

Docket: 2009-647(IT)G

BETWEEN:

SUNDOG DISTRIBUTING INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Motion heard on March 18, 2010, at Calgary, Alberta.

Before: The Honourable Gerald J. Rip, Chief Justice

Appearances:

Counsel for the appellant: Shaun T. MacIsaac
 R. Paul Jacobson

Counsel for the respondent: Marta E. Burns
 Leona Tesar

DETERMINATION

Upon motion by the appellant for a determination of the following question of law, as raised by the appellant's pleadings in these proceedings pursuant to paragraph 58(1)(a) of the *Tax Court of Canada Rules (General Procedure)*:

Whether the Minister of National Revenue (the "Minister") issued the reassessments after the expiry of the applicable limitation period.

And upon reading the material filed on the motion;

And upon hearing counsel for the parties;

The Court finds that the Minister has not issued the reassessments for the 1998, 1999 and 2000 taxation years after the expiry of the applicable limitation periods.

The respondent is entitled to its costs.

Signed at Ottawa, Canada, this 22nd day of July 2010.

"Gerald J. Rip"

Rip C.J.

Citation: 2010 TCC 392

Date: 20100722

Docket: 2009-647(IT)G

BETWEEN:

SUNDOG DISTRIBUTING INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR DETERMINATION

Rip, C.J.

[1] Sundog Distributing Inc. has applied in accordance with section 58 of the *Tax Court of Canada Rules (General Procedure)* ("Rules") for a determination, before the hearing of its appeals from reassessments of income tax for 1998, 1999 and 2000, of the following question of law raised in paragraph 2 of its Notice of Appeal: whether the Minister of National Revenue ("Minister") issued the reassessments after the expiry of the applicable limitation periods.

[2] The issue to be decided is if the appropriate limitation period for each taxation year is the five year period described in Article IX(3) and Article XXVII(3) of the Canada-Barbados Tax Treaty¹ or the period determined by subparagraph 152(4)(b)(iii) of the *Income Tax Act* ("Act").

[3] Article IX(3) of the Treaty provides that:

A contracting State shall not change the profits of an enterprise in the circumstances referred to in paragraph 1 after the expiry of the time limits	Un État contractant ne rectifiera pas les bénéfices d'une entreprise dans les cas visés au paragraphe 1 après l'expiration des délais prévus par sa législation
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¹ *Agreement Between Canada and Barbados for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital* signed on January 22, 1980 ("Treaty"). Articles I, III, VII, IX, XXVII and XXX of the Treaty are reproduced in the Appendix to these reasons.

provided in its national laws and, in any case, after five years from the end of the year in which the profits which would be subject to such change would have accrued to an enterprise of that State. This paragraph shall not apply in the case of fraud, wilful default or neglect.

nationale et, en tout cas, après l'expiration de cinq ans à dater de la fin de l'année au cours de laquelle les bénéfices qui feraient l'objet d'une telle rectification auraient été réalisés par une entreprise de cet État. Le présent paragraphe ne s'applique pas en cas de fraude, d'omission volontaire ou de négligence.

[4] Article XXVII(3)² states:

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.

Un État contractant n'augmentera pas la base imposable d'un résident de l'un ou l'autre État contractant en y incluant des éléments de revenu qui ont déjà été imposés dans l'autre État contractant, après l'expiration des délais prévus par sa législation nationale et, en tout cas, après l'expiration de cinq ans à dater de la fin de la période imposable au cours de laquelle les revenus en cause ont été réalisés. Le présent paragraphe ne s'applique pas en cas de fraude, d'omission volontaire ou de négligence.

[5] The parties agreed to the following facts:

- a. The Appellant appeals the reassessments made by the Respondent's Minister of National Revenue (the "Minister") under the *Income Tax Act*, R.S.C. 1985, c. 1(5th Supp.), (the "*Act*") for the 1998, 1999 and 2000 taxation years (the "Reassessments" and the "Taxation Years Under Appeal");
- b. The Minister reassessed the Appellant's 1998, 1999 and 2000 taxation years. The Appellant served the Minister with Notices of Objection in relation to the Reassessments;
- c. The Minister confirmed the Reassessments by Notice of Confirmation dated December 3, 2008;

² Article IX and XXVII of the Treaty serve separate purposes: Article IX of the Treaty is concerned with the taxation of business profits of enterprises in Canada and Barbados by both countries and imposes a time limit on the taxation of these profits. Article XXVII(3) imposes a time limit by both countries to assess tax on the same item of income.

- d. In the Taxation Years Under Appeal, the Appellant, an Alberta incorporated company, was controlled by William Hoogstraten and Roderick Hoogstraten, who are father and son, and are individuals resident in Alberta;
- e. In the Taxation Years Under Appeal, William Hoogstraten and Roderick Hoogstraten indirectly controlled Sun Island Optics International Inc. ("Sun Island Optics") and Sun Island International Inc. ("Sun Island") for the Taxation Years Under Appeal;
- f. Sun Island Optics and Sun Island are both Barbados International Business Companies ("IBC") licensed under the Barbados *International Business Companies Act*, both corporations are resident in Barbados, and both corporations did not deal at arm's length with the Appellant under the *Act*;
- g. The fiscal year end of the Appellant is November 30;
- h. The Minister conducted an audit of the Appellant's 1998, 1999 and 2000 taxation years;
- i. The Minister issued a Notice of Reassessment for the Appellant's 1998 taxation year on August 9, 2005 increasing the Appellant's income by \$458,446 pursuant to subsection 69(3) of the *Act*;
- j. The Minister issued Notices of Reassessment for the Appellant's 1999 and 2000 taxation years on April 13, 2006 increasing the Appellant's income by \$183,451 and \$227,225 for the 1999 and 2000 taxation years, respectively, pursuant to paragraphs 247(2)(a) and (c) of the *Act*;
- k. Each of the three Notices of Reassessment indicated that the figures added to reported income of the Appellant were transfer pricing adjustments;
- l. The amounts added to reported income of the Appellant were previously reported as gross profit by Sun Island Optics for the 1998 and 1999 taxation years and by Sun Island for the 2000 taxation year;
- m. The amounts added to reported income of the Appellant were previously taxed by the Government of Barbados in Sun Island Optics for the 1998 and 1999 taxation years and by Sun Island for the 2000 taxation year;
- n. A copy of the Canada-Barbados Income Tax Convention, 1980 (the "Treaty") is attached as Schedule "A". It is agreed between the parties that the provisions of the Treaty are of full force and effect, and it is not necessary to call additional evidence to prove the terms of the Treaty;
- o. For the purposes of a preliminary rule 58 motion only, the issue to be determined is whether the Minister issued the Reassessments after the expiry

of the applicable limitation periods under the Treaty;

- p. The parties agree that the issue as set forth herein is an appropriate one to proceed by way of section 58 of the *Act*, as the motion is decided in favour of the Appellant, the Reassessments would then be vacated.

[6] In addition, the appellant produced the Affidavit of Roderick Hoogstraten, President of the appellant, which included, as attachments, the tax returns of Sun Island Optics and Sun Island for fiscal years 1998, 1999 and 2000 filed with the Government of Barbados, and the notices of assessment and proofs of payment issued by the Government of Barbados to these corporations.

[7] The appellant's fiscal year ended on November 30 for each of 1998, 1999 and 2000. The words "taxable period" and "fiscal period" are analogous and the end of the "taxable period" is the end of the "fiscal period" as defined in subsection 249.1(1) of the *Act*. "Taxation year", as defined in subsection 249(1) of the *Act*, and in the case of a corporation, is a fiscal period. I agree that the end of the appellant's taxable period in each of 1998, 1999 and 2000 was on November 30 of each year. The notice of reassessment for 1998 is dated August 9, 2005 and the notices for 1999 and 2000 are dated April 13, 2006, all after the five year periods described in Article IX(3) and XXVII(3) of the Treaty.

[8] Article I of the Treaty applies "to persons who are residents of one or both of the Contracting States", that is, Canada and Barbados. This provision is identical to Article I of the current *OECD Model Convention for the Avoidance of Double Taxation with respect to Tax on Income and Capital* ("*OECD Model Treaty*").

[9] However, Article XXX(3) of the Treaty states that the Treaty excludes IBCs from the benefits of the Treaty:

This Agreement shall not apply to companies entitled to any special tax benefit under the <i>Barbados International Business Companies (Exemption from Income Tax) Act</i> , Chap. 77 or to companies entitled to any special tax benefit under any similar law enacted by Barbados in addition to or in place of that law ³ .	Le présent Accord ne s'applique pas aux sociétés ayant droit à un avantage fiscal spécial en vertu de la <i>Loi portant exonération de l'impôt sur le revenu pour les sociétés d'affaires internationales de la Barbade</i> , chap. 77 (<i>Barbados International Business Companies (Exemption from Income Tax) Act</i> , Chap. 77) ni aux sociétés ayant
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³ Sections 10 and 11 of the *International Business Companies Act* ("*IBC Act*") of Barbados are included in the Appendix to these reasons.

droit à un avantage fiscal spécial en vertu d'une loi analogue adoptée par la Barbade et qui s'ajouterait ou qui remplacerait la loi mentionnée ci-dessus.

[10] There is no question that the appellant is resident of Canada and that the Treaty applies to the appellant. An underlying issue before me is whether Sun Island Optics and Sun Island are residents of Barbados for purposes of the Treaty. The appellant says they are; the respondent says they are not.

[11] Appellant's counsel submitted that the limitation period to assess tax in Article XXVII(3) of the Treaty is a benefit available to the appellant as resident of Canada since, on the facts agreed to by the parties, the income previously reported and taxed in Barbados is the income subject to the assessments in appeal, notices of which were issued after the limitation period of five years in Article XXVII(3) of the Treaty. Thus, the reassessments ought to be vacated.

[12] Appellant's counsel analyzed Article IX of the Treaty as it relates to the facts at bar and concluded that all the conditions of Article IX are present to preclude Canada from reassessing by virtue of Article IX(3). The parties have agreed that William and Roderick Hoogstraten controlled the appellant and indirectly controlled Sun Island and Sun Island Optics⁴; this satisfies clause (b) of Article IX(1). The amounts added to the appellant's reported income were transfer pricing adjustments, the amounts of which were included in the reported income of Sun Island Optics in its 1998 and 1999 taxation years and Sun Island for its 2000 taxation year⁵; this satisfies Article IX(2).

[13] Since the purpose of the Treaty is to prevent double taxation, the appellant sees the words used in Article XXX(3) as merely preventing Barbados IBCs from obtaining benefits under the Treaty, nothing more.

[14] Counsel for the appellant sought support in the reasons of the Federal Court of Appeal in *Canada v. CanWest MediaWorks Inc.*⁶. In *CanWest*, the Court considered that Article XXX(2) of the Treaty, on its facts, would exclude a resident of Barbados from application of the Treaty. The Minister justified the reassessment against CanWest on the basis that the exclusion of the Barbados resident corporation from

⁴ Paragraphs 5(d) and (e) of the agreed facts.

⁵ Paragraphs 5(k) and (l) of the agreed facts.

⁶ 2008 FCA 5.

the Treaty was proper. Article XXX(2) allowed Canada to tax Canadian residents' foreign accrual property income ("FAPI"), as defined in the *Act*.

[15] The Court of Appeal held that notwithstanding the limitation period in the Treaty, the FAPI provision, that is, Article XXX(2), stipulates that the ability of Canada to tax FAPI inclusions in the income of Canadian residents is to be unfettered by any provision of the Treaty but concluded that the FAPI assessment does not render the limitation provision meaningless. The appellant finds comfort in the Court's view that the limitation provision "will be applicable with respect to items of income other than FAPI that have been added to the income of a resident of Canada for the purposes of the" *Act*. Appellant's counsel stated that *CanWest* is authority for the proposition that the limitation period provision of the Treaty applies to income unless otherwise excluded as, for example, FAPI.

[16] I agree with the appellant that *CanWest* is authority that the limitation period applies to all income, unless specifically excluded. However, to come within the "protection" of the limitation period in Article IX(3) the conditions of paragraph 1 of Article IX must be present, that is, there must be enterprises of both Contracting States.

[17] Appellant's counsel referred to the 1992-1997 Commentary on Article 1 of the *OECD Model Treaty*⁷ ("Commentary"), at paragraph 15 which reads in part:

Conduit situations can be created by the use of tax-exempt (or nearly tax-exempt) companies that may be distinguished by special legal characteristics. The improper use of tax treaties may then be avoided by denying the tax treaty benefits to these companies (the exclusion approach). The main cases are specific types of companies enjoying tax privileges in their State of residence giving them in fact a status similar to that of a non-resident. As such privileges are granted mostly to specific types of companies as defined in the commercial law or in the tax law of a country, the most radical solution would be to exclude such companies from the scope of the treaty. Another solution would be to insert a safeguarding clause ...

[Emphasis added in counsel's notes of argument.]

[18] In counsel for the appellant's view, the reference in the Commentary to the special treatment given to tax-exempt or nearly tax-exempt companies was that the *OECD Model Treaty* was drafted in such a fashion as only to deny IBCs treaty benefits and this, he says, is a reasonable interpretation of Article XXX(3).

⁷ *Commentary On the Model Double Taxation Convention on Income and Capital – 1992, OECD, 1996.*

[19] The respondent's position is that the limitation periods in Article XXVII(3) and Article IX(3) of the Treaty do not apply to the reassessments in issue where the appellant was transacting with IBCs.

[20] IBCs, respondent's counsel explained, are freed from normal Barbadian tax rates under the provisions of the *IBC Act* and are subjected to minimal tax (between 1 and 2.5 per cent) within Barbados⁸. This contrasts to a rate of 37.5 per cent of taxable income payable by a company that is not an IBC⁹. Also, an IBC is not subject to withholding tax on dividends paid to its shareholders. Thus, when a Canadian beneficiary owner of an IBC receives a dividend, it may apply section 113(1) of the *Act* and deduct from its Canadian taxable income dividends received out of the exempt surplus of the IBC as a foreign affiliate.

[21] Counsel for the respondent submitted that Article IX does not apply to the facts at bar. Sun Island and Sun Island Optics are IBCs that are not within the scope of the Treaty and therefore neither is "an enterprise of a Contracting State" to which the provisions of Article IX can be applied to the benefit of the appellant. In addition, her counsel adds that Article IX is a provision to prevent double taxation, that is, to tax the same profits in the hands of two different enterprises, one in Canada and the other in Barbados. Thus, if two enterprises are not covered by the Treaty, the provision does not apply.

[22] Because IBCs are excluded from the application of the Treaty pursuant to Article XXX(3) of the Treaty, it is the respondent's view that the IBCs lose the protection afforded by the Treaty. An exclusionary provision is not unusual in treaties and is directed at specific types of companies enjoying a tax privilege in their resident jurisdiction. She referred to paragraph 21 of the current version of the Commentary on Article I¹⁰:

Specific types of companies enjoying tax privileges in their State of residence facilitate conduit arrangements and raise the issue of harmful tax practices. Where tax-exempt (or nearly tax-exempt) companies may be distinguished by special legal characteristics, the improper use of tax treaties may be avoided by denying the tax treaty benefits to these companies (the exclusion approach). **As such privileges are granted mostly to specific types of companies as defined in the commercial law or in the tax law of a country, the most radical solution would be to exclude such companies from the scope of the treaty.** Another solution would be to insert

⁸ Sections 10 and 11 of the *IBC Act*: see Appendix.

⁹ Section 43(1) of the *Barbados Income Tax Act*, included in Appendix to these reasons.

¹⁰ Commentary, Condensed Version, OECD, July 17, 2008.

a safeguarding clause which would apply to the income received or paid by such companies ... :

...

The scope of this provision could be limited by referring only to specific types of income, such as dividends, interest, capital gains, or directors' fees. Under such provisions companies of the type concerned would remain entitled to the protection offered under Article 24 (non-discrimination) and to the benefits of Article 25 (mutual agreement procedure) and they would be subject to the provisions of Article 26 (exchange of information).

[Emphasis added in respondent's notes of argument]

[23] The substance of these comments is similar to the earlier Commentary referred to by the appellant's counsel in paragraph 17 of these reasons. Indeed, the essential difference is the emphasis put on the passages by each counsel.

[24] Contracting parties have a choice when negotiating a tax treaty. Respondent's counsel said the countries can opt for a radical solution of excluding companies, as was done in the Treaty, or include a safeguarding clause to permit all or certain companies to exist within the scope of the Treaty.

[25] Respondent's counsel explained that Canada and Barbados chose to exclude companies such as IBCs that would normally be considered resident in Barbados from the scope of the Treaty. IBCs, counsel repeated, are not resident of Barbados for the purpose of the Treaty and the Treaty does not apply to them: Article XXX(3). The Treaty does not offer any limited protection to IBCs; there is no safeguarding clause. An IBC is not "an enterprise of a Contracting State" for the purpose of Article IX of the Treaty.

[26] Counsel also added that to have any force or effect, Article IX requires the consideration or presence of two enterprises, one in each Contracting State. Since an IBC is excluded from the scope of the Treaty, it is not "an enterprise of a Contracting State" and the provision does not apply. Article IX is designed to assist corporations in both Canada and those in Barbados that are not IBCs, she declared.

[27] Respondent finds some comfort in the provisions of paragraph 5907(11.2)(c)¹¹ of the *Income Tax Regulations* ("*Regulations*") which grant benefits to persons who have foreign affiliates in Barbados. This provision deems a foreign affiliate not to be

¹¹ See Appendix to these reasons.

a resident of a country with which Canada has a tax treaty unless one of three conditions is met. The third condition pertains to IBCs. It applies when the foreign affiliate (the IBC) would be a resident of the treaty country but for a provision in a tax convention that provides that the convention does not apply to the foreign affiliate. Therefore, respondent's counsel concludes that Parliament is of the view that the effect of Article XXX of the Treaty is to render IBCs non-residents for purposes of the Treaty.

[28] Counsel for the appellant noted that paragraph 5907(11.2)(c) of the *Regulations* does not mention IBCs at all but is a "fairly complicated domestic tax provision" that has as its purpose an exemption from taxation of dividend income derived from active business income by a company in another jurisdiction that is a foreign affiliate. He acknowledged that the regulation applies to IBCs but that it is an admission of nothing; the regulation simply provides relief to double taxation by not taxing dividend income paid out of exempt supplies from IBCs.

[29] It is interesting that while IBCs are not mentioned specifically in paragraph 5907(11.2)(c), the description of the foreign affiliate in the opening words of the regulation and subparagraph (c) appear to meet the description of an IBC.

[30] The foundation of the appellant's submission that the Canada Revenue Agency has assessed beyond the five year period in Article IX(3) is that IBCs are enterprises and residents of Barbados for the purposes of the Treaty, except that IBCs are not entitled to the Treaty's benefits. An IBC is not a non-person when an analysis of Article IX is undertaken.

[31] If the respondent is correct that Article XXX(3) denies an IBC the status of a resident and thus an enterprise of Barbados, the appellant's submissions are not tenable.

[32] Article XXX(3) of the Treaty states that the Treaty "shall not apply" or, in French, "ne s'applique pas" to IBCs. It does not say only that the benefits of the Treaty shall not apply to IBCs, as the appellant posits.

[33] Definitions of "apply" in *The Shorter Oxford English Dictionary*, 3d ed., 1983, include:

4. To appropriate *to* ...; to put to use, dispose of ...
6. To bring (a law, list, etc.) into contact with facts, to "put into practical operation.
7. To refer ... *to* a particular instance.

8. To have a valid reference to ...

[34] *The Random House Dictionary of the English Language*, 2e ed, Random House, N.Y., 1987, defines "apply" in part:

6. to put into effect. *They applied the rules to new members only.*

[35] *Le Petit Robert 1, Dictionnaire de la langue française*, Le Robert, Paris, 1983, offers an example how "s'appliquer" may be used:

Cette remarque s'applique à tout le monde. v. Concerner, intéresser, viser.

[36] The words in Article XXX(3), then, are rather clear. From appellant's counsel's submission it appears to me that he is attempting to construe Article XXX(3) to read that "the benefits of" precede the opening words of paragraph 3 so that the paragraph (3) would read: "The benefits of this Agreement shall not apply to [IBCs] ...". It is not only the benefits of the Treaty that do not apply to IBCs but that all of the Treaty does not apply. Counsel is adding words to the Treaty.

[37] The dictionary definitions signify that the Treaty is not to be used insofar as IBCs are concerned, that the Treaty is not to be concerned with an IBC. IBCs are excluded from the provisions of the Treaty.

[38] The appellant's counsel disagreed with the respondent's position concerning Article IX. He reiterated that Article IX(1) gives a Contracting State the authority to adjust profits if subparagraphs (a) and (b) of paragraph (1) of Article IX apply and paragraph (2) then allows for the profits to be adjusted if previously reported as profits, that is, to avoid double taxation.

[39] However, appellant's counsel argued that if the respondent is correct, that IBCs are excluded from the Treaty because they are not "enterprises" of a Contracting State within the meaning of that term for the purpose of the Treaty¹², then "the logical interpretation and conclusion to draw is that Canada cannot adjust and tax the profits at all, the condition in subparagraph (a) of paragraph (1) of Article IX could never be met", that is, there is no enterprise of Barbados. Counsel stated that "the absurd result is that if the respondent's submission is correct, Canada has lost its ability to make transfer pricing adjustments". There is an enterprise of a Contracting State, Canada, but not of the other Contracting State, Barbados. He therefore proposes that an interpretation different from that of the respondent should be preferred.

¹² See Article III(1), para. (d).

[40] I do not agree with appellant's counsel. If the respondent is correct and the Treaty makes IBCs non residents and non enterprises of Barbados, Canada may still make transfer pricing adjustments in assessing a resident of Canada by applying the provisions of the *Act* itself. Canada, then, need not be concerned with the mechanics of Article IX.

[41] The reason for the time limit in Article IX(3) or, for that matter, Article XXVII(3) is not explained in the Treaty itself¹³. However, paragraph 10 of the current OECD Commentary on Article IX offers a reasonable explanation:

The paragraph also leaves open the question whether there should be a period of time after the expiration of which State B would not be obliged to make an appropriate adjustment to the profits of enterprise Y following an upward revision of the profits of enterprise X in State A. Some States consider that State B's commitment should be open-ended — in other words, that however many years State A goes back to revise assessments, enterprise Y should in equity be assured of an appropriate adjustment in State B. Other States consider that an open-ended commitment of this sort is unreasonable as a matter of practical administration. In the circumstances, therefore, this problem has not been dealt with in the text of the Article; but Contracting States are left free in bilateral conventions to include, if they wish, provisions dealing with the length of time during which State B is to be under obligation to make an appropriate adjustment

[42] Respondent's counsel also submitted that Article XXVII(3) imposes a time limit for the imposition of the same item of income by both Contracting States. Article XXVII does not apply in the appeal at bar, counsel submits, because notwithstanding that the parties have agreed that the amounts included in the appellant's income for Canadian tax purposes also had been reported as gross profits by Sun Island Optics and Sun Island to the Government of Barbados and they each paid tax on the gross profits, the income of the appellant itself had not been taxed in Barbados as contemplated by Article XXVII of the Treaty. Barbados has not taxed the appellant any income it assessed any entity in Barbados. In other words, as I understand the respondent's argument, Article XXVII would apply when the item of income is included in the income of the appellant by both Canada and Barbados.

¹³ Appellant's counsel submitted that the limitation period in Article IX(3) is to ensure that Canada reassesses on a timely basis and represents an additional method to avoid double taxation as a result of transfer pricing adjustments. He relied on the evidence of Ross John Kauffman, a witness in *CanWest* who at the time was a senior official of the Canada Revenue Agency; Mr. Kauffman did not testify at the trial of this appeal. I cannot consider evidence given in another proceeding. For one reason, the person who is not a witness at a trial cannot be cross-examined on any prior testimony.

[43] The parties have agreed that the amounts added to the appellant's reported income had been reported as gross profit to the Barbados fisc by Sun Island and Sun Island Optics and taxed by the Government of Barbados. The Government of Barbados has not charged any tax to the appellant.

[44] The appellant is of the view that it is irrelevant to determine the nature of the income given that Article XXVII applies to income generally. Its position is that the Government of Barbados has assessed income against Sun Island Optics and Sun Island and Canada is trying to assess the same income — I assume he means the same quantum of income — in the hands of the appellant.

[45] Thus, applying Article XXVII(3) of the Treaty, the appellant claims Canada, in assessing the appellant, has increased the tax base of the appellant by including income previously charged to tax in Barbados.

[46] I do not agree with the appellant's submissions. First of all, Article XXVII(3) prohibits a State from increasing a person's tax base by including items of income already charged to tax in the other State; it is not income generally. Secondly, Barbados has never charged tax to the appellant on its income. Thirdly, the word "income" and "revenu" (in the French version of Article XXVII(3)) are modified by the words "items of" in English and "éléments de" respectively. It is not income alone, or the quantum of the income, that is addressed in Article XXVII(3); it is a description of what part of income has entered into an account¹⁴ or a "partie constitutrice d'une chose",¹⁵ a constructive or essential part of a thing that is being charged to tax. It is not the general description of income but what the income is composed of, what the income is, that interests Article XXVII(3). The income may be a dividend, interest, sales, professional fees or management fees, among others.

[47] According to the income tax returns of Sun Island Optics and Sun Island, each of these corporations carried on business and earned income from sales and were charged tax on this basis by the Government of Barbados.

[48] Canada is charging tax to the appellant as management fees (Article XIII) from sources in Barbados or as business profits (Article VII) from business carried on in Barbados. The Government of Barbados has not taxed the appellant on the income it earned in Barbados, whether as management fees or business profits. The

¹⁴ *Shorter Oxford Dictionary, supra.*

¹⁵ *Le Petit Robert, Dictionnaire de la langue française, supra.*

appellant had no permanent establishment in Barbados and is therefore exempt from tax by the Government of Barbados: Article VII. In addition, if the income in dispute is management fees, neither Sun Island Optics nor Sun Island apparently paid such fees to the appellant. Canada is taxing the appellant on fees that the two Barbados companies ought to have paid to the appellant but did not. Again, the appellant was not charged tax on management fees or on any type of income by Barbados; the items of income charged to tax against the appellant by Canada are different items of income than were charged to tax to Sun Island Optics and Sun Island by the Government of Barbados.

[49] The limitation periods described in Articles IX(3) and XXVII(3) of the Treaty do not apply to the facts at bar. To answer the question of law stated in paragraph 1 of these reasons: the Minister has not issued the reassessments for 1998, 1999 and 2000 after the expiry of the applicable limitation periods. The respondent is entitled to its costs.

Signed at Ottawa, Canada, this 22nd day of July 2010.

"Gerald J. Rip"

Rip C.J.

**Appendix to Reasons for Determination
in the appeal of *Sundog Distributing Inc. v. The Queen***

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APPENDIX

Agreement Between Canada and Barbados for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital

Accord entre le Canada et la Barbade tendant à éviter les doubles impositions et à prévenir l'évasion fiscale en matière d'impôts sur le revenu et sur la fortune

Article I Personal Scope

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

Article I Personnes visées

Le présent Accord s'applique aux personnes qui sont des résidents d'un État contractant ou de chacun des deux États contractants.

Article III General Definitions

1. In this Agreement, unless the context otherwise requires:

...

(e) the terms "enterprise of a Contracting State" and "enterprise of the other Contracting State" mean respectively an enterprise carried on by a resident of a Contracting State and an enterprise carried on by a resident of the other Contracting State;

...

2. As regards the application of this Agreement by a Contracting State any term not otherwise defined shall, unless the context otherwise requires, have the meaning which it has under the laws of that Contracting State relating to the taxes which are the subject of this Agreement.

Article VII Business Profits

1. The profits of an enterprise 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. If

Article III Définitions générales

1. Au sens du présent Accord, à moins que le contexte n'exige une interprétation différente:

...

e) les expressions « entreprise d'un État contractant » et « entreprise de l'autre État contractant » désignent respectivement une entreprise exploitée par un résident d'un État contractant et une entreprise exploitée par un résident de l'autre État contractant;

...

2. Pour l'application du présent Accord par un État contractant, toute expression qui n'est pas autrement définie a le sens qui lui est attribué par la législation du présent Accord, à moins que le contexte n'exige une interprétation différente.

Article VII Bénéfices des entreprises

1. Les bénéfices d'une entreprise d'un État contractant ne sont imposables que dans cet État, à moins que l'entreprise n'exerce ou n'ait exercé son activité dans l'autre État contractant par l'intermédiaire d'un établissement stable qui

the enterprise carries on or has carried on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment.

2. Subject to the provisions of paragraph 3, where an enterprise of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein, there shall be attributed to that permanent establishment the profits which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment.

3. In the determination of the profits of a permanent establishment situated in a Contracting State, there shall be allowed as deductions all expenses which would be deductible under the law of that State if the permanent establishment were an independent enterprise insofar as such expenses are reasonably allocable to the permanent establishment including executive and general administrative expenses, so deductible and allocable, whether incurred in the State in which the permanent establishment is situated or elsewhere.

4. No profits shall be attributed to a permanent establishment by reason of the mere purchase by that permanent establishment of goods or merchandise for the enterprise.

5. For the purposes of the preceding paragraphs, the profits to be attributed to a permanent establishment shall be determined by the same method year by year unless there is good and sufficient reason to the contrary

6. Where profits include items of income which are dealt with separately in other

y et situé. Si l'entreprise exerce ou a exercé son activité d'une telle façon, les bénéfices de l'entreprise sont imposables dans l'autre État mais uniquement dans la mesure où ils sont imputables audit établissement stable.

2. Sous réserve des dispositions du paragraphe 3, lorsqu'une entreprise d'un État contractant exerce son activité dans l'autre État contractant par l'intermédiaire d'un établissement stable qui y est situé, il est imputé à cet établissement stable les bénéfices qu'il aurait pu réaliser s'il avait constitué une entreprise distincte et séparée exerçant des activités identiques ou analogues dans des conditions identiques ou analogues et traitant en toute indépendance avec l'entreprise dont il constitue un établissement stable.

3. Dans le calcul des bénéfices d'un établissement stable situé dans un État contractant, sont admises en déduction, dans la mesure où elles sont raisonnablement afférentes à l'établissement stable, toutes les dépenses qui seraient déductibles conformément à la législation de cet État si l'établissement stable était une entreprise indépendante, y compris les dépenses de direction et les frais généraux afférents et déductibles, qu'elles aient été exposées dans l'État où est situé l'établissement stable ou ailleurs.

4. Aucun bénéfice n'est imputé à un établissement stable du fait que cet établissement stable a simplement acheté des marchandises pour l'entreprise.

5. Aux fins des paragraphes précédents, les bénéfices à imputer à un établissement stable sont calculés chaque année selon la même méthode, à moins qu'il n'existe des motifs valables et suffisants de procéder autrement.

6. Lorsque les bénéfices comprennent des éléments de revenu traités séparément dans

Articles of this Agreement, then, the provisions of those Articles shall not be affected by the provisions of this Article, unless otherwise expressly provided by these Articles.

Article IX
Associated Enterprises

1. Where

- (a) an enterprise of a Contracting State participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State, or
- (b) the same persons participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State,

and in either case conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly.

2. Where profits on which an enterprise of a Contracting State has been charged to tax in that State are also included in the profits of an enterprise of the other Contracting State and taxed accordingly, and the profits so included are profits which would have accrued to that enterprise of the other State if the conditions made between the enterprises had been those which would have been made between independent enterprises, then the first-mentioned State shall make an appropriate adjustment to the amount of tax charged on those profits in the first-mentioned State. In determining such an adjustment due regard

d'autres articles du présent Accord, les dispositions de ces articles ne sont pas affectées par les dispositions du présent article à moins que ces articles ne prévoient expressément le contraire.

Article IX
Entreprises associées

1. Lorsque

- a) une entreprise d'un État contractant participe directement ou indirectement à la direction, au contrôle ou au capital d'une entreprise de l'autre État contractant, ou que
- b) les mêmes personnes participant directement ou indirectement à la direction, au contrôle ou au capital d'une entreprise d'un État contractant et d'une entreprise de l'autre État contractant

et que, dans l'un et l'autre cas, les deux entreprises sont, dans leurs relations commerciales ou financières, liées par des conditions acceptées ou imposées, qui diffèrent de celles qui seraient convenues entre des entreprises indépendantes, les bénéfices qui, sans ces conditions, auraient été obtenus par l'une des entreprises mais n'ont pu l'être en fait à cause de ces conditions, peuvent être inclus dans les bénéfices de cette entreprise et imposés en conséquence.

2. Lorsque des bénéfices sur lesquels une entreprise d'un État contractant a été imposée dans cet État sont aussi inclus dans les bénéfices d'une entreprise de l'autre État contractant et imposés en conséquence, et que les bénéfices ainsi inclus sont des bénéfices qui auraient été réalisés par cette entreprise de l'autre État si les conditions convenues entre les deux entreprises avaient été celles qui auraient été fixées entre des entreprises indépendantes, le premier État procédera à un ajustement correspondant du montant de l'impôt qu'il a perçu sur ces bénéfices. Pour déterminer l'ajustement à faire, il sera tenu

shall be had to the other provisions of this Agreement in relation to the nature of the income.

3. A Contracting State shall not change the profits of an enterprise in the circumstances referred to in paragraph 1 after the expiry of the time limits provided in its national laws and, in any case, after five years from the end of the year in which the profits which would be subject to such change would have accrued to an enterprise of that State. This paragraph shall not apply in the case of fraud, wilful default or neglect.

Article XXVII
Mutual Agreement Procedure

1. Where a resident of a Contracting State considers that the actions of one or both of the Contracting States result or will result for him in taxation not in accordance with this Agreement, he may, without prejudice to the remedies provided by the national laws of those States, address to the competent authority of the Contracting State of which he is a resident an application in writing stating the grounds for claiming the revision of such taxation. To be admissible, the said application must be submitted within two years from the first notification of the action which gives rise to taxation not in accordance with this Agreement.

2. The competent authority referred to in paragraph 1 shall endeavour, if the objection appears to it to be justified and if it is not itself able to arrive at an appropriate solution, to resolve the case by mutual agreement with the competent authority of the other Contracting State, with a view to the avoidance of taxation not in accordance with this Agreement.

3. A Contracting State shall not, after the expiry of the time limits provided in its

compte des autres dispositions du présent Accord relatives à la nature du revenu.

3. Un État contractant ne rectifiera pas les bénéfices d'une entreprise dans les cas visés au paragraphe 1 après l'expiration des délais prévus par sa législation nationale et, en tout cas, après l'expiration de cinq ans à dater de la fin de l'année au cours de laquelle les bénéfices qui feraient l'objet d'une telle rectification auraient été réalisés par une entreprise de cet État. Le présent paragraphe ne s'applique pas en cas de fraude, d'omission volontaire ou de négligence.

Article XXVII
Procédure amiable

1. Lorsqu'un résident d'un État contractant estime que les mesures prises par un État contractant ou par chacun des deux États entraînent ou entraîneront pour lui une imposition non conforme au présent Accord, il peut, sans préjudice des recours prévus par la législation nationale de ces États, adresser à l'autorité compétente de l'État contractant dont il est un résident, une demande écrite et motivée de révision de cette imposition. Pour être recevable, ladite demande doit être présentée dans un délai de deux ans à compter de la première notification de la mesure qui entraîne une imposition non conforme au présent Accord.

2. L'autorité compétente visée au paragraphe 1 s'efforce, si la réclamation lui paraît fondée et si elle n'est pas elle-même en mesure d'apporter une solution satisfaisante, de régler la question par voie d'accord amiable avec l'autorité compétente de l'autre État contractant, en vue d'éviter une imposition non conforme au présent Accord.

3. Un État contractant n'augmentera pas la base imposable d'un résident de l'un ou l'autre

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.

4. The competent authorities of the Contracting States shall endeavour to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of this Agreement. In particular, the competent authorities of the Contracting States may consult together to endeavour to agree:

(a) to the same attribution of profits to a resident of a Contracting State and its permanent establishment situated in the other Contracting State;

(b) to the same allocation of income between a resident of a Contracting State and any associated person provided for in Article IX.

5. The competent authorities of the Contracting States may consult together for the elimination of double taxation in cases not provided for in this Agreement.

Article XXX
Miscellaneous Rules

1. The provisions of this Agreement shall not be construed so as to restrict in any manner any exclusion, exemption, deduction, credit, or other allowance now or hereafter accorded

(a) by the laws of one of the Contracting States in the determination of the tax imposed by that Contracting State, or

(b) by any other agreement between the

État contractant en y incluant des éléments de revenu qui ont déjà été imposés dans l'autre État contractant, après l'expiration de cinq ans à dater de la fin de la période imposable au cours de laquelle les revenus en cause ont été réalisés. Le présent paragraphe ne s'applique pas en cas de fraude, d'omission volontaire ou de négligence.

4. Les autorités compétentes des États contractants s'efforcent, par voie d'accord amiable, de résoudre les difficultés ou de dissiper les doutes auxquels peuvent donner lieu l'interprétation ou l'application du présent Accord. En particulier, les autorités compétentes des États contractants peuvent se consulter en vue de parvenir à un accord:

a) pour que les bénéfices revenant à un résident d'un État contractant et à son établissement stable situé dans l'autre État contractant soient imputés d'une manière identique;

b) pour que les revenus revenant à un résident d'un État contractant et à toute personne associée visée à l'article IX soient attribués d'une manière identique.

5. Les autorités compétentes des États contractants peuvent se concerter en vue d'éviter la double imposition dans les cas non prévus par le présent accord.

Article XXX
Dispositions diverses

1. Les dispositions du présent Accord ne peuvent être interprétées comme limitant d'une manière quelconque les exonérations, abattements, déductions, crédits ou autres allègements qui sont ou seront accordés

a) par la législation d'un État contractant pour la détermination de l'impôt prélevé par cet État, ou

b) par tout autre accord intervenu entre les

Contracting States.

États contractants.

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*.

2. Aucune disposition du présent Accord ne peut être interprétée comme empêchant le Canada de prélever son impôt sur les montants inclus dans le revenu d'un résident du Canada en vertu de l'article 91 de la *Loi de l'impôt sur le revenu* du Canada.

3. This Agreement shall not apply to companies entitled to any special tax benefit under the Barbados *International Business Companies (Exemption from Income Tax) Act*, Chap. 77 or to companies entitled to any special tax benefit under any similar law enacted by Barbados in addition to or in place of that law.

3. Le présent Accord ne s'applique pas aux sociétés ayant droit à un avantage fiscal spécial en vertu de la *Loi portant exonération de l'impôt sur le revenu pour les sociétés d'affaires internationales de la Barbade*, chap. 77 (*Barbados International Business Companies (Exemption from Income Tax) Act*, Chap. 77) ni aux sociétés ayant droit à un avantage fiscal spécial en vertu d'une loi analogue adoptée par la Barbade et qui s'ajouterait ou qui remplacerait la loi mentionnée ci-dessus.

4. The competent authorities of the Contracting States may communicate with each other directly for the purpose of applying this Agreement.

4. Les autorités compétentes des États contractants peuvent communiquer directement entre elles pour l'application du présent Accord.

International Business Companies Act of Barbados

10.(1) Subject to this section and section 11, in lieu of tax at the rate specified under the *Income Tax Act*, there shall levied and paid to the Commissioner of Inland Revenue, in respect of the income year 1991 and in each subsequent income year of an international business company, a tax on the profits and gains of the company at the following rates

- (a) 2.5 per cent on all profits and gains up to \$10 000 000;
- (b) 2 per cent on all profits and gains exceeding \$10 000 000 but not exceeding \$20 000 000
- (c) 1.5 per cent on all profits and gains exceeding \$20 000 000 but not exceeding \$30 000 000
- (d) one per cent on all profits and gains in excess of \$30 000 000.

(2) An international business company may elect to take a credit in respect of taxes paid to a country other than Barbados provided that such an election does not reduce the tax payable in Barbados to a rate less than one per cent of the profits and gains of the company in any income year.

(3) An international business company all of whose shares form part of the assets of a trust described in section 105 of the *Off-shore Banking Act*, shall not be subject to tax under that section

or under the *Income Tax Act* on the profits and gains of that company if it is managed by an off-shore bank and if its activities are restricted to engaging exclusively in the business of buying, selling, holding or managing securities.

11. An international business company shall not be liable to pay any tax under the *Income Tax Act* except as is provided by section 10 hereof in respect of an income year, nor shall it be liable under this or any other enactment to pay any other direct tax on its profits and gains in respect of that income year.

Income Tax Act of Barbados

43(1) Subject to this Act, with effect from the income year 2002, the tax payable by a company upon its taxable income is 37.5 per cent of every complete dollar of that taxable income.

(2) With effect from income year 2003, the tax payable by a company upon its taxable income is 36 per cent of every complete dollars of that taxable income.

(3) With effect from income year 2004, the tax payable by a company upon its taxable income is 33 per cent of every complete dollars of that taxable income.

(4) With effect from income year 2005, the tax payable by a company upon its taxable income is 30 per cent of every complete dollars of that taxable income.

(5) With effect from income year 2006, the tax payable by a company upon its taxable income is 25 per cent of every complete dollars of that taxable income.

Regulations to the Income Tax (Canada)
Règlements de l'impôt sur le revenu (Canada)

5907(11.2) For the purposes of this Part, a foreign affiliate of a corporation is, at any time, deemed not to be resident in a country with which Canada has entered into a comprehensive agreement or convention for the elimination of double taxation on income unless

(a) the affiliate is, at that time, a resident of that country for the purpose of the agreement or convention;

(b) the affiliate would, at that time, be a resident of that country for the purpose of the agreement or convention if the affiliate were treated, for the purpose of income taxation in that country, as a body corporate;

(c) where the agreement or convention entered into force before 1995, the affiliate would, at that time, be a resident of that country for the purpose of the agreement or convention but for a provision in the agreement or convention that has not been amended after 1994 and that provides that the agreement or convention does not apply to the affiliate; or

(d) the affiliate would, at that time, be a resident of that country, as provided by paragraph (a), (b) or (c) if the agreement or convention had entered into force.

5907(11.2) Pour l'application de la présente partie, une société étrangère affiliée d'une société est réputée, à un moment donné, ne pas résider dans un pays désigné, sauf dans le cas où, pour l'application de l'accord ou de la convention visé au paragraphe (11) et intervenu entre le Canada et ce pays :

a) la société affiliée réside dans le pays désigné à ce moment;

b) la société affiliée résiderait dans le pays désigné à ce moment si elle était considérée comme une personne morale aux fins de l'impôt sur le revenu de ce pays;

c) dans le cas où l'accord ou la convention est entré en vigueur avant 1995, la société affiliée résiderait dans le pays désigné à ce moment si ce n'était une disposition de l'accord ou de la convention -- qui n'a pas été modifiée après 1994 -- selon laquelle elle est exclue de son application;

d) la société affiliée résiderait dans le pays désigné à ce moment, ainsi qu'il est prévu aux alinéas a), b) ou c), si l'accord ou la convention était entré en vigueur.

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HER MAJESTY THE QUEEN

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REASONS FOR
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APPEARANCES:

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