Dockets: 2004-2006(IT)G
2004-4226(IT)G

BETWEEN:

PRÉVOST CAR INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeals heard on September 4, 5, 6 and 7, 2007 at Toronto, Ontario.

Before: The Honourable Gerald J. Rip, Associate Chief Justice

Appearances:

Counsel for the Appellant:	William I. Innes, Chia-yi Chua, Matthew Peters
Counsel for the Respondent:	Roger Leclaire, Ifeanyi Nwachukwu, Daniel Bourgeois

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AMENDED JUDGMENT

The Judgment and Reasons for Judgment are issued in substitution for the Judgment and Reasons for Judgment signed on April 22, 2008.

The appeals from assessments made under Part XIII of the *Income Tax Act*, notices of which are dated July 13, 2000, August 29, 2001 and April 15, 2004, are allowed with costs and the assessments are vacated. Counsel may be heard concerning questions on costs.

Signed at Ottawa, Canada, this 30th day of April 2008.

"Gerald J. Rip"

Rip A.C.J.

Citation: 2008TCC231
Date: 20080422
Dockets: 2004-2006(IT)G
2004-4226(IT)G

BETWEEN:

PRÉVOST CAR INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

AMENDED REASONS FOR JUDGMENT

Rip, A.C.J.

[1] The issue in these appeals by Prévost Car Inc. ("Prévost"), is to determine who was the beneficial owner of dividends paid by Prévost in 1996, 1997, 1998, 1999 and 2001. The term "beneficial owner" is found in Article 10, paragraph 2 of the Canada-Netherlands Tax Treaty ("Tax Treaty").[1] Prévost is a resident Canadian corporation who declared and paid dividends to its shareholder Prévost Holding B.V. ("PHB.V."), a corporation resident in the Netherlands. The Minister of National Revenue ("Minister") issued assessments under Part XIII of the *Income Tax Act* ("*Act*") against Prévost, notices which are dated July 13, 2000, August 29, 2001 and April 15, 2004, in respect of the aforementioned dividends.[2] The Minister assessed on the basis that the beneficial owners of the dividends were the corporate shareholders of PHB.V., a resident of the United Kingdom and a resident of

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1 *Convention Between Canada and the Kingdom of the Netherlands for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income*.

2 Four notices of assessment are dated July 13, 2000 and one notice is dated August 29, 2001 and were in respect of dividends paid in 1996, 1997, 1998, 1999 and 2001 respectively. Three notices of assessment dated April 15, 2004 are in respect of dividends paid in 1998, 1999 and 2001. The appellant filed two notices of appeal, the first is in respect of assessments issued in 2000 and 2001 and the second is in respect of assessments issued in 2004.

Sweden, and not PHB.V. itself. When Prévost paid the dividends it withheld tax by virtue of subsections 212(1) and 215(1) of the *Act*. According to Article 10 of the Tax Treaty, the rate of withholding tax was five percent.[3]

[2] In her replies to the notices of appeal the respondent stated that pursuant to subsection 215(1) of the *Act*, the appellant was required to withhold and remit to the Crown 25 percent of the dividends paid to PHB.V. but, she adds, facetiously, I might add, "fortunately for the appellant, the Minister applied the reduced rates of taxation of 15 and 10% from the *Canada-Sweden Tax Treaty* and *Canada-U.K. Tax Treaty* respectively to the dividends paid even though the treaties had no application".

Facts

[3] The appellant was incorporated under the laws of Quebec and is resident of Canada. It manufactures buses and related products in Quebec and has parts and services facilities throughout North America. On or about May 3, 1995 the appellant's erstwhile shareholders agreed to sell their shares of the appellant to Volvo Bus Corporation (also known as Volvo Bussar A.B. and referred to in these reasons as "Volvo"), a resident of Sweden and Henlys Group PLC ("Henlys"), a resident of the United Kingdom. Volvo and Henlys were parties to a Shareholders' and Subscription Agreement ("Shareholders' Agreement") dated May 3, 1995, under which Volvo undertook to incorporate a Netherlands resident company and subsequently transfer to the Dutch Company all of the shares Volvo acquired in Prévost; the shares of the Netherlands company would be owned as to 51 percent by Volvo and 49 percent by Henlys. The transfer of Prévost shares to Henlys would take place after Henlys had secured funding for its share of the purchase.

[4] On or about June 12, 1995, the agreements of May 3, 1995 were carried out: Volvo transferred all of the issued and outstanding shares in Prévost to PHB.V. Shares of PHB.V. were transferred by Volvo to Henlys so that the issued and outstanding shares of PHB.V. were owned by Volvo as to 51 percent (51 Class "A" shares) and Henlys as to 49 percent (49 Class "B" shares).

[5] The relevant corporate structure was:

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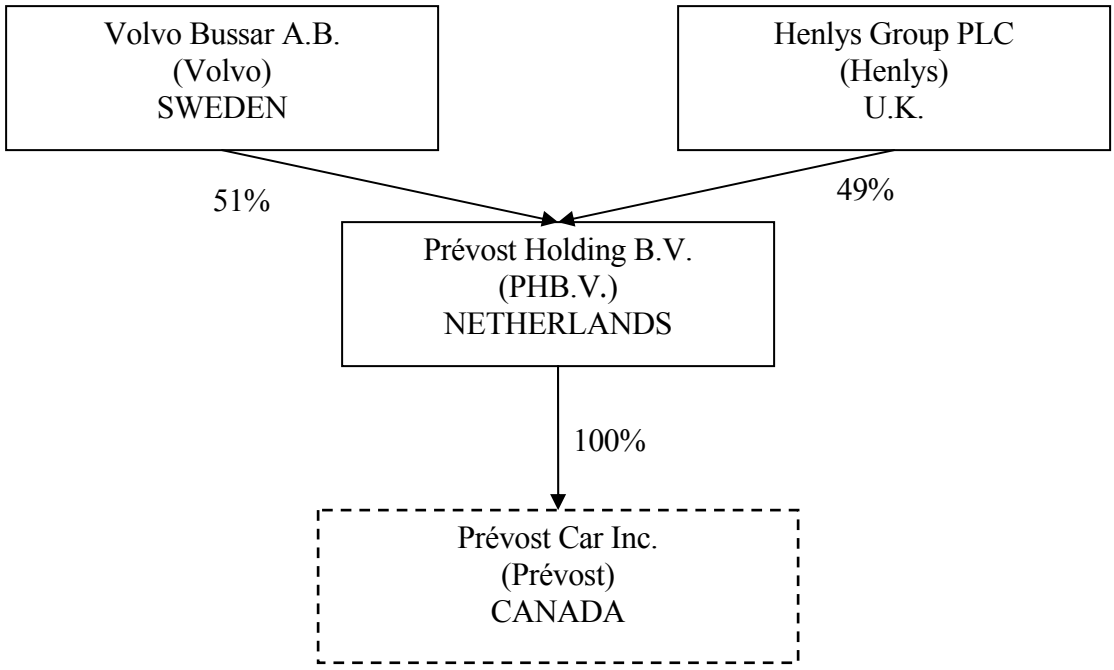
[3] Six percent for 1996.



[6] Volvo and Henlys were both engaged in the manufacture of buses, Volvo manufacturing the chassis and Henlys, the bus body. Prévost was in the same business, building coaches for different types of buses and bus body shells. Mr. Tore Backstrom, Senior Vice-President for North and South America for Volvo Bus Operations, described a body shell as a coach without any seats but may have other facilities, such as expendable side walls and may be convertible into a motor home or coach for entertainers on tour, for example.

[7] In the early 1990s Volvo learned that the erstwhile shareholders of Prévost were prepared to sell their shares. At the time Volvo and Henlys were seeking to expand their markets to North America and decided to acquire Prévost through a holding company.

[8] Mr. Backstrom declared that the reason Volvo and Henlys formed a holding company was that both Henlys and Volvo were involved in two different aspects of bus construction, body and chassis, and "we saw in front of us a clear avenue whereby the corporation should be enlarged further to encompass other operations and to have a holding company . . . where we share our knowledge". He added that where Volvo purchases all the shares of a company, it "very often" does not use a holding company.

[9] The reason for choosing a Dutch holding company was very simple, according to Mr. Backstrom. Tax was a consideration, but not an overriding

consideration. He explained that Henlys did not want a Swedish company and Volvo did not want an English company. Both wanted a company resident in Europe where they have "a set-up" for that type of activity that is not too expensive and where business could be conducted in English. The choices were Switzerland, Luxembourg, Belgium and Holland, the latter being "very neutral".

[10] However, the office of Arthur Anderson & Co. in Rotterdam had recommended that in order to avoid tax claims from the United Kingdom or Sweden, and other international tax issues, the effective management and control of PHB.V. be located in the Netherlands.

[11] Mr. Backstrom also testified that PHB.V. was established as a vehicle for Henlys and Volvo to pursue multiple North American projects. The first of these projects was Prévost. The second was to be a Mexican company, Masa. The original intention was for Henlys to participate in the purchase and that PHB.V. would hold the Masa's shares. However, by this time, Henlys was in financial difficulty. Henlys had the option "for some years" to join Volvo in the Mexican venture but, in the end, did not do so. In fact, said Mr. Backstrom, Henlys is in "liquidation and . . . does not exist anymore".

[12] The Shareholders' Agreement also provided, among other things, that not less than 80 percent of the profits of the appellant and PHB.V. and their subsidiaries, if any, (together called the "Corporate Group") were to be distributed to the shareholders. The distribution of the profits was subject to the Corporate Group having sufficient financial resources to meet its normal and foreseeable working capital requirements at the time of payment unless the shareholders otherwise agreed. Amounts were to be distributed by way of dividend, return of capital or loan. The distribution for a fiscal year was to be declared and paid to shareholders "as soon as practicable" after the end of the fiscal year. The Board of Directors of PHB.V. was to take reasonable steps to "procure" that dividends or other payments are declared by the appellant or other steps are taken to enable PHB.V. to make payments of dividends or return of capital or that any monies loaned by shareholders are repaid.

[13] The directors of Prévost were directors of PHB.V. Directors of Prévost frequently discussed PHB.V.'s affairs as well, including future declarations and payments of dividends.

[14] The amounts of dividends in question were paid by the appellant to PHB.V. and then distributed by PHB.V. to Volvo and Henlys in accordance with the Shareholders' Agreement.

[15] At a meeting on November 27, 1995, the directors of Prévost confirmed that the dividend for 1996 would be at least 80 percent of after tax profit and agreed that a "procedure will be written to determine how this will work". At a meeting on March 23, 1996, the purported shareholders of Prévost agreed to a dividend policy "that following the completion of accounts for each quarter, and subject to adequate working and investment capital being available to the company, a dividend of 80 percent of the net retained profit after tax should be paid by the end of the following quarter". At a meeting following the end of each financial year the directors of Prévost also were to consider whether more than 80 percent of the retained profit for the period be paid out as a dividend. On March 23, 1996 the shareholders met and agreed that a dividend representing 80 percent of the retained earnings for the period June 7, 1995 to December 31, 1995 be paid by April 30, 1996.

[16] There is a reason that I referred to Prévost's "purported shareholders" in the immediately preceding paragraph. The minutes of the meeting of shareholders of Prévost held on March 23, 1996 record that the shareholders attending the meeting are proxies for Volvo and Henlys. At the time, however, Prévost had only one shareholder, PHB.V. An identical error appears in a resolution of shareholders of Prévost dated August 15, 1996, signed by Volvo and Henlys. This is at least sloppy maintenance of corporate records but also could be an indication of something more significant. Minutes of a meeting of shareholders of Prévost held on May 9, 2002 however do state that the shareholder of Prévost is PHB.V.

[17] The English translation of the Deed of Incorporation of PHB.V. is headed "Incorporation of the Private Closed Company with Limited Liability Prévost Holding B.V." and is dated June 12, 1995. Article 24 of the Deed describes how profits are to be allocated and refers to the Shareholders' Agreement:

> 1. The management board shall be authorized to, with due observance of what has been agreed in the shareholders' agreement, reserve part of the accrued profits.
>
> 2. The profits remaining after the reservation referred to in paragraph 1 of this article shall be at the disposal of the general meeting.

3. Dividends may be paid only up to an amount which does not exceed the amount of the distributable part of the net assets.

4. Dividends shall be paid after adoption of the annual accounts from which it appears that payment of dividends is permissible.

5. The management board, may subject to due observance of paragraph 3, resolve to pay an interim dividend.

6. The general meeting may, subject to due observance of paragraph 3, and after approval of the management board resolve to make payments to the charge of any reserve which need not be maintained by virtue of the law.

7. A claim of a shareholder for payment of dividend shall be barred after five years have elapsed.

[18] The Joint Book of Documents contains copies of resolutions of the Board of Managing Directors of PHB.V. declaring dividends to its shareholders, Volvo and Henlys. However, there is only one resolution of the Board of Directors of Prévost in the Joint Book that records the declaration of a dividend; that resolution, dated December 30, 1996, records a dividend of $9,000,000 payable during the first quarter of 1997. There is also evidence that some monies were paid to PHB.V. before dividends were declared by Prévost's directors. However, on examination for discovery Cindy Kalb, an official of the Canada Revenue Agency, acknowledged that the respondent does not dispute that the dividends in question were properly declared by the appellant and paid to PHB.V.

[19] On February 27, 1996 Mr. Brian Chivers, Finance Director of Henlys, wrote to Volvo stressing the importance that Volvo and Henlys agree to a regular dividend stream before the next directors meeting of Prévost. Henlys was always pressing for quick payment of dividends since it required money to service the loan it undertook to finance its purchase of Prévost or, more accurately, its purchase of PHB.V. In one instance $5,684,523 was transferred to Henlys on fax instructions by Mr. Chivers without a resolution of the managing directors of PHB.V. having been signed.

[20] Ms. Lyne Bissonnette, Chief of Treasury at Prévost was (and is) responsible for accounting and financial matters at Prévost. She described how money was usually paid by Prévost to PHB.V. She recalled that Prévost's Chief Financial Officer or its Vice-President, Finance, would inform her of any dividend declared by Prévost's directors. Usually Mr. Chivers would have been pressing for payment. Ms. Bissonnette would receive a fax instructing her to whom she should make

payment. She would verify the amounts and then inform Volvo and Henlys of the amount of money being transferred.

[21] On April 2, 1996, a week after Prévost's purported shareholders adopted its dividend policy at its March 23, 1996 meeting, Mr. Chivers wrote to Prévost setting out the dividend policy and asking for the payment of a dividend for the period June 7 to December 31, 1995. Mr. Chivers advised Prévost of the amount of the dividend, being 80 percent of profit and instructed Prévost to pay the dividend to PHB.V. once he advises Prévost of PHB.V.'s bank account. On April 15th he set out the details of PHB.V.'s Canada dollar bank account. Two days later Ms. Bissonnette sent a memo to Mr. Chivers and a Mr. Hiller at Volvo detailing the amount of the dividend, the amount of the withholding tax at six percent, and that the net dividend "was wired" to the Banque Nationale du Canada.

[22] The Banque Nationale du Canada then transferred the amount of net dividend to Citco Bank Netherlands PHB.V., PHB.V.'s banker in Amsterdam. The actual dividend was declared after Prévost had advanced the amount equal to the proposed dividend, less withholding tax, to PHB.V. It was expected that the recipient would get payment within 24 hours.

[23] There were 11 dividends paid by Prévost that are subject to the assessments under appeal. The payment of the dividends would be processed in a manner similar to that described in the immediately preceding paragraphs, although there were also payments made after an interim dividend was declared.[4]

[24] At all relevant times PHB.V.'s registered office was in the offices of Trent International Management PHB.V. ("TIM"), originally in Rotterdam and later in Amsterdam. TIM was affiliated with PHB.V.'s banker, Citco Bank. In March 1996 the directors of PHB.V. executed a Power of Attorney in favour of TIM to allow it to transact business on a limited scale on behalf of PHB.V. There is no evidence what this "limited" business included. Later, on December 1996, PHB.V. executed another Power of Attorney in favour of TIM to allow it to arrange for the execution of payment orders in respect of interim dividend payments to be made to PHB.V.'s shareholders.

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[4] It is my understanding that under Dutch corporate law, Articles of Incorporation may permit the managing directors to declare an interim dividend which is later confirmed by the shareholders as a final dividend. See Evidence of Professor Raas, para. 48(c).

[25] During the years in appeal, PHB.V. had no employees in the Netherlands nor does it appear it had any investments other than the shares in Prévost.

[26] From time to time PHB.V. had to provide "Know Your Client" documentation to its banker. According to this documentation PHB.V. represented that the beneficial owners of the shares of Prévost were by Volvo and Henlys, not PHB.V. itself. The appellant states that the "Know Your Client" policies concerned anti-money laundering and bank regulatory issues and were intended to determine who was ultimately "behind the funds" in an account.

Treaty & OECD Model Conventions

[27] The appellant withheld tax of (six and) five percent on the payment of the dividends to PHB.V., relying on paragraphs 1 and 2 of Article 10 of the Tax Treaty. From July 30, 1994 to January 14, 1999, the relevant portions of Articles 10(1) and (2) of the Tax Treaty read as follows:

1. Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State.	1. Les dividendes payés par une société qui est un résident d'un État contractant à un résident de l'autre État contractant sont imposables dans cet autre État.
2. However, such dividends may also be taxed in the State of which the company paying the dividends is a resident, and according to the laws of that State, but if the recipient is the beneficial owner of the dividends the tax so charged shall not exceed:	2. Toutefois, ces dividendes sont aussi imposables dans l'État dont la société qui paie les dividendes est un résident et selon la législation de cet État, mais si la personne qui reçoit les dividendes en est le bénéficiaire effectif, l'impôt ainsi établi ne peut excéder :
a) 5 per cent of the gross amount of the dividends if the beneficial owner is a company (other than a partnership), that holds directly or indirectly at least 25 per cent of the capital or at least 10 per cent of the voting power of the company paying the dividends;	*a*) 5 pour cent du montant brut des dividendes si le bénéficiaire effectif est une société (autre qu'une société de personnes) qui détient directement ou indirectement au moins 25 pour cent du capital ou au moins 10 pour cent des droits de vote de la société qui paie les

	dividendes;
. . .	[…]
c) 15 per cent of the gross amount of the dividends in all other cases.	*c*) 15 pour cent du montant brut des dividendes, dans tous les autres cas.

[28] Subparagraph (*a*) of paragraph 2 of Article 10 of the Tax Treaty was replaced effective January 15, 1999 as follows:

a) 5 per cent of the gross amount of the dividends if the beneficial owner is a company (other than a partnership) that owns at least 25 per cent of the capital of, or that controls directly or indirectly at least 10 per cent of the voting power in, the company paying the dividends;	*a*) 5 pour cent du montant brut des dividendes si le bénéficiaire effectif est une société (autre qu'une société de personnes) qui détient au moins 25 pour cent du capital de la société qui paie les dividendes, ou qui contrôle directement ou indirectement au moins 10 pour cent des droits de vote dans cette société;
. . .	[…]

[29] The Tax Treaty is based on the Organization for Economic Cooperation and Development ("OECD") Model Tax Convention on Income and on Capital 1977 ("Model Convention"). Paragraph 1 and the opening words of paragraph 2 of Articles 10 of the Model Convention and the Tax Treaty are identical except for the word "Contracting" describing the word "State" in Article 10(2) of the 1977 Model Convention.[5] The subparagraphs of paragraph 2 differ. However, the subparagraphs have no bearing on these reasons.[6]

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[5] Article 10(2) of the Model Convention was amended in 1995. See para. 33 of these reasons.

[6]

a) 5 per cent of the gross amount of the dividends if the beneficial owner is a company (other than a partnership), that holds directly at least 25 per cent of the capital of the company paying the dividends;	*a*) 5 pour cent du montant brut des dividendes si le bénéficiaire effectif est une société (autre qu'une société de personnes) qui détient directement au moins 25 pour cent du capital de la société qui paie les dividendes;
b) 15 per cent of the gross amount of the dividends in all other cases.	*b*) 15 pour cent du montant brut des dividendes, dans tous les autres cas.

[30] Paragraphs 2 of Article 10 of the Model Convention and the Tax Treaty require that the recipient of dividends be the "beneficial owner" or, in French, "le bénéficiaire effectif" of the dividends. The words used for "beneficial owner" and "le bénéficiaire effectif" in the Dutch version of the Treaty is ***uiteindelijk gerechtigde***. These words are defined neither in the Model Convention nor in the Tax Treaty. The French version of the *Act* generally uses the words "propriétaire effectif" or "personne ayant la propriété effective" for "beneficial owner".[7]

[31] The Commentary on Article 10 of the 1977 OECD Model Convention states that:

> 12. Under paragraph 2, the limitation of tax in the State of source is not available when an intermediary, such as an agent or nominee, is interposed between the beneficiary and the payer, unless the beneficial owner is a resident of the other Contracting State. States which wish to make this more explicit are free to do so during bilateral negotiations.

Canada has not undertaken any negotiations with the Netherlands to make paragraph 2 of Article 10 of the Tax Treaty any more explicit.

[32] In 2003 the OECD Commentaries to Article 10 of the OECD Model Convention were modified. Paragraphs 12, 12.1 and 12.2 of the Commentaries explain that the term "beneficial owner in Article 10(2) of the Model Convention" is not used in a narrow technical sense, rather, it would be understood in its context and in light of the object and purposes of the Convention, including avoiding double taxation and the prevention of fiscal evasion and avoidance. With respect to conduit companies, a report from the Committee on Fiscal Affairs concluded "that a conduit company cannot normally be regarded as the beneficial owner if, though the formal owner, it has, as a practical matter, very narrow powers which render it, in relation to the income concerned, a mere fiduciary or administrator acting on account of the interested parties".

[33] In 1995, Article 10, paragraph 2 of the Model Convention, 1977 was amended by replacing the words "if the recipient is the beneficial owner of the dividends" with "if the beneficial owner of the dividends is a resident of the other Contracting State". (There was no change to this wording in the Tax Treaty.) The Commentary was also amended to explain that the Model Convention was amended to clarify the first sentence of the original commentary, above, "which

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[7] See paras. 62-64 *infra*.

has been the consistent position of all Member countries". The second sentence of the Commentary was not altered. The key words, as far as these appeals are concerned, in both the 1977 and 1995 versions of the OECD Model Convention and the Tax Treaty are "beneficial owner" and the equivalent words in the French and Dutch languages.

[34] Article 3(2) of the Tax Treaty provides an approach to understanding undefined terms:

> 2. As regards the application of the Convention by a State any term not defined therein shall, unless the context otherwise requires, have the meaning which it has under the law of that State concerning the taxes to which the Convention applies.
>
> 2. Pour l'application de la Convention par un État, toute expression qui n'y est pas définie a le sens que lui attribue le droit de cet État concernant les impôts auxquels s'applique la Convention, à moins que le contexte n'exige une interprétation différente.

In other words, when Canada wishes to impose our income tax, a term not defined in the Tax Treaty will have the meaning it has under the *Act*, assuming it has a meaning under the *Act*.

[35] The *Income Tax Conventions Interpretation Act*,[8] at section 3, directs how the meaning of undefined terms in a tax treaty are to be understood:

> 3. Notwithstanding the provisions of a convention or the Act giving the convention the force of law in Canada, it is hereby declared that the law of Canada is that, to the extent that a term in the convention is
>
> (*a*) not defined in the convention,
>
> (*b*) not fully defined in the convention, or
>
> (*c*) to be defined by reference to the laws of Canada,
>
> that term has, except to the extent that the context otherwise requires, the
>
> 3. Par dérogation à toute convention ou à la loi lui donnant effet au Canada, le droit au Canada est tel que les expressions appartenant aux catégories ci-dessous s'entendent, sauf indication contraire du contexte, au sens qu'elles ont pour l'application de la *Loi de l'impôt sur le revenu* compte tenu de ses modifications, et non au sens qu'elles avaient pour cette application à la date de la conclusion de la convention ou de sa prise d'effet au Canada si, depuis lors, leur sens pour la même application a changé. Les catégories en question sont:
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> *a*) les expressions non définies dans la

[8] R.S., 1985, c.I-4. Referred to as "*ITCIA*".

meaning it has for the purposes of the *Income Tax Act*, as amended from time to time, and not the meaning it had for the purposes of the *Income Tax Act* on the date the convention was entered into or given the force of law in Canada if, after that date, its meaning for the purposes of the *Income Tax Act* has changed.	convention; *b*) les expressions non définies exhaustivement dans la convention; *c*) les expressions à définir d'après les lois fédérales.
1984, c. 48 s. 3.	1984, ch. 48, art. 3.

[36] The *Vienna Convention on The Law of Treaties* ("*VCLT*"), at Article 31(1), states that:

> A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and are the light of its object and purpose.

[37] Tax treaties are to be given a liberal interpretation with a view of complementing the true intentions of the contracting states.[9] The paramount goal is to find the meaning of the words in question.[10]

[38] Article 3(2) of the OECD Model Convention 1977 is similar to Article 3(2) of the Tax Treaty:

... [A]s regards the application of the Convention by a Contracting State any term not defined therein shall, unless the context otherwise requires, have the meaning which it has under the law of that State concerning the taxes to which the Convention applies.	Pour l'application du présent Accord à un moment donné par un État contractant, tout terme ou expression qui n'y est pas défini a, saut si le contexte exige une interprétation différente, le sens que lui attribue à ce moment le droit de cet État concernant les impôts auxquels s'applique le présent Accord.

[39] In 1999 Article 3(2) of the Model Convention, was amended as follows:

2. As regards the application of the Convention at any time by a Contracting State, any term not defined therein shall, unless the	2. Pour l'application de la Convention à un moment donné par un État contractant, tout terme ou expression qui n'y est pas défini a, sauf si le contexte

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9 *Gladden Estate v. The Queen*, [1985] 1 C.T.C. 163.

10 *Crown Forest Industries v. The Queen*, [1955] S.C.R. 802.

context otherwise requires, have the meaning that it has at that time under the law of that State for the purposes of the taxes to which the Convention applies, any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State.	exige une interprétation différente, le sens que lui attribue, à ce moment, le droit de cet État concernant les impôts auxquels s'applique la Convention, le sens attribué à ce terme ou expression par le droit fiscal de cet État prévalant sur le sens que lui attribuent les autres branches du droit de cet État.

[40] The concept of "beneficial ownership" or "beneficial owner" is not recognized in the civil law of Quebec or other civil law countries who are members of OECD. Paragraph 248(3)(*f*) of the *Act* attempts to harmonize civil law and common law for purposes of the *Act*. Subsection 248(3) states that in applying the *Act* in Quebec usufruct, right of use in habitation and substitution, are deemed in certain circumstances to be a trust. Paragraph (*f*) concludes that:

(*f*) property in relation to which any person has, at any time, (i) the right of ownership, (ii) a right as a lessee in an emphyteutic lease, or (iii) a right as a beneficiary in a trust shall, notwithstanding that such property is subject to a servitude, be deemed to be beneficially owned by the person at that time.	*f*) les biens sur lesquels une personne a, à un moment donné, un droit de propriété, un droit de preneur dans un bail emphytéotique ou un droit de bénéficiaire dans une fiducie sont réputés, même s'ils sont grevés d'une servitude, être la propriété effective de la personne à ce moment.

Expert Evidence

[41] The appellant produced several expert witnesses to explain Dutch law and the development of the OECD Model Conventions and the Commentaries on the Model Conventions.

van Weeghel

[42] Professor Dr. S. van Weeghel was an expert witness for the appellant. He is a Professor of Law and practices taxation law in the Netherlands. At time of trial Professor van Weeghel was a partner in the Amsterdam office of the law firm, Linklaters. He had earlier worked at another law firm, Stibbe, in Amsterdam and New York as Head of Tax, among other positions. He was called to the Amsterdam Bar in 1987. He obtained a LL.M. degree in taxation from New York

University in 1990 and a doctorate from the University of Amsterdam in 2000. He is a tenured professor of tax law at the University of Amsterdam. Professor van Weeghel has lectured at several universities in Europe. He has published numerous articles on European tax matters and tax treaties. He is an expert in Dutch tax treaties, Dutch tax law and abuse of tax treaties.

[43] Professor van Weeghel concluded that under Dutch law PHB.V. is the beneficial owner of Prévost's shares. He relied, in particular, on an interpretation by the *Hoge Raad*[11] (Dutch Supreme Court). In his report Professor van Weeghel described the facts and *ratio* of that case as follows:

> . . . The taxpayer, a stockbroker resident in the United Kingdom, had acquired a number of dividend coupons detached from Royal Dutch shares. At the time of the purchase, the dividends had been declared but not yet paid. The stockbroker had paid approximately 80 per cent of the face value of the coupons. The dividend was paid to the stockbroker, subject to 25 per cent dividend withholding tax – the full statutory rate – which was withheld by the paying agent. Subsequently, the stockbroker filed for a refund of 10 per cent of the gross dividend, based upon Article 10, paragraph 2 of the 1980 Netherlands-United Kingdom tax treaty, which – in relevant part – is substantially similar to Article 10, paragraph 2 of the Convention.
>
> The tax inspector denied the refund and asserted that ownership of the shares was a prerequisite for refund of withholding tax. The *Gerechtshof* – on appeal of the stockbroker – established as a fact that the stockbroker had acquired a number of dividend claims of which the amounts were entirely certain and which would be payable within days from the acquisition. Under those circumstances, the court ruled, the taxpayer did not qualify as the beneficial owner of the dividends.[13]
>
> The *Hoge Raad* reversed the decision of the *Gerechtshof*, deciding as follows . . . [translation by Professor Weeghel]:
>
> > The taxpayer became owner of the dividend coupons as a result of purchase thereof. It can further be assumed that subsequent to the purchase the taxpayer could freely avail of those coupons and, subsequent to the cashing thereof, could freely avail of the distribution, and in cashing the coupons the taxpayer did not act as voluntary agent (*zaakwaarnemer*, SvW) or for the account of the principal (*lasthebber*, SvW). Under those circumstances the taxpayer is the beneficial owner of the dividend. The treaty does not contain the condition that the beneficial owner of the dividend must also be the owner of the shares and further it is irrelevant that the taxpayer purchased the coupons at the time the dividend had already been announced, because the question who is the beneficial owner

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[11] 6 April 1994, BNB 1994/217, sometimes called the "*Royal Dutch*" case.

> must not be answered at the time the dividend is announced, but at the time the dividend is made payable.

Based on the *Hoge Raad's* interpretation, Professor van Weeghel concluded that:

> . . . a clear and simple rule emerges. A person is the beneficial owner of a dividend if i) he is the owner of the dividend coupon, ii) he can freely avail of the coupon, and iii) he can freely avail of the monies distributed. One could read the formulation of this rule by the Court so as to leave open the question whether the freedom to avail of the coupon or of the distribution must exist in law or in fact, or both. The reference to the wording pertaining to the "*zaakwaarnemer*" and the "*lasthebber*", however, seems to require a narrow reading of the ruling, i.e., one in which the freedom must exist in law. The addition of these terms cannot be read as a further condition, because a *zaarkwaarnemer* and a *lasthebber* by definition cannot freely avail of the dividend. Thus the addition must be seen as a clarification of the conditions of free avail and the *zaakwaarnemer* and the *lasthebber* both lack that freedom in law.

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[13] The taxpayer had argued that the language of Article 10 is clear and that neither the text nor the rationale of this provision justify the condition that the recipient of the dividend must also be the owner of the shares.

[44] Appellant's counsel led evidence that the Canada Revenue Agency, or its predecessor, and the Dutch tax authorities disagreed who was the "beneficial owner" of the dividends received from Prévost. The Dutch are of the view PHB.V. was the "beneficial owner". The appellant requested competent authority assistance relating to the term "beneficial owner" in Article 10(2) of the Tax Treaty. There was some communication between the tax authorities of Canada and the Netherlands, but when the Dutch and Canadian views differed as to whether the beneficial ownership requirement in Article 2 of the 1986 Convention affected situations similar to those in the appeals at bar, the Canadian authorities terminated the competent authority review.

[45] Professor van Weeghel stated that under Dutch law, PHB.V. would be regarded as the beneficial owner of the dividends. However, if PHB.V. were legally obligated to pass on the dividends to its shareholders, Dutch law would consider PHB.V. not to be the beneficial owner of the dividends.

Raas

[46] Professor Rogier Raas is a professor in European banking and securities law at the University of Luden in the Netherlands. Since 2000 he has practiced law with the law firm of Stibbe; he also acts as counsel to corporations and financial

institutions on finance related and regulating matters. Professor Raas did not testify. The appellant produced his redacted report and the respondent did not object.

[47] Professor Raas opined that the dividends received by PHB.V. were within the taxing authority of the Dutch government and that, but for the participation exemption granted by the Dutch government to PHB.V., PHB.V. would have been subject to Dutch tax in respect of the dividends.[12] Despite the existence of a Shareholders' Agreement between Volvo and Henlys and the Powers of Attorney granted to TIM, PHB.V. itself was not contractually or otherwise required to pass on the dividends it received from the appellant. In all cases, dividend payments had to be authorized by PHB.V.'s directors in accordance with Dutch law and practice. The Shareholders' Agreement and Powers of Attorney did not have any effect on the ownership of the dividends by PHB.V., Professor Raas stated.

[48] Professor Raas summarizes Dutch corporate law as it relates to the distribution of profits as follows:

(a) The default scenario under the Netherlands Civil Code is that profits are to be distributed up to the shareholders in full with the only proviso being that the equity of the company remains greater than the sum of its paid up capital, called share capital and statutory reserves;

(b) The mandatory distribution of profits can be deviated from in the Articles of Association of a Dutch B.V., with the majority of Dutch B.V.'s opting to have annual profits at the disposal of the general meeting of shareholders. The shareholders then decide the allocation of the profits between annual reserves and the dividends to be distributed to the shareholders; and

(c) The Board of Directors of a Dutch B.V. can pay interim dividends as opposed to year-end dividends if so authorized by the Articles of Association. Interim dividends are of a provisional nature. They only become final when shareholders pass a year-end resolution to declare an annual dividend equal to the sum of the interim dividends or adopt the annual accounts for the relevant financial year confirming the sufficiency of the reserves.

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[12] A "participation exemption" exempts the taxed entity in the Netherlands from tax on profits including dividends.

[49] In respect of the impact of the dividend policy in the Shareholders' Agreement on the powers of PHB.V. Professor Raas concluded that:

(a) the dividend policy in the Shareholders' Agreement does not provide for a limitation of the powers of the Board of Directors of PHB.V. that is uncommon in a Netherlands law context. A considerable influence of shareholders on the dividend policy of a Dutch B.V. is very common; and

(b) unlike the default scenario or where annual profits are at the disposal of the general meeting of PHB.V.'s shareholders, the Board of Directors had the discretion under PHB.V.'s Articles of Association and the dividend policy to decide the adequacy of the working capital requirements, before dividends were paid.

[50] The respondent argues that Professor Raas assumed incorrectly that PHB.V. had a dividend policy independent of that of the Corporate Group set out in the Shareholders' Agreement and referred to in PHB.V.'s Articles of Association. Instead, respondent's counsel argued, the discretion of the directors of PHB.V. to determine the adequacy of working capital of PHB.V. was inextricably tied to the same determination being made by the directors of Prévost. The proviso in the Shareholders' Agreement on the payment of not less than 80 percent of the after tax profits of the Corporate Group was limited only by a determination of the Board of Directors of both PHB.V. and Prévost as to the adequacy of normal and foreseeable working capital requirement of the Corporate Group at the time of each dividend payment. The dividend policy of PHB.V., as described in the Raas report, was in fact a resolution of purported shareholders of Prévost, represented as Volvo and Henlys, and adopted by the Board of Directors of Prévost, both occurring on March 23, 1996.

[51] Taken together, the respondent says, the dividend policy in the Shareholders' Agreement, the shareholder and director resolutions of March 23, 1996, coupled with the authorization in PHB.V.'s Articles of Association to pay interim dividends defined the scope of the discretion of the directors of the PHB.V. to determine its working capital requirement. This discretion was purely academic.

Lüthi

[52] Daniel Lüthi, a graduate in law, worked in the Swiss Ministry of Finance and negotiated about 30 tax treaties on behalf of Switzerland. He was also a member of the Swiss delegation to the OECD Fiscal Committee, member of

OECD Committee on Fiscal Affairs ("CFA") a member and chairman of the Swiss delegation to the OECD Working Party 1 on Double Taxation as well as a member of the OECD Informal Advisory Group in international tax matters.

[53] Counsel for the Crown objected to the qualification of Mr. Lüthi as an expert and to his potential evidence that is neither relevant nor necessary. I agree with respondent's counsel that several of the questions that were posed to Mr. Lüthi were questions of law, for example, "What is the meaning of the term 'beneficial owner' found in paragraph 2 of Article 10, dividends, in the Model Convention?" I advised the parties that I would hear Mr. Lüthi's evidence and reserve my decision as to admissibility until after the trial. But, at the same time, I informed appellant's counsel that I did not want any questions of law put to Mr. Lüthi and suggested that his report be amended and that all questions of law and his opinion on such questions be redacted from his report. This was done.

[54] I find that the rest of Mr. Lüthi's report is acceptable; it was essentially a fact driven recollection of events that transpired during OECD Model Convention discussions and negotiations. His summary of OECD statements and reports that were in evidence are not legal opinions. I permitted Mr. Lüthi to testify on matters relating to the term "beneficial owner" and to the issues facing draftsmen of the OECD Convention more for background than for anything else.

[55] The term "beneficial owner" was introduced into Article 10(1) of the 1977 OECD Convention, Mr. Lüthi stated, so as to explicitly exclude intermediaries in third States, such as agents and nominees, from treaty benefits. Article 10(1) still caused concern as to whether the shareholder was entitled to treaty benefits in a case where the dividend was received by an agent or nominee but not the shareholder directly. Hence Article 10(1) was further amended in 1995.

[56] Mr. Lüthi could find "no traces" why the term "beneficial owner" had been chosen in the 1977 OECD Convention. Other terms were considered, for example, "final recipient". The intention was that the "beneficial owner" of the income being a resident of the other Contracting State was to benefit from a treaty, not an agent or nominee who is not considered to be the beneficial owner of the income.

[57] There was no expectation that a holding company was a mere agent or nominee for its shareholders, that is, that its shareholders were the beneficial owners of the holding company's income. Indeed, a holding company is the beneficial owner of dividend paid to it unless there is strong evidence of tax avoidance or treaty abuse.

[58] With respect to conduit companies, that is, companies acting as a mere conduit, Mr. Lüthi referred to the CFA Report of 1987, Double Taxation Conventions and the Use of Conduit Companies.[13] He summarized the CFA's report as follows:

> . . . According to this Report, OECD does not deny every conduit company the ability to be the beneficial owner by stating "…The fact that the conduit company's main function is to hold assets or rights is not itself sufficient to categorise it as a mere agent or nominee, although this may indicate that further examination is necessary …". On the other hand, a conduit company cannot normally be considered to be the beneficial owner of the income received if it has very narrow powers, performs mere fiduciary or administrative functions and acts on account of the beneficiary (most likely the shareholder). In the view of OECD, such a company has only title to property, but no other economic, legal or practical attributes of ownership. In such a case, the company, based on a contract or by way of obligations taken over, will have similar functions to those of an agent or a nominee.
>
> According to Article 4 of the OECD Model Convention a conduit company, in order to be entitled to claim treaty benefits, must be liable to tax in its residence country on the basis of its domicile, place of management etc. In addition, the assets and rights giving rise to the income must have effectively been transferred to the conduit company. If this is the case, the conduit company cannot be considered to act as a mere agent or nominee with respect to the income received.

[59] The respondent referred to Mr. Lüthi's observation that when, in 1977, the OECD members, 18 of the 24 of which were civil law countries, adopted the term "beneficial owner", the civil law countries did not intend the term to have the meaning under the law of equity in common law countries.

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[13] An OECD working party's report on conduit companies adopted by the OECD Council on 27 November 1986 distinguishes between two types of conduit companies, direct conduit companies and "stepping-stone" conduits; the former is the conduit discussed here and is described as follows:

> *1. Direct conduits*
>
> A company resident of State A receives dividends, interest or royalties from State B. Under the tax treaty between States A and B, the company claims that it is fully or partially exempted from the withholding taxes of State B. The company is wholly owned by a resident of a third State not entitled to the benefit of the treaty between States A and B. It has been created with a view to taking advantage of this treaty's benefits and for this purpose the assets and rights giving rise to the dividends, interest or royalties were transferred to it. The income is tax-exempt in State A, e.g. in the case of dividends, by virtue of a parent-subsidiary regime provided for under the domestic laws of State A, or in the convention between States A and B.

Analysis

[60] The term "beneficial owner" is not unique to the Tax Treaty; appellant's counsel informs me that it is found in 85 of Canada's 86 tax treaties. Only Canada's treaty with Australia uses the term "beneficially entitled".

[61] The evidence of Professor van Weeghel is that the Netherlands recognizes PHB.V. as beneficial owner of Prévost's dividends. Professor Raas suggests the same. The respondent says Volvo and Henlys are the beneficial owners of the dividends.

[62] The terms "beneficial owner", "beneficially owned" and "beneficial ownership" are found in the English version of the *Act*.[14] The French version of the *Act* uses the words "propriété effective", (as opposed to "bénéficiaire effectif" in the Tax Treaty) sometimes preceded by the word "avoir" where the context of the paragraph requires a verb. However, in the French language version of subsection 227(4.1) of the *Act*, where there is reference to amounts held in trust ("fiducie"), the words used are "droit de bénéficiaire", altogether different from "bénéficiaire effectif". As I mentioned earlier, these terms are not defined in the *Act*.

[63] The term "beneficial owner" is not new to the *Act*. The words were found, for example, before 1971 in section 12A of the *Act*[15] a section limiting advertising expenses. Clause 12A(5)(*a*)(v)(c) of the English text refers to "3/4 of the paid up capital [of a corporation], are beneficially owned by Canadian citizens . . .". The French version of the *Act* referred to "les trois quarts du capital versé, appartiennent à titre de *beneficial interests* à des citoyens canadiens . . .".

[64] When the *Act* was amended effective in 1972[16] the English version of section 19 (previously section 12A) continued to use the term *beneficially owned* but the French version changed "beneficial interests" to *beneficial ownership*. That

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14 The words "beneficial owner" appears in the definition of "propriety held" and "biens détenue" in s. 146.3. The term "beneficially owned" appears in s.s. 19(5), 85.1(2) and (6), 87(9), 115.2(2) and (3), 138(8), 227(4.1), 248(3) and the term "beneficial ownership" appears in s.s. 69(1), 73(1.02), 79(2), 79.1(2), 104(4), 107.4(1), 122(2), 138(11.93), 248(1), 248(25.2). See also s.s. 201(3), 1104(2) and 500 of the Regulations and s.s. 59(2) of the Income Tax Application Rules.

15 R.S.C., 1952, c. 148.

16 Chap. 63, S.C. 1970-71-72. In paragraph 64, words in *italics* were used in French versions of the *Act*.

common law terminology was used in the French version of the *Act* more than suggests the term "beneficial owner" is a common law term. It was only in 1992 that the English words were struck from the French version of the *Act* and were replaced by the words "propriété effective".

[65] The respondent maintains that there is no meaning of the terms "beneficial ownership" and "bénéficiaire effectif" for the purposes of the *Act* which can be invoked for the purpose of Article 3(2) of the Tax Treaty. First of all, according to the respondent, the words used in the *Act* have multiple and often irreconcilable meanings. Counsel referred to a study by Professor Catherine Brown who concluded that the term "beneficial owner" has different meanings under the *Act* depending on the provision.[17] For example, she identified at least four categories of meaning for the expression "beneficial ownership", "beneficial owner" and "beneficially owned" when used in a trust context: (a) the owner is the beneficial owner; (b) the beneficiary is considered to be the beneficial owner as a result of tax decisions and the operation of the *Act*, for example subsection 104(1); (c) the beneficiary is the beneficial owner of trust property on the basis of private law principles; and (d) the trust is the owner of trust property, for example, the *Act* deems the trust to be the owner of the trust property. Also, the term "beneficial owner" is not used in any provision of the *Act* concerned with withholding tax on Canadian source dividends, interest or royalties.[18]

[66] Respondent's counsel, citing an article by Mr. Mark D. Brender, submits that there is no settled definition of "beneficial ownership" even under common law, let alone for the purposes of the *Act*.[19] Indeed, Mr. Brender suggests that words or concepts neutral as between the civil and common laws be used in place of "beneficial owner" or "beneficial ownership".[20]

[67] Counsel for the respondent referred to the VCLT, the Tax Treaty, Model Conventions as well as the *Act* to suggest how the terms "beneficial owner" and "bénéficiaire effectif" should be interpreted, bearing in mind that these terms are not defined in the Tax Treaty, Model Conventions and the *Act* and have no legal meaning in Quebec, a civil law jurisdiction. The respondent's submission was that these words should not have a technical or legal meaning but an interpretation recognized internationally.

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17 *Symposium: Beneficial ownership and the Income Tax Act* (2003) 51 *Canadian Tax Journal*, No. 1, pp. 424-427. See also pp. 412, 452, among others.

18 S. 212 of the *Act*.

19 *Symposium: Beneficial ownership and the Income Tax Act*, *supra*, at pp. 315-318.

20 *Supra*, pp. 42-43.

[68] The terms "beneficial owner" and "bénéficiaire effectif", together with the Dutch term ***uiteindelijk gerechtigde***, appear in the Tax Treaty and must be given meaning. The words "bénéficiaire effectif" appear nowhere in the French version of the *Act*. This may, it is suggested, limit the scope of Article 3(2) of the Tax Treaty. The term "bénéficiaire effectif" also does not appear in the Quebec Civil Code. Respondent's counsel submits that the use of the words "bénéficiaire effectif" in the Tax Treaty rather than "propriétaire effectif", which are used in the *Act*, suggests that Parliament intended to use the private law of the provinces to compliment the *Act* and the words are not be determined by reference to the common law.

[69] The respondent also states that while the Tax Treaty refers to the "beneficial owner of the dividends", the *Act* never uses such a phrase. The *Act* refers to a taxpayer who has income from property, for example, a dividend received by a taxpayer, and this income is included in the taxpayer's income for the year. The phrase is never used in conjunction with the income which is derived from the property. Respondent's counsel submits the term "beneficial owner" or a similar expression is never used in the *Act* in the same context as it is used in the Tax Treaty and Model Convention.

[70] Respondent's counsel declared that when determining the meaning of an undefined treaty term, Canadian courts have relied on the meaning relevant to the specific tax provision in respect of which the treaty applies. Thus, in *A.G. of Canada v. Kubicek Estate*,[21] the word "gain", which was not defined in the Canada U.S. Tax Treaty, was given the meaning found in subsection 40(1) of the *Act*. The *Hoge Raad*[22] could not find the meaning of the word "present" in the domestic laws of the Netherlands and therefore held that the word appearing in tax treaties between the Netherlands and Brazil and the Netherlands and Nigeria be interpreted in accordance with Articles 31 and 32 of the VCLT and not the equivalent provisions of Article 3(2) of the Model Convention.

[71] Respondent's counsel therefore concluded that the terms "beneficial owner" and similar terms in the *Act* are based on legalistic trust meanings originating under

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[21] 97 DTC 5454 (FCA) para. 8. See also *Hinkley v M.N.R.*, 91 DTC 1336 (TCC) at p. 1340.

[22] *Hoge Raad*, February 21, 2003, case No. 37, 011, BNB 2003/177a; *Hoge Raad*, case No. 37024, BNB 2003/178c, cited by Michael N. Kandev; "Tax Treaty Interpretation": Determining Domestic Meaning Under Article 3(2) of the OECD Model, *Canadian Tax Journal*, (2007) Vol. 55, No. 1, p. 31, at note 115.

the laws of equity and ought not to apply to the Tax Treaty. The words "beneficial owner" and "bénéficiaire effectif" have no meaning in the *Act*.[23]

[72] Respondent's counsel informs me that the phrase "beneficial owner" does not appear in English dictionaries. The words do appear separately, of course. The word "beneficial" in the *Canadian Dictionary of the English Language* is defined primarily as "producing or promoting a favourable result" or "receiving or having the right to receive proceeds or other advantages". The word "beneficial", counsel states, connotes both a factual ("receiving") and legal ("right to") meaning.[24] The *Shorter Oxford Dictionary* (1973) defines "beneficial" as "of or pertaining to the usufruct of property; enjoying the usufruct", usufruct being a civil law concept. In *The New Shorter Oxford Dictionary* "beneficial" is defined as "Of, pertaining to, or having the use of benefit of property etc.".

[73] The *Canadian Dictionary* defines "owner" as "of or belonging to oneself", "to have or possess as property", and "to have control over". The word "owner" he states also connotes both a factual (possess, control) and legal ("belonging") meaning. The *Shorter Oxford* defines "own" as "one's own . . . to have or hold as own's own". The word "owner" is "one who owns or holds something; one who has a rightful claim or title to a thing".

[74] In the *Jodrey Estate* the Supreme Court approved of the meaning given by Hart J., in *MacKeen v. Nova Scotia*, who wrote:

> It seems to me that the plain ordinary meaning of the expression "beneficial owner" is the real or true owner of the property. The property may be registered in another name or held in trust for the real owner, but the "beneficial owner" is the one who can ultimately exercise the rights of ownership in the property.[25]

[75] Respondent's counsel submits that from a textual reading of the term "beneficial owner", its meaning can be distilled as applying to the person who can exercise the normal incidents of ownership (possession, use, risk, control) and as such ultimately benefits from the income. The ordinary meaning of "bénéficiaire

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[23] Respondent's counsel submissions also referred to the Department of Justice policy on legislative bijuralism, the essence of which is presented in the preamble to the *Federal Law - Civil Law Harmonization Act, No. 1*, S.C. 2001, c. 4.

[24] *Canadian Dictionary of the English Language*, International Thomson Publishing, 1997, see also *Webster's Ninth New Collegiate Dictionary* (Meriam-Webster 1989), and the *Shorter Oxford English Dictionary* (Oxford University Press, 1973).

[25] *Covert v. Nova Scotia (Minister of Finance)*, [1980] S.C.J. No. 101 (Q.L.), [1980] 2 S.C.R. 774, at p. 784, citing *MacKeen Estate v. Nova Scotia*, [1977] C.T.C. 230 (NSSC), para. 46.

effectif" in the French text and ***uiteindelijk gerechtigde*** in the Dutch share common features with the ordinary meaning of "beneficial owner", but have a significant difference.

[76] The word "bénéficiaire", used as a noun in the French version, is defined as follows in the modern French dictionaries:

> Se dit de qqn, d'un groupe qui profite d'un benefice, d'un avantage (…)[26] Personne qui bénéficie (d'un avantage, d'un droit, d'un privilège)[27].

[77] "Bénéficiaire" is defined, counsel submits, consistently, as the person who enjoys or takes advantage of a benefit of any kind, including a right or a privilege. Therefore, he submits that "bénéficiaire" is clearly not a technical term and does not *per se* connote a legal right, such as that of ownership.

[78] The word "effectif", on the other hand, counsel for the respondent argues, is used as an adjective in the French version. The word "effectif" he adds, is the clearest expression of a factual determination that the drafters could have used. It is defined as follows:

> 1. Se dit de qqch dont la réalité est incontestable, qui produit un effet reel, tangible (…) 2. Se dit de ce qui est une réalité[28].

> 1. Qui se traduit par un effet, par des actes reels. Concret, efficace, réel, tangible, vrai (…) Avantage effectif : Certain, concret, positif[29].

[79] "Effectif" is defined as "real" or "producing actual effects" or "resulting in real action". The synonyms that are offered can be translated to "concrete, meaningful, real, tangible and true". Accordingly, respondent's counsel states, the word "effectif" is inconsistent with a search for legal rights or entitlement because it is concerned with reality and the actual results.

[80] Therefore, respondent's counsel concludes, the term "bénéficiaire effectif" means the person or group that actually and truly enjoys or benefits from an advantage of any kind. Authors have translated the words "bénéficiaire effectif" to

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26 *Grand Larousse Universel*, (1997, Larousse, Paris), p. 1167.

27 *Le Grand Robert de la Langue Française*, (deuxième édition, Dictionnaires Le Robert, Paris, 2001), p. 1336.

28 *Grand Larousse Universel*, *supra*.

29 *Le Grand Robert de la Langue Française*.

"real beneficiary",[30] which is a fairly accurate translation as long as the word beneficiary is not understood in a legal sense.

[81] The Dutch version of the Convention uses the term ***uiteindelijk gerechtigde*** for "beneficial owner". This term, translated back to English, means "he who is ultimately entitled". Professor van Weeghel, notes in his text *The Improper Use of Tax Treaties* that:

> It is unclear why this translation [***uiteindelijk gerechtigde***] was chosen. The term 'beneficial owner' (One who does not have title to property but has rights in the property which are the normal incidents of owning the property', Black's Law Dictionary, Fifth Edition) has a closer equivalent in Dutch language and this would be '*economisch eigenaar*' a term which has a well understood meaning also in Dutch law.[31]

[82] However, as respondent's counsel declares, the government of the Kingdom of the Netherlands opted in the Tax Treaty to use a term for "beneficial owner" whose English translation of "ultimately entitled" connotes a factual inquiry, meaning "final" or "in the end". Just as in the French text, there is no reference to ownership in the Dutch text. ***Uiteindelijk gerechtigde*** is also consistent with the ordinary meaning given to the term by the *Royal Dutch* case, *supra*, in which the ***uiteindelijk gerechtigde*** of a dividend is one who can "freely avail of the distribution"; being the person ultimately entitled to the benefit of the income.[32]

[83] Respondent's counsel submits that the plain and ordinary meaning of the terms "beneficial owner", "bénéficiaire effectif" and ***uiteindelijk gerechtigde*** in the three languages of the text of the Tax Treaty does not suggest that an exclusively legal meaning should be given to the terms. Counsel is of the view that the term "bénéficiaire effectif" points strongly to a determination of the true relationship and is inconsistent with a narrow legalistic meaning. Respondent insists that the meaning of each term used in all three versions accommodates only a non-legal meaning. It is this commonality between the three versions which must form the basis for defining the term, he suggests.

[84] The respondent's view is that a reconciliation of the three language versions of the Tax Treaty results in a meaning that requires a search behind the legal

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30 Du Toit, Charl P., *Beneficial ownership of Royalties in Bilateral Tax Treaties*, IBFD Publications, 1999, p. 165.

31 *The Improper Use of Tax Treaties* (Kluwer Law International, The Hague, 1998), p. 73, note 131.

32 Cited in van Weeghel, *Improper Use of Tax Treaties*, *supra*, pp. 75-77.

relationships in order to identify the person who, as a matter of fact, can ultimately benefit from the dividends. The respondent seeks support from a non tax case before the England and Wales Court of Appeal that was called upon to interpret the term "beneficial ownership" within the context of the civil law of Indonesia: *Indofood International Ltd. v. JP Morgan Chase Bank N.A. London Branch*.[33]

[85] The facts of *Indofood* are as follows: An Indonesian company, Indofood ("Parent"), set up a Mauritian special purpose vehicle ("Issuer") to issue loan notes. Back to back loans were put in place. The loan notes contained a gross-up clause and provided for early redemption in case that, due to tax or treaty changes, the Issuer had to pay additional tax. The notes also contained a clause requiring the Issuer to try to mitigate any additional tax liability by "taking reasonable measures available to it" before seeking to redeem the notes. The financing was structured via Mauritius to avail of the beneficial withholding tax rates under the Indonesia-Mauritius Double Tax Treaty. Mauritius has no outbound withholding taxes.

[86] As a result of abuse of the treaty by conduit companies, Indonesia terminated its tax treaty with Mauritius effective January 1, 2005, thus increasing to 20 percent the withholding on the interest payments between the Parent and the Issuer. In other words, the gross-up, instead of being 10 percent became 20 percent under domestic Indonesian law. Since the issue of the notes in 2002, both interest and exchange rates had moved against the Parent and in favour of the noteholders. The Parent, therefore, sought to redeem the notes and refinance more cheaply. However, JP Morgan Chase (the "Defendant") acting as trustee for the bondholders was not satisfied that the best endeavours clause had been complied with, alleged that *Indofood* could have interposed a Dutch entity ("Newco") into their structure and availed of the preferable rates under the Netherlands-Indonesia Double Taxation Convention. Therefore, the Defendant refused to approve the redemption.

[87] The main substantive issue at trial was whether Newco would be the beneficial owner of the interest payable to it by the Parent for the purposes of the reduced withholding tax rate in Article 11 of the Indonesia-Netherlands Tax Convention.

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[33] [2006] E.W.C.A. Civ. 158, S.T.L. 1195. I also note that the Court of Appeal had regard to substance over form, as required by the law of Indonesia (paras. 18 and 24).

[88] In the High Court,[34] Justice Evans-Lombe found largely in favour of the Defendant and found that Newco would be the beneficial owner of the interest from the Parent. In particular, he noted:

> It is clear that Newco, just as the Issuer, will not be a nominee or agent for any other party and, not being any sort of trustee or fiduciary, will have power to dispose of the interest when received as it wishes, although it will be constrained by its contractual obligation to the Issuer to apply the proceeds of the interest payments in performance of those obligations.[35]

[89] Justice Evans-Lombe determined beneficial ownership by referring to the rights of creditors in the event of Newco's insolvency:

> It is clear to me that in the absence of any trust or fiduciary relationship between Newco and the Issuer, in an insolvency of Newco undistributed interest received from the Parent Guarantor would be an asset of Newco for distribution amongst its creditors generally, including the Issuer, pari passu.[36]

[90] *Indofood* appealed to the Court of Appeal, while the Defendant, JPMorgan, cross-appealed on the point that had gone against them. The Court of Appeal found unanimously for *Indofood*, that the Issuer was not the beneficial owner and, if interposed, Newco could not be the beneficial owner of the interest received from the Parent for purposes of Article 11(2) of the Indonesia–Mauritius Tax Convention or the Indonesia–Netherlands Tax Convention.

[91] On the question of whether Newco would be the beneficial owner of the interest, Sir Andrew Morritt said as follows:

> The fact that neither the Issuer nor Newco was or would be a trustee, agent or nominee for the noteholders or anyone else in relation to the interest receivable from the Parent Guarantor is by no means conclusive. Nor is the absence of any entitlement of a noteholder to security over or right to call for the interest receivable from the Parent Guarantor. The passages from the OECD commentary and Professor Baker's observations thereon show that the term "beneficial owner" is to be given an international fiscal meaning not derived from the domestic laws of contracting states. As shown by those commentaries and observations, the concept of beneficial ownership is incompatible with that of the formal owner who does not have "the full privilege to directly benefit from the income".[37]

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34 [2005] EWHC 2103 (Ch).

35 *Ibid*., para. 46.

36 *Ibid*., para. 49.

37 *Supra*, note 20, para. 42.

[92] He continued:

> The legal, commercial and practical structure behind the loan notes is inconsistent with the concept that the Issuer or, if interposed, Newco could enjoy any such privilege. In accordance with the legal structure the Parent Guarantor is obliged to pay the interest two business days before the due date to the credit of an account nominated for the purpose by the Issuer. The Issuer is obliged to pay the interest due to the noteholders one business day before the due date to the account specified by the Principal Paying Agent. The Principal Paying Agent is bound to pay the noteholders on the due date.[38]
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> But the meaning to be given to the phrase "beneficial owner" is plainly not to be limited by so technical and legal an approach. Regard is to be had to the substance of the matter. In both commercial and practical terms the Issuer is, and Newco would be, bound to pay on to the Principal Paying Agent that which it receives from the Parent Guarantor. This is recognised by what we were told actually happens now as recorded in paragraph 13 above. The Parent Guarantor is bound to ensure that such an arrangement continues lest it is required to pay again under its guarantee to the noteholders contained in the Trust Deed. In practical terms it is impossible to conceive of any circumstances in which either the Issuer or Newco could derive any 'direct benefit' from the interest payable by the Parent Guarantor except by funding its liability to the Principal Paying Agent or Issuer respectively. Such an exception can hardly be described as the 'full privilege' needed to qualify as the beneficial owner, rather the position of the Issuer and Newco equates to that of an "administrator of the income".

[93] The decision in *Indofood* conflicts somewhat with the opinion the Dutch government and the *Hoge Raad* in the *Royal Dutch* case, *supra*, that a recipient is not the beneficial owner of income only if it is contractually obligated to pay the largest part of the income to a third party.[39] In *Indofood*, the Court of Appeal did not base its reasoning on contractual obligation to forward the interest, but rather whether the recipient enjoyed the "full privilege" of the interest or if it was simply an "administrator of income".

[94] The parties agree that PHB.V. was not an agent, trustee or nominee for Volvo and Henlys. Rather, it is the respondent's view that PHB.V. was acting as a

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38 Para. 43.

39 In his report Professor van Weeghel quotes from comments by the Dutch Underminister of Finance in a Ministry of Finance memorandum to the Finance Committee of the Dutch Parliament in the 1987-1988 Parliamentary year.

mere conduit or funnel in favour of Volvo and Henlys upon receiving dividends from Prévost.

[95] I am being asked to determine what the words "beneficial owner" and "bénéficiare effectif" (and the Dutch equivalent) mean in Article 10(2) of the Tax Treaty. Article 3(2) of the Tax Treaty requires me to look to a domestic solution in interpreting "beneficial owner". The OECD Commentaries on the 1977 Model Convention with respect to Article 10(2) are also relevant.

[96] The Commentary for Article 10(2) of the Model Convention explains that one should look behind "agents and nominees" to determine who is the beneficial owner. Also, a "conduit" company is not a beneficial owner. In these three examples, the person − the agent, nominee and conduit company − never has any attribute of ownership of the dividend. The "beneficial owner" is another person.

[97] I want to give a very short example of a civil law concept affecting ownership of property. Article 908 of the *Civil Code of Quebec* states that property, according to its relation to other property, is divided into capital, and fruits and revenue. Article 947 of the *Civil Code* grants the owner of property the right to use, enjoy and dispose of the property fully and freely. These are rights that in common law belong to the beneficial owner of property. In civil law, one person may be the bare owner ("nu-propriétaire") of the property but another person, called the usufructary, may use and enjoy the property and the usufructary is the owner of the usufruct in his or her own right, subject to the obligation of preserving the substance of the property: *Civil Code*, article 1120. The usufructary receives the income from the property as owner of the income. He or she is not accountable to the bare owner for any income. That person is similar to the "beneficial owner" in common law of the income. When a property is held by a nominee, agent or trustee in a civil law jurisdiction and a common law jurisdiction, that person acknowledges the relationship that he or she is not actually the owner of the property.

[98] In common law, a trustee, for example, holds property for the benefit of someone else.[40] The trustee is the legal owner but does not personally enjoy the attributes of ownership, possession, use, risk and control. The trustee is holding the property for someone else and that, ultimately, it is that someone else who has the use, risk and control of the property. Also, in common law, one person may have a life interest in property and another may have a remainder interest in the same

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40 The *Civil Code of Quebec* recognizes a trust: articles 1260 to 1298.

property. The owner of the life interest receives income from the property and owns the income; the owner of the remainder interest owns the capital of the property. There is no division of property in common law as there is in civil law. The word "beneficial" distinguishes the real or economic owner of the property from the owner who is merely a legal owner, owning the property for someone else's benefit, i.e., the beneficial owner.

[99] In both the common law and the civil law, the persons who ultimately receive the income are the owners of the income property. It may well be, as respondent's counsel argues, that when the terms "beneficial owner", "beneficially owned" or "beneficial ownership" are used in the *Act*, it is either used in conjunction with property, such as shares or some other property but is never used in conjunction with the income which is derived from the property. i.e., dividends from shares. However, dividends, whether coin or something else, are in and by themselves also property and are owned by someone. Section 12 of the *Act* includes in computing income of a taxpayer for a taxation year income from property, including amounts of dividends received in the year. The taxpayer required to include the amount of dividends in income is usually the person who is the owner − the beneficial owner − of the dividends, except, for example, when the *Act* deems another person to have received the dividend or requires a trust to include the dividend in its income.[41] The words "beneficial owner" in plain ordinary language used in conjunction with dividends is not something alien.

[100] In my view the "beneficial owner" of dividends is the person who receives the dividends for his or her own use and enjoyment and assumes the risk and control of the dividend he or she received. The person who is beneficial owner of the dividend is the person who enjoys and assumes all the attributes of ownership. In short the dividend is for the owner's own benefit and this person is not accountable to anyone for how he or she deals with the dividend income. When the Supreme Court in *Jodrey*[42] stated that the "beneficial owner" is one who can "ultimately" exercise the rights of ownership in the property, I am confident that the Court did not mean, in using the word "ultimately", to strip away the corporate veil so that the shareholders of a corporation are the beneficial owners of its assets, including income earned by the corporation.[43] The word "ultimately" refers to the recipient of the dividend who is the true owner of the dividend, a person who could

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41 For example, s.s. 82(3), subpara. 82(1)(*a*)(1.1). Reference is to taxable dividends.

42 *Supra*, 784.

43 See, for example, *Radwell Securities, Ltd. v. Inland Revenue Commissions*, [1968] 1 All E.R. 257.

do with the dividend what he or she desires. It is the true owner of property who is the beneficial owner of the property. Where an agency or mandate exists or the property is in the name of a nominee, one looks to find on whose behalf the agent or mandatary is acting or for whom the nominee has lent his or her name. When corporate entities are concerned, one does not pierce the corporate veil unless the corporation is a conduit for another person and has absolutely no discretion as to the use or application of funds put through it as conduit, or has agreed to act on someone else's behalf pursuant to that person's instructions without any right to do other than what that person instructs it, for example, a stockbroker who is the registered owner of the shares it holds for clients. This is not the relationship between PHB.V. and its shareholders.

[101] What we have at bar is a Canadian corporation, Prévost, paying dividends to its sole shareholder, PHB.V., a Dutch corporation. There is evidence that Prévost's minute book contains reference to Henlys and Volvo being its shareholders and there are reported references by Ms. Bissonnette that Henlys wanted its dividends. These errors are not fatal to the appellant's case. Minute books do contain errors. And it is not uncommon that the principals of corporations, rather than the shareholders, are erroneously referred to as the owners of the corporation.

[102] There is no evidence that PHB.V. was a conduit for Volvo and Henlys. It is true that PHB.V. had no physical office or employees in the Netherlands or elsewhere. It also mandated to TIM the transaction of its business as well for TIM to pay interim dividends on its behalf to Volvo and Henlys. However, there is no evidence that the dividends from Prévost were *ab initio* destined for Volvo and Henlys with PHB.V. as a funnel of flowing dividends from Prévost. The financial statements of PHB.V. for fiscal periods ending on December 31st in each of 1995, 1996 and 1997 and copies of PHB.V.'s corporate income tax returns for 1996, 1997, 1998, 1999 and 2000 reflect that PHB.V. owned assets and had liabilities. For Volvo and Henlys to obtain dividends, the directors of PHB.V. had to declare interim dividends and subsequently shareholders had to approve the dividend. There was no predetermined or automatic flow of funds to Volvo and Henlys even though Henlys' representatives were trying to expedite the process.

[103] PHB.V. was a statutory entity carrying on business operations and corporate activity in accordance with the Dutch law under which it was constituted. PHB.V. was not party to the Shareholders' Agreement; neither Henlys nor Volvo could take action against PHB.V. for failure to follow the dividend policy described in the Shareholders' Agreement. Henlys may have a cause of action against Volvo and Volvo a cause of action against Henlys under the Shareholders' Agreement if the

dividend policy was not carried out. But neither would have a *bona fide* action in law under the Shareholders' Agreement against a person not a party to that agreement, that is, PHB.V. Volvo and Henlys, of course, may have action against PHB.V. if PHB.V. did not repay monies advanced as loans by them, but such action would be taken as creditors of PHB.V., not shareholders.

[104] Article 24 of PHB.V.'s Deed of Incorporation does not obligate it to pay any dividend to its shareholders. The directors of PHB.V. are to duly observe what has been agreed to in the Shareholders' Agreement concerning reserving part of its accrued profits. Article 24, paragraph 2 of the Deed provides that any profits remaining after the reservation of part of the accrued profits shall be at the disposal of the general meeting.[44] I cannot find any obligation in law requiring PHB.V. to pay dividends to its shareholders on a basis determined by the Shareholders' Agreement. When PHB.V. decides to pay dividends it must pay the dividends in accordance with Dutch law.

[105] PHB.V. was the registered owner of Prévost shares. It paid for the shares. It owned the shares for itself. When dividends are received by PHB.V. in respect of shares it owns, the dividends are the property of PHB.V. Until such time as the management board declares an interim dividend and the dividend is approved by the shareholders, the monies represented by the dividend continue to be property of, and is owned solely by, PHB.V. The dividends are an asset of PHB.V. and are available to its creditors, if any. No other person other than PHB.V. has an interest in the dividends received from Prévost. PHB.V. can use the dividends as it wishes and is not accountable to its shareholders except by virtue of the laws of the Netherlands. Volvo and Henlys only obtain a right to dividends that are properly declared and paid by PHB.V. itself, notwithstanding that the payment of the dividend has been mandated to TIM. Any amount paid by PHB.V. to Henlys and Volvo before a dividend was properly declared and paid, as I see it, was a loan from PHB.V. to its shareholders. This, too, is not uncommon. There is a practice in Canada of corporations advancing funds to its shareholders without a declaration of dividend. At the end of the fiscal year, the corporation's directors determine whether the funds are to remain a loan or be "adjusted" to a dividend, with the proper directors' resolutions. This practice, I understand, is accepted by the fisc.

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[44] "General meeting" is defined in the Deed of Incorporation as "the body of the company formed by shareholders". The "general meeting of shareholders" is "the meeting of shareholders". The "management board" is what we in Canada refer to as the board of directors.

Secondary Issue

[106] In its amended notice of appeal from the assessments issued in 2000 and 2001, the appellant alleges that throughout the assessment process the Minister's actions improperly deprived PHB.V. of substantive rights afforded it under Article 25 of the Canada/Netherlands Convention. The appellant complains that the Minister confirmed the assessments in issue notwithstanding that the Dutch government had, at the request of PHB.V., commenced Competent Authority Proceedings under the Treaty and only relented in such course of conduct after the appellant and PHB.V. commenced proceedings in the Federal Court, Trial Division. The appellant claims that such action was contrary to Canada's obligations under the Treaty and to the Minister's published position in this regard.[45] The appellant also takes umbrage that the Minister terminated the Competent Authority Proceedings unilaterally and did not act in good faith to attempt to arrive at a satisfactory position in accordance with the Treaty. Apparently, according to the appellant, the Minister and the Dutch tax authority did not agree on the interpretation of the relevant provisions of the Treaty and the Minister did not take into account the position of the Dutch government.

[107] Accordingly, the appellant argues that the Minister's actions improperly deprived PHB.V. of substantive rights afforded it under Article 25 of the Treaty and therefore this Court has jurisdiction to strike out the Minister's reply. Appellant's counsel produced documentation filed by the appellant and PHB.V. in the Federal Court through Mr. Backstrom. The documents include an application for an order of Mandamus requiring: (a) the tax authority to endeavor to resolve by mutual agreements any difficulties or doubts arising between the competent authorities of Canada and the Netherlands as to the interpretation or application of the Treaty to the subject matter raised in the assessments in good faith: and (b) an application for an interlocutory order prohibiting the Canadian tax authorities from proceeding with any determination or confirmation of the assessments pending the hearing of the application. The appellant, PHB.V. and the Crown eventually settled their dispute and the application to the Federal Court was withdrawn.

[108] The Minister's reply will not be struck. PHB.V., the party purportedly aggrieved, is not a party to the matter before me. Section 12 of the *Tax Court of Canada Act* provides that the Court has ". . . exclusive original jurisdiction to hear and determine references and appeals . . . on matters arising under . . . the *Income*

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[45] Article 25 of the Treaty, Information Circular 71-17R5 [Draft, 2003] and Information Circular 71-17R4, dated May 12, 1995.

Tax Act . . .". In accordance with subsection 169(1) of the *Act*, only those persons who have been notified of an assessment of tax or have filed a notice of objection under section 165 of the *Act* may appeal to the Tax Court of Canada. A person who is not an appellant has no standing in this Court except in exceptional circumstances and then, only with leave.

[109] The Tax Court's interest is in whether an assessment is correct or not correct. If a person believes that he or she has suffered prejudice during the course of the Minister's actions in administering the *Act*, that person may take action in the Federal Court. Rule 53 of the *Tax Court of Canada Rules (General Procedure)* provides that the Court may strike out or expunge all or part of a pleading or other document, which may prejudice or delay the fair hearing of the action, scandalous, frivolous or vexatious or an abuse of the process of this Court. There is no evidence before me of any such ground to strike out all or any portion of the Minister's reply.

Judgment

[110] The assessments will be vacated. Volvo and Henlys were not the beneficial owners of the dividends paid by Prévost. I have not heard any evidence satisfying me that PHB.V. was a conduit for Volvo and Henlys. The appeals are allowed, with costs. At the conclusion of the trial appellant's counsel requested submissions be made with respect to costs following the issue of these reasons. If either counsel still wishes to make submissions he should get in touch with the Registrar of the Court to advise whether he and opposing counsel wish to make oral or written submissions and suggest deadlines for the submissions.

Signed at Ottawa, Canada, this 30th day of April 2008.

"Gerald J. Rip"

Rip A.C.J.

CITATION:	2008TCC231
COURT FILES NO.:	2004-2006(IT)G and 2004-4226(IT)G
STYLE OF CAUSE:	PRÉVOST CAR INC. v. HER MAJESTY THE QUEEN
PLACE OF HEARING:	Toronto, Ontario
DATE OF HEARING:	September 4, 5, 6 and 7, 2007
REASONS FOR JUDGMENT BY:	The Honourable Gerald J. Rip, Associate Chief Justice
DATE OF JUDGMENT:	April 22, 2008
DATE OF AMENDED JUDGMENT	April 30, 2008

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