assets, contributors and beneficiaries are all Canadian. To apply the *Treaty* exemption in these circumstances would facilitate the avoidance of tax by Canadians.
>
> [381] The problem that I have with this argument is that, if accepted, it would result in a selective application of the *Treaty* to residents of Barbados, depending on criteria other than residence. It seems to me that this is contrary to the object and spirit of the *Treaty*, which is apparent in Article I and Article IV(1). Residents of Barbados, as defined for purposes of the *Treaty*, are entitled to the benefits of Article XIV(4) as long as they are not also residents of Canada.
>
> [382] I would also mention that there is no special rule for trusts in the *Treaty*. They are defined as persons in Article III(1)(c) of the *Treaty*.
>
> [383] If the Trusts are resident only in Barbados under these principles, then the *Treaty* contemplates that Article XIV(4) will apply to them. It does not matter that the Trusts have few connections with Barbados.
>
> (emphasis added)

[64] In dismissing the appeal (identified as *St. Michael Trust Corp. v. Canada*, 2010 FCA 309, [2012] 2 F.C.R. 374), this Court noted that:

> [89] If, contrary to the opinions expressed above, the residence of a trust is to be determined only on the basis of the residence of the trustee and therefore the Trusts are resident in Barbados, but are entitled to the exemption in paragraph 4 of Article XIV of the Barbados Tax Treaty, it would be necessary to consider whether the assessments under appeal are nevertheless justified by the general anti-avoidance rule in section 245 of the *Income Tax Act*. In this Court as in the Tax Court, that issue turns on whether the series of transactions that resulted in the Trusts becoming entitled to the treaty exemption in the face of section 94 is a misuse or abuse of the Barbados Tax Treaty. Justice Woods said no. I agree.
>
> [90] If the residence of the Trusts is to be determined on the basis of the residence of St. Michael Trust Corp. (which is the premise for the Crown's argument based on the general anti-avoidance rule), then the Trusts have not avoided section 94. On the contrary, they have fallen squarely into it. The fact that the Trusts would also be entitled to a treaty exemption flows from the fact that in the Barbados Tax Treaty, Canada has agreed not to tax certain capital gains realized by a person who is a resident of Barbados. If the residence of the Trusts is Barbados for treaty purposes, the Trusts cannot misuse or abuse the Barbados Tax Treaty by claiming the exemption.

[65] The same logic applies here. Since there is no dispute that Alta Luxembourg is a resident of Luxembourg, it is entitled to claim the benefit of Articles 13(4) and (5) of the Luxembourg Convention. There is no distinction in the Luxembourg Convention between residents with strong economic or commercial ties and those with weak or no commercial or economic ties. If a person satisfies the definition of resident in Article 4, then that person is a resident for the purposes of Articles 13(4) and (5). The Crown did not provide any support for its contention that the object, spirit and purpose of Articles 13(4) and (5) was only to exclude from taxation in Canada gains arising from the disposition of shares held by Luxembourg residents with strong economic or commercial ties to Luxembourg.

D. *Conclusion on the Rationale for Articles 1, 4 and 13(4)*

[66] The Crown has not identified any clear rationale for the provisions of Articles 1, 4 and 13(4) of the Luxembourg Convention, other than what can be gleaned from the text of these provisions. In *Copthorne*, the Supreme Court of Canada noted that:

> [110] I do not rule out the possibility that in some cases the underlying rationale of a provision would be no broader than the text itself. Provisions that may be so construed, having regard to their context and purpose, may support the argument that the text is conclusive because the text is consistent with and fully explains its underlying rationale.

[67] The text of the provisions provides that the exemption from tax in Canada is available to residents of Luxembourg who realize a gain from the sale of shares of a company, if the underlying value of that company is derived from immovable property (other than rental property) used in a business carried on in Canada.

[68] During the hearing of this appeal, the Crown implied that the residence of the partners of Alta Energy Canada Partnership (which held the shares of Alta Luxembourg) was a relevant factor. However, the exemption in the Luxembourg Convention does not include a qualification based on the ownership of the shares of any resident corporation that sold the shares that gave rise to the gain in issue. It would not seem appropriate, in the absence of express language requiring the Court to do so, to search for an underlying rationale for corporate residents that would require the Court to pierce the corporate veil to determine who owns the shares of the resident corporation. If the exemption was only intended to apply to certain corporate residents

of Luxembourg, then whatever qualification was intended could have been specified in the Luxembourg Convention.

[69] In my view, the rationale for the relevant provisions of the Luxembourg Convention can be found in the text of these provisions. These provisions are neither lengthy nor complex. The only external aid that is related to these provisions is the technical interpretation referred to in paragraphs 43 - 45 above. As noted above, this technical interpretation is of little assistance in determining the rationale for these provisions.

[70] As a result, these provisions speak for themselves. This conclusion (that the rationale for the relevant provisions of the Luxembourg Convention can be found in the text of these provisions) is also reflected in the decision of this Court in *MIL (Investments) S.A. v. Canada*, 2007 FCA 236, [2007] 4 C.T.C. 235. The issue in that case was also the application of the GAAR in relation to Article 13(4) of the Luxembourg Convention.

[71] The Tax Court Judge in *MIL (Investments) S.A. v. The Queen,* 2006 TCC 460, [2006] 5 C.T.C. 2552 found that none of the transactions in question in that case was an avoidance transaction. Therefore, he did not need to address the issue of whether there was an abuse of the Luxembourg Convention.

[72] On appeal, the taxpayer conceded that its continuance as a Luxembourg corporation was an avoidance transaction. The question was then whether the sale of shares was part of the same

series of transactions. In determining that it did not have to answer this question to decide whether the GAAR applied, this Court stated that:

> [5] We do not have to answer that question as we are of the view that the appeal would fail in any event as we are unable to see in the specific provisions of the Income Tax Act, R.S.C. 1985, c. 1 (5th Supp.) (the Act) and the Tax Treaty to which we were referred, interpreted purposively and contextually, any support for the argument that the tax benefit obtained by the respondent was an abuse or misuse of the object and purpose of any of those dispositions.
>
> [6] It is clear that the Act intends to exempt non-residents from taxation on the gains from the disposition of treat *[sic]* exempt property. It is also clear that under the terms of the Tax Treaty, the respondent's stake in DFR was treaty exempt property. The appellant urged us to look behind this textual compliance with the relevant provisions to find an object or purpose whose abuse would justify our departure from the plain words of the disposition. We are unable to find such an object or purpose.
>
> [7] If the object of the exempting provision was to be limited to portfolio investments, or to non-controlling interests in immoveable property (as defined in the Tax Treaty), as the appellant argues, it would have been easy enough to say so. Beyond that, and more importantly, the appellant was unable to explain how the fact that the respondent or Mr. Boulle had or retained influence of control over DFR, if indeed they did, was in itself a reason to subject the gain from the sale of the shares to Canadian taxation rather than taxation in Luxembourg.
>
> [8] To the extent that the appellant argues that the Tax Treaty should not be interpreted so as to permit double non-taxation, the issue raised by GAAR is the incidence of Canadian taxation, not the foregoing of revenues by the Luxembourg fiscal authorities.
>
> (emphasis added)

[73] Just as this Court was unable to find any rationale behind Article 13(4) and the related provisions of the Luxembourg Convention, other than as reflected in the words chosen for these provisions, I am also unable to find any object, spirit, or purpose other than as reflected in these words. The object, spirit and purpose of Articles 1, 4 and 13(4) is that a person will qualify for

the exemption in issue in this appeal, which is applicable to gains arising on the disposition of certain shares, if:

(a) that person is a resident of Luxembourg for the purposes of the Luxembourg Convention, and

(b) the value of the shares is principally derived from immovable property (other than rental property) situated in Canada in which the business of that corporation is carried on.

E. *Treaty Shopping*

[74] The Crown also referred to an excerpt from the comments of Justice Iaccobucci in paragraph 52 of *Crown Forest Industries Ltd. v. The Queen*, [1995] 2 S.C.R. 802, 1995 CanLII 103 (SCC). The application of the GAAR was not in issue in that case. The full text of paragraph 52 of *Crown Forest* is as follows:

> 52. But the shortcomings to the respondent's interpretation go beyond the scenarios envisioned by the appellant. In fact, under the respondent's interpretation, a foreign corporation whose place of management is in the U.S. would be a resident of the U.S. for purposes of the Convention notwithstanding that such a corporation may not have any effectively connected income to the U.S. and hence no U.S. tax liability at all. I find this possibility to be highly undesirable. "Treaty shopping" might be encouraged in which enterprises could route their income through particular states in order to avail themselves of benefits that were designed to be given only to residents of the contracting states. This result would be patently contrary to the basis on which Canada ceded its jurisdiction to tax as the source country, namely that the U.S. as the resident country would tax the income. On this point, see also Richard G. Tremblay, "Crown Forest -- Tax Treaty Interpretation Bonanza" (1994), 4 Can. Curr. Tax C41.

[75] The comments of Justice Iaccobucci in *Crown Forest* were raised in relation to treaty shopping. The only direct reference to “treaty shopping” in the Crown’s memorandum (other than in a footnote) is in paragraph 61:

> 61. The Government of Canada has, for many years, consistently expressed the position that it would challenge abusive treaty shopping arrangements, including by having recourse to the GAAR. In addition, many of Canada’s tax treaties contain specific provisions that are intended to limit treaty abuses. For example some of Canada’s treaties contain provisions that limit access to treaty benefits (e.g. by denying treaty benefits for certain types of entities, or with respect to certain transactions). However, such provisions do not preclude the application of the GAAR to counter the abusive use of the provisions of the treaty.
>
> (footnote references have been omitted)

[76] The footnote reference for the first sentence is to the “Consultation Paper on Treaty Shopping – The Problem and Possible Solutions”, Canada, Department of Finance: August 2013 and to earlier Technical Interpretations provided by the Canada Revenue Agency.

[77] The Tax Court Judge also referred to the steps that the Department of Finance indicated that it would be taking to curb treaty shopping. However, there were no steps that were taken prior to the transactions in this case. Any actual steps that were taken after the transactions in this case were completed, or that may possibly be taken in the future, are not applicable in this case but may have an impact on future transactions.

[78] With respect to treaty shopping, the Tax Court Judge in *MIL (Investments) S.A.* noted that:

> [72] In written argument, Respondent's counsel argued that 'treaty shopping' is an abuse of bilateral tax conventions and that this is recognized by the Supreme Court of Canada. In oral argument, the following passage from *Crown Forest Industries Limited v. The Queen*, [1995] 2 S.C.R. 802 at page 825, was quoted to establish that if the Supreme Court had access to section 245, it would have used that section to deny a benefit from "treaty shopping":
>
>> It seems to me that both Norsk and the respondent are seeking to minimize their tax liability by picking and choosing the international tax regimes most immediately beneficial to them. Although there is nothing improper with such behaviour, I certainly believe that it is not to be encouraged or promoted by judicial interpretation of existing agreements...
>
> I do not agree that Justice Iaccobucci's *obiter dicta* can be used to establish a prima facie finding of abuse arising from the choice of the most beneficial treaty. There is nothing inherently proper or improper with selecting one foreign regime over another. Respondent's counsel was correct in arguing that the selection of a low tax jurisdiction may speak persuasively as evidence of a tax purpose for an alleged avoidance transaction, but the shopping or selection of a treaty to minimize tax on its own cannot be viewed as being abusive. It is the *use* of the selected treaty that must be examined.
>
> (emphasis in original and footnote references have been omitted)

[79] The issue and arguments of the Crown, in this case, were consistent with these comments, as the Crown focused on the provisions of the Luxembourg Convention itself.

VII. Conclusion

[80] I agree with the decision of this Court in *MIL (Investments) S.A.* that the object, spirit and purpose of the relevant provisions of the Luxembourg Convention is reflected in the words as chosen by Canada and Luxembourg. Since the provisions operated as they were intended to operate, there was no abuse.

[81] As a result, I would dismiss the appeal.

[82] Alta Luxembourg, in its memorandum, requested the opportunity to provide written submissions on costs, if it was successful in this appeal. I would propose that the parties first be given the opportunity to reach an agreement on costs, failing which submissions could be made. I would propose that if the parties are unable to reach an agreement on costs by March 13, 2020, Alta Luxembourg will have the right to make additional written submissions, not exceeding 10 pages, on costs on or before April 3, 2020. The Crown will then have the right to make written submissions, not exceeding 10 pages, on costs on or before April 24, 2020. Alta Luxembourg will then have the right to make reply submissions, not exceeding three pages, on or before May 1, 2020. The parties are to notify the Court on or before March 13, 2020 whether an agreement on costs has been reached and, if so, the terms of that agreement.

"Wyman W. Webb"
J.A.

"I agree
D. G. Near J.A."

"I agree
George R. Locke J.A."

FEDERAL COURT OF APPEAL

NAMES OF COUNSEL AND SOLICITORS OF RECORD

APPEAL FROM A JUDGMENT OF THE TAX COURT OF CANADA DATED AUGUST 22, 2018, CITATION NO. 2018 TCC 152, DOCKET NO. 2014-4359(IT)G

DOCKET:	A-315-18
STYLE OF CAUSE:	HER MAJESTY THE QUEEN v. ALTA ENERGY LUXEMBOURG S.A.R.L.
PLACE OF HEARING:	TORONTO, ONTARIO
DATE OF HEARING:	NOVEMBER 12, 2019
REASONS FOR JUDGMENT BY:	WEBB J.A.
CONCURRED IN BY:	NEAR J.A. LOCKE J.A.
DATED:	FEBRUARY 12, 2020

APPEARANCES:

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