Docket: 2005-469(IT)G

BETWEEN:

CANWEST MEDIAWORKS INC.
(successor by amalgamation to CanVideo Television Sales (1983) Limited),
Appellant,

and

HER MAJESTY THE QUEEN,
Respondent.

Appeal heard on October 11, 2006, at Toronto, Ontario, by
The Honourable Justice Campbell J. Miller

Appearances:

Counsel for the Appellant:	Ian S. MacGregor and Kimberley J. Wharram
Counsel for the Respondent:	Donald G. Gibson

JUDGMENT

The appeal from the reassessment of tax made under the *Income Tax Act* for the 1997 taxation year is allowed, and the reassessment of August 16, 2004, is vacated as it was made beyond the maximum reassessment period of the *Canada-Barbados Income Tax Convention, 1980*. The Appellant is entitled to its costs.

Signed at Ottawa, Canada, this 24th day of October, 2006.

"Campbell J. Miller"
Miller J.

Citation: 2006TCC579
Date: 20061024
Docket: 2005-469(IT)G

BETWEEN:

CANWEST MEDIAWORKS INC.
(successor by amalgamation to CanVideo Television Sales (1983) Limited),

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Miller J.

[1] The Appellant, Canwest Mediaworks Inc., is the successor by amalgamation to CanVideo Television Sales (1983) Limited (CanVideo). Canwest International Communications Inc. (CICI) was a resident Barbadian company and a controlled foreign affiliate (CFA) of CanVideo at the relevant time. The Minister of National Revenue (the Minister), relying on the foreign accrual property income (FAPI) provisions of section 91 of the *Income Tax Act* (the *Act*), reassessed CanVideo for its 1997 taxation year within the time limits provided by Canadian domestic laws (due to a waiver), though beyond the five-year limitation period set forth in *Article* XXVII(3) of the *Canada-Barbados Income Tax Convention, 1980* (the "*Treaty*"). The Minister justifies the reassessment on the basis that *Article XXX*(2) of the *Treaty* overrides *Article* XXVII(3).

[2] *Article* XXVII(3) and XXX(2) of the *Treaty* read as follows:

> XXVII(3) A Contracting State shall not, after the expiry of the time limits provided in its national laws and, in any case, after five years from the end of the taxable period in which the income concerned has accrued, increase the tax base of a resident of either Contracting State by including therein items of income which have also been charged to tax in the other Contracting State. This paragraph shall not apply in the case of fraud, wilful default or neglect.
>
> …
>
> XXX(2) Nothing in this Agreement shall be construed so as to prevent Canada from imposing its tax on amounts included in the income of a resident of Canada according to section 91 of the Canadian *Income Tax Act*.

[3] The sole issue is whether the limitation period in *Article* XXVII(3) applies or whether *Article* XXX(2) overrides the limitation period, allowing the Minister's reassessment after the five-year limitation period. I find the limitation period applies and the Minister's reassessment was issued too late.

[4] The parties provided an Agreed Statement of Facts which put some meat on the factual barebones set forth in the previous paragraphs. The following are segments of those agreed facts:

> 6. During its taxation year ending August 31, 1996 (the "1996 CICI Taxation Year"), CICI earned, among its other income, interest on treasury bills and deposits with the Royal Bank of Canada (collectively, the "RBC Deposits") in the aggregate amount of C$659,974 (the "RBC Interest").
>
> 7. The RBC Interest was included as interest income in determining the Barbados tax liability of CICI for the 1996 CICI Taxation Year. The Barbados Department of Inland Revenue issued an assessment of the 1996 CICI Taxation Year on September 12, 1997, charging the RBC Interest to tax in Barbados
>
> 8. The RBC Interest was not included as foreign accrual property income ("FAPI"), as that term is defined in subsection 95(1) of the *Act*, in the tax return filed by CanVideo for the Taxation Year. There is no suggestion of fraud, wilful default or neglect on the part of CanVideo in not including the RBC Interest as FAPI in its tax return for the Taxation Year.
>
> 9. On December 18, 1997, the Minister of National Revenue (the "Minister") issued to CanVideo an original notice of assessment for the Taxation Year on the basis that the RBC Interest was not included as FAPI, pursuant to

subsection 91(1) of the *Act*, in determining CanVideo's tax liability for the Taxation Year.

10. The normal reassessment period for the Taxation Year, as defined in subsection 152(3.1) of the *Act*, was four years from the date of the original notice of assessment and therefore ended on December 18, 2001.

11. Prior to the expiry of the normal reassessment period of the Taxation Year, the Minister requested a waiver of the limitation periods under the *Act* relating to a number of issues concerning the Taxation Year, including in respect of FAPI earned by CFA of CanVideo. On November 9, 2001, GCL delivered such a waiver to the Minister in respect of CanVideo that allowed the Minister a continuation of its review of the Taxation Year.

12. On August 16, 2004, the Minister issued to GCL a notice of reassessment in respect of CanVideo for the Taxation Year (the "Reassessment"). In the Reassessment, the Minister increased the tax base of CanVideo for the Taxation Year to include the amount of C$659,974 attributable to the RBC Interest earned by CICI in its 1996 CICI Taxation Year, which the Minister characterized as FAPI under subsection 91(1) of the *Act*. As a result of the delivery of the waiver, the Reassessment was issued prior to the expiry of the limitation periods under the *Act* but beyond the limitation period set out in *Article* XXVII of the *Treaty*.

…

14. The *Treaty* was signed on January 22, 1980 by representatives of the Governments of Canada and Barbados. The *Treaty* is generally patterned on the 1977 Model Double Taxation Convention prepared by the Organisation for Economic Co-operation and Development (the "OECD") (the "OECD Model Convention").

…

17. There have been no public or published statements by the Government of Canada or the Government of Barbados, or in each case by any agency, department or similar subdivision thereof, with respect to the interaction between paragraph 3 of *Article* XXVII and paragraph 2 of *Article* XXX. There has been no exchange of diplomatic notes between the Government of Canada and the Government of Barbados with respect to the interaction between paragraph 3 of *Article* XXVII and paragraph 2 of *Article* XXX. Canada is not aware of any documentation, internal directives or other written material that demonstrate that one of the purposes of paragraph 2 of *Article* XXX of the *Treaty* is to overcome the limitation period in paragraph 3 of *Article* XXVII. Canada is not aware of any documentation, internal

directives or other written material that demonstrate that one of the purposes of paragraph 3 of *Article* XXVII of the *Treaty* is to overcome the effect of paragraph 2 of *Article* XXX.

…

21. Barbados tax law does not have regime analogous to the FAPI regime described in subsections 91(1) and 95(1) of the *Act*. Canada has entered into tax treaties with approximately 14 countries that have a FAPI regime. Most of those treaties have a provision analogous to paragraph 2 of *Article* XXX of the *Treaty*, approximately half of those treaties have no provision analogous to paragraph 3 of *Article* XXVII of the *Treaty*, approximately one quarter of those treaties have a provision analogous to paragraph 3 of *Article* XXVII of the *Treaty*, and approximately one quarter of those treaties have a limitation provision that is restricted to *Article* IX of the *Treaty* (Association Enterprises, sometimes described as Related Persons).

…

25. Pursuant to subsection 91(1) of the *Act*, items of income qualifying as FAPI that are earned by a CFA in a particular taxation year of the CFA are added to the tax base of the Canadian resident in the taxation year of the Canadian resident in which the particular taxation year of the CFA ends.

[5] The Respondent also called Mr. Ross John Kauffman, a senior advisor on tax treaties with the Canada Revenue Agency. Over the last ten years he was involved in negotiating 20 treaties, all of which had a provision similar to, or broader than, *Article* XXX(2) of the *Treaty* (the FAPI provision). He explained that the reason for including such a provision in the treaties he negotiated was to preserve or ensure Canada's right to "get at" FAPI. With respect to *Article* XXVII(3) his understanding was that this was a relieving provision, setting a maximum time limit within which either state would be required to adjust the taxpayer's income. Mr. Kauffman testified that his experience was this type of provision was driven by transfer pricing cases and by concerns over records not being available from too many years gone by.

Appellant's position

[6] The Appellant argues that the two *Articles* can live in harmony, as one deals with Canada's jurisdiction to tax, while the other is a procedural limitation provision only. They can be read cohesively, enabling the Minister to assess FAPI

giving effect to *Article* XXX(2) but only within the *Article* XXVII(3) limitation. In other words, *Article* XXVII(3), as a clear procedural provision, does not prevent the taxation of FAPI.

Respondent's position

[7] The Respondent argues that the words of *Article* XXX are clear and that *Article* XXVII(3) is a provision in the *Treaty* that can be construed so as to prevent Canada from taxing FAPI. In this case, it is therefore in order for the Minister to not construe *Article* XXVII(3) in that fashion by giving *Article* XXX paramountcy. As an alternative argument, the Respondent falls back on the implied exception principle of statutory interpretation that the specific overrides the general, arguing that the FAPI provision is a specific provision overriding the general limitation period provision.

Analysis

[8] Both sides agree that, in line with the Supreme Court of Canada decision in *The Queen v. Crown Forest Industries Limited et al.*,[1] it is essential in interpreting a treaty to look to the language used and the intention of the parties.

Language used

[9] The Respondent's position is simple – the words "Nothing in this Agreement shall be construed so as to prevent Canada" from taxing FAPI could not be clearer. *Article* XXVII(3), as a limitation provision, can be construed to prevent Canada from taxing FAPI in certain circumstances. This case is one of those circumstances. The Respondent sees no ambiguity in the wording of either *Article*.

[10] The Appellant scrutinizes the expression "construed so as to prevent" in some detail, arguing that limiting the application of a rule to five years is fundamentally different from preventing the application of a rule. The Appellant contends that even beyond the five-year period, *Article* XXVII(3) does not prevent taxation by Canada of FAPI, but simply narrows the items that may be included in income to those that have not been subjected to tax in Barbados, those in respect of which there has been fraud, neglect or wilful default, and those that have been included in income within the five years and assessed. In effect, Canada's right to tax FAPI is not prevented. I find this argument persuasive.

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[1] 95 DTC 5389.

[11] "Prevent" implies a total prohibition of something before it occurs. The Oxford English Dictionary defines "prevent":

> To stop, keep, or hinder (a person or other agent) from doing something (7); To provide beforehand against the occurrence of (something); to render (an act or event) impracticable or impossible by anticipatory action; to preclude, stop, hinder (8).

Justice Kerr in *Abbott Laboratories, Limited v. The Queen*[2] gave the following definitions:[3]

> … Various dictionary definitions were referred to, including the following:
>
> Prevent
>
> > … To prevent is to stop something effectually by forestalling action and rendering it impossible. *(Random House Dictionary of the English Language*, 1966).
> >
> > … 7. To use preventive measures. *(The Shorter Oxford English Dictionary*, Third Edition, 1956).
>
> Prevention
>
> > … the action of keeping from happening or of rendering impossible an anticipated event or an intended act; a means of prevention; (*The Shorter Oxford English Dictionary*, Vol. 1, 3rd ed., 1944, reprinted in 1947).
> >
> > The act of preventing; effectual hindrance. (*Random House Dictionary of the English Language*, 1966).

[12] This degree of a permanent cessation or forestalling is not what *Article* XXVII(3) does. I regard *Article* XXVII(3) as providing that Canada can tax FAPI as a Canadian resident, except after five years if FAPI has been charged to tax in Barbados. In effect, Canada is not "prevented" from imposing tax by *Article* XXVII(3); it is precluded from imposing tax by it own actions of not imposing tax on a timely basis.

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2 [1971] C.T.C. 26 (Ex. Ct.)

3 at pages 37 and 38.

[13] I find further support for this view of the interplay between the two *Articles* by considering the use of the term "shall be construed so as to". These words must mean something: *Article* XXVII(3) does not read simply, "nothing in this agreement shall prevent". These additional words are inserted for a reason. Why? The logical explanation is because there may be provisions which are open to construction – they need interpretation one way or another. Nothing in *Article* XXVII(3) requires interpretation: it is a straightforward limitation provision – no construction necessary (unlike *Articles* VII and XX which I will consider later in reviewing the intent of *Articles* XXVII and XXX).

[14] Simply based on the language of the *Articles*:

(i) Does *Article* XXVII(3), on any construction, prevent Canada from taxing a Canadian resident on its FAPI? No.

(ii) Specifically, does *Article* XXVII(3) prevent Canada from taxing the Appellant on its FAPI? No. Canada can tax Canwest on its FAPI.

(iii) Even more specifically, does *Article* XXVII(3) prevent Canada from taxing Canwest on its FAPI after the five-year limitation? No, in certain circumstances Canada could still tax Canwest on its FAPI; and

(iv) Finally, does *Article XXVII*(3) prevent Canada from taxing Canwest after the five-year limitation period on FAPI charged to tax in Barbados? Yes, says the Respondent, so *Article* XXX(2) requires that *Article* XXVII(3) not be construed that way.

This is illogical, as there is no other way to construe *Article* XXVII(3). What the Respondent is really saying is that *Article* XXVII(3) be ignored, not that *Article* XXVII(3) be construed in a different way consistent with *Article* XXX(2). It is to be "construed" as though it does not exist; that is, that there simply is no limitation on FAPI. That is not a construction: that is a destruction. All to say, by its use of "construe", I find *Article* XXX is not directed at *Article* XXVII(3).

[15] It is clear to me that *Article* XXX, in addressing "nothing in this Agreement shall be construed so as to prevent" is directing the reader to consider the wording of other *Articles* in the *Treaty*, not the specific facts of a specific taxpayer. Just look at the other *Articles* and on their face do they prevent Canada from taxing FAPI; not a question of do they prevent Canada from taxing FAPI in certain specific situations. Does any part of the *Treaty* effectively strike down Canada's

authority to tax FAPI? That is what the words imply to me. In that context, a limitation provision cannot be read to deprive Canada of that authority. Certainly the language of *Article* XXVII(3) does not except FAPI out of its application, as it does for situations of fraud, neglect or wilful default.

Intention

[16] I am reinforced in my interpretation of the language of the two *Articles* by my findings as to the intent of the *Articles*. While there is no direct evidence from anyone engaged in the negotiating of the *Canada-Barbados Treaty*, some guidance was offered by Mr. Kauffman as to the rationale behind both *Articles*. With respect to *Article* XXVII(3), he suggested that this type of limitation provision avoids the problem of having to rely on competent authority provisions to make relieving adjustments long after records may have been lost or destroyed. I also accept the Appellant's position that limitation provisions of this sort do provide taxpayers some certainty. There was no evidence to suggest the provision was inserted for any reason related to specifically curtailing Canada's ability to tax FAPI arising in Barbados.

[17] It is the intention behind *Article* XXX(2) that is of greater import. The Respondent argues that the intention is clearly gleaned from the words, and where the words are clear, it is inappropriate to rely on extrinsic sources to determine intention. The Appellant argues that the correct interpretation of *Article* XXX(2) revolves around a determination that the intention of the negotiators in inserting this provision was to remove any uncertainty regarding Canada's right to tax FAPI. This intention can be readily ascertained from a review of other provisions in the *Treaty* and also from consideration of extrinsic sources, such as academics' opinions, the OECD Model Tax Convention and case law. Given that the Crown introduced Mr. Kauffman's evidence that similar provisions were written into other treaties to basically preserve Canada's right to "get at" FAPI, and given that the wording of *Article* XXX did require some considerable probing, I am prepared to consider the sources just mentioned in confirming the intention of the *Articles*.

[18] Before considering those sources, I shall consider just the *Treaty* itself in determining intention. The language of *Article* XXX(2) implies that there may be other *Articles* in the *Treaty* whose meaning is open to an interpretation of preventing Canada from taxing FAPI. So, are there such *Articles*? The Appellant's counsel referred to *Articles* VII(1) and X(5) of the *Treaty*.

[19] *Article* VII states:

> The profits of an enterprise of a Contracting State [defined in *Article* III(1) as an enterprise carried on by a resident of a Contracting State] shall be taxable only in that State unless the enterprise carries on or has carried on business in the other Contracting State through a permanent establishment situated therein.

It is not difficult to see how this provision could be construed to prevent Canada taxing profits of a CFA, unless the CFA has a permanent establishment in Canada. Another interpretation is that the CFA's profits are simply notionally attributed to the Canadian parent and, therefore, not within the "profits" referred to in *Article* VII.

[20] *Article* X(5) states:

> Where a company is a resident of only one Contracting State, the other Contracting State may not impose any tax on the dividends paid by the company to persons who are not residents of that other State, or subject the company to a tax on undistributed profits, even if the dividends paid or the undistributed profits consist wholly or partly of profits or income arising in such other State.

This provision too could be interpreted as preventing Canada from taxing FAPI, since such taxation could in substance be considered to be the imposition of tax on the undistributed profits of a resident in Barbados. Again, another interpretation would be that the *Article* does not prevent the taxation of FAPI, because the FAPI regime seeks to tax the Canadian parent and imposes such tax on a notional amount attributed to the Canadian parent, rather than directly on the undistributed profits of the CFA.

[21] I conclude, that within the *Treaty* itself, there are uncertainties as to Canada's right to tax FAPI that could justify the need for *Article* XXX to, as Mr. Kauffman put it, ensure Canada can get at FAPI.

[22] This issue appears to have been addressed by the 2002 *Update to the OECD Model Tax Convention*:

> Thus, whilst some countries have felt it useful to expressly clarify, in their conventions, that controlled foreign companies legislation did not conflict with the Convention, such clarification is not necessary. It is recognised that controlled foreign companies legislation structured in this way is not contrary to the provisions of the Convention.

Clearly, Canada was one of the countries that expressly clarified that the *Treaty* was not to be in conflict with domestic FAPI legislation. As Professor Brian

Arnold indicated in "*Tax Treaties and Tax Avoidance: The 2003 Revisions to the Commentary to the OECD Model*":

> Before the 2003 changes, the Commentary to the OECD Model was unclear and unsatisfactory in its treatment of the relationship between CFC rules and tax treaties.

[23] The Courts have also had to deal with the issue of a country's authority to tax controlled foreign companies' (CFC) income. The Appellant referred to the French case of *Re Société Schneider Electric*[4] and the Finnish case of *Re A Oyj Abp*.[5] Both cases dealt with treaties with *Articles* similar to *Article* VII of the *Canada-Barbados Treaty*. The French Conseil d'État held that France's CFC legislation was not compatible with the *France/Switzerland Treaty*. The Finnish Supreme Administrative Court held profits of a Belgium subsidiary did fall within Finland's CFC regime and that *Article* VII of the *Belgium-Finland Treaty* did not prevent Finland from imposing such taxes. Neither treaty had the equivalent of *Article* XXX of the *Canada-Barbados Treaty*. While these cases are both long after the *Canada-Barbados Treaty* was negotiated, they confirm some degree of uncertainty of a treaty's impact on CFC legislation, barring a clarifying provision such as *Article* XXX.

[24] The Appellant also referred to statements of Professor Dr. Michael Lang. In "*CFC Regulations and Double Taxation Treaties"*, Professor Lang wrote:

> In many countries, the issue of the compatibility of the CFC regulations with treaty law is far from settled. In many cases, there are no supreme court decisions on the issue. Most of the opinions mentioned in the 1987 OECD report and the 1992 Commentaries to the OECD Model represent the views of tax administrations of OECD countries. These views by no means reflect the current conclusions of other experts or the latest case law.
>
> …
>
> Tax treaties have a limiting effect on national taxation regimes. Therefore, in the absence of any arguments to the contrary, one may not assume that tax treaties will have no impact on inconsistent CFC regulations.

Also, Renata Fontana in a paper called "*The Uncertain Future of CFC Regimes in the Member States of the European Union – Part I*", stated:

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4 4 ITRL 1077.

5 4 ITRL 1009.

> The application of tax treaties to CFC regimes and their compatibility is neither a recent nor a settled debate. Rather, this is still a disputed issue in the national courts of the various states involved, with divergent decisions on the issues.
>
> …
>
> Although scholars, domestic (administrative and judicial) courts and the OECD itself have continuously addressed the issue of the compatibility between CFC regimes and tax treaties, no uniform and definitive solution has been found to date.

I appreciate that academics' comments, statements concerning the OECD and pronouncements by French and Finnish Courts do not constitute any direct evidence of the Canadian and Barbadian negotiators' true intent, but these sources do present a useful background. Combined with Mr. Kauffman's testimony of Canada's position with respect to other treaties on these particular provisions, and with the very wording of *Article* XXX, these extrinsic sources confirm my conclusion that *Article* XXX was intended to ensure no other *Article* takes away Canada's authority to impose tax on FAPI of a Barbadian resident. There is no evidence to suggest anything contrary. In that light, is the limitation provision, *Article* XXVII(3) incompatible with that intention? I find it is not. Indeed, as I indicated earlier, if anything, it supports Canada's right to tax FAPI. I accept the Appellant's position that *Article* XXX(2) goes to Canada's very jurisdiction to tax, while *Article* XXVII is simply a clear procedural provision.

[25] Based on both the language used in the *Treaty* itself, and the intent of *Articles* XXVII(3) and XXX(2), I am satisfied that *Article* XXX(2) is not to be interpreted as overriding *Article* XXVII(3) rendering the limitation meaningless. The five-year limitation is in play and the Respondent has, in this case, missed that limitation. I therefore allow the appeal and vacate the reassessment of August 16, 2004 as it was made beyond the *Treaty* maximum reassessment period. Costs to the Appellant.

Signed at Ottawa, Canada, this 24th day of October, 2006.

"Campbell J. Miller"

Miller J.

CITATION:	2006TCC579
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