Canadian Tax Highlights

Editor: Vivien Morgan, LL.B.

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Danish Holdco on Hot Seat

In recent times, Danish holdcos have been particularly popular for holding investments in non-EU countries. (See "Danish Holdco," *Canadian Tax Highlights*, September 27, 1999, at 70.) On November 10, 2000, a new Danish tax bill proposed a 25 percent Danish withholding tax on dividends paid to a resident of a non-EU country that does not have an income tax treaty with Denmark. Although the tax was originally intended to be effective for dividend distributions after 2000, Danish tax authorities indicate privately that the effective date will be sometime in the first half of 2001 if the legislation is adopted by then.

Currently, dividends from a foreign sub to a Danish holdco are not taxed in Denmark if they are received in a 12-month period during which the holdco owns at least 25 percent of the sub's shares and the sub's activities do not attract CFC taxation. Nor is there withholding on dividends paid by the holdco if they were declared during a similar period and degree of ownership by the foreign parent, regardless of its residence or the existence of a relevant treaty. There is no capital gains tax on the holdco's sale of its sub's shares held for at least three years—unless the sub is taxed at a low rate (normally less than 24 percent) and engages mainly in financial activities—nor is there capital duty on holdco's formation or on a contribution of capital.

The proposal to withhold tax on outbound dividends is aimed at distributions to offshore companies resident in non-treaty countries such as Bermuda, the Cayman Islands, and the Bahamas. Dividends from a Danish holdco to, say, a Canadian corporation will enjoy continued exemption from Danish withholding tax, but US check-the-box entities may create issues. For example, if a US corporation owns shares in a non-treaty-country entity that is disregarded and treated as a part of the US entity for US tax purposes, and that entity holds shares in a Danish holdco, arguably the US-Denmark treaty provides a withholding tax exemption on dividends to the entity because they are considered paid to a US person (article 4(1)(d)). However, Danish government sources suggest that Danish withholding tax may apply if the intermediary entity is a reverse hybrid, such as a Dutch CV.

The OECD and the EU have attacked many tax regimes as harmful tax practices. The report of the EU Council of Economic Finance Ministers' Primarolo group, released in March 2000, included the Danish holding company regime in a list of harmful tax practices. The OECD's June 2000 report did not include holding company regimes on its list, but its position on this issue has not yet crystallized. Denmark's proposal was purportedly bowing to criticism from several EU countries and may augur other countries' following suit with legislation designed to appease the OECD's or the EU's concerns. Such changes are just one more reminder to consider exit strategies before a structure is established.

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Directors' Defence Narrowed?

The taxpayers won the battle, but Revenue may have won the war in *Worrell*, a recent directors' liability decision that may expunge a well-established line of defence for non-remittance of employee source deductions and GST.

The taxpayers were inside directors of an established company in a construction-related industry in the Toronto area. In an attempt to remedy financial difficulties it was suffering during the last recession, the company engaged a consultant with considerable success in assisting similar companies in financial difficulty. The consultant confirmed that the company could be revived quickly with an injection of new capital. In spite of an apparently successful meeting with the bank following the dishonouring of a remittance to Revenue, the bank dishonoured another remittance cheque. The bank then began to scrutinize the company's financial health and assumed de facto control over the company's finances, exercising

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its discretion in honouring cheques, including the remittance cheques that the company continued to issue. After six months the consultant had not produced an investor acceptable to the bank; the bank called the company's loans and forced it into bankruptcy.

Revenue assessed the directors personally under subsection 227.1(1) for failure to remit the employer portions of CPP and UI and GST that was not recoverable from the company. Before *Worrell*, some lower court decisions held that a director's defences to such an assessment included a defence that he or she did not have de facto control over the company's finances at the time of the failure. *Robitaille* was the leading case on the de facto defence: the FCTD concluded that the directors were not liable if the bank had taken control of the company's finances, because the exercise of a director's freedom of choice over company finances was essential in order to establish the director's personal liability under subsection 227.1(1). The TCC in *Worrell* absolved the directors because they did not have de facto control of the company's finances during the period of failed remittances and because they also exercised due diligence ([1990] 1 CTC 121 and 98 DTC 1783, respectively).

The FCA rejected that reasoning, saying that the words of subsection 227.1(1) do not contemplate a de facto control precondition and such should not be read into the statutory text approved by Parliament. To do so could absolve directors who continue business operations without any reasonable chance of preventing nonremittance and without regard to how long failure to remit continued. Furthermore, the FCA said that the due diligence defence was broad enough to protect "directors who have acted with propriety in attempting to prevent defaults by their company." The FCA emphasized that the due diligence defence only operates to protect a director who takes reasonable care to prevent a failure to remit, and does not protect a director who makes a reasonable business decision to carry on business because the recovery of financial health will allow catch-up remittances. "[I]t is no defence for the directors to say that the risk they took would have been taken by a reasonable person." "Taxpayers are not required involuntarily to underwrite this risk, no matter how reasonable it may have been from a business perspective for the directors to have continued the business without doing anything to prevent future failures to remit."

The saving grace in *Worrell* appears to be the short tether that the directors had on the situation, reinforced by the consultant's reassurance that the business could be quickly turned around and the continuing issuance of remittance cheques that were occasionally honoured by the bank. For the brief period before bankruptcy it was reasonable for the directors to believe that the company's fortunes could be turned around quickly and the bank would then honour its next remittance cheque.

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Unfinished Business

The numerous proposals consequential on the new capital gains inclusion rate do not address certain inequities both in the recapture mechanism for allowable business investment losses (ABILs) in the capital gain exemption (CGE) rules and in the taxation of capital gains and qualifying stock option benefits for alternate minimum tax (AMT) purposes.

Before using their CGEs, taxpayers who have already claimed an ABIL may need to recapture an amount in excess of the original business investment loss. For example, an individual who realized a $1,000 business investment loss (a $750 ABIL) in 1995, with no other gains or losses since, must realize a capital gain in excess of $1,500 (a $750 taxable capital gain) in 2001 to access his remaining CGE.

Another concern relates to the taxation of capital gains and stock option benefits for individuals qualifying for full deductions under paragraph 110(1)(d) or (d.1). Currently, taxpayers who realize capital gains or stock option benefits but have little other income may be subject to AMT. After the capital gain inclusion rate dropped to 50 percent and the said deductions were adjusted accordingly, the effective top marginal basic federal tax rate applicable to such gains and benefits became 14.5 percent, lower than the AMT rate of 17 percent in 2000, 16 percent in 2001, et seq. Although corrective measures are not contained in the December 21, 2000 draft legislation, the backgrounder indicates that the AMT inclusion rate for capital gains is 80 percent, not 100 percent. Similarly, 40 percent of the stock option deduction claimed in calculating regular income tax on taxable stock option benefits is deductible in calculating AMT taxable income in order to arrive at a net inclusion rate of 80 percent. These inclusion rates, effective for 2000 et seq., result in an effective federal AMT rate of 13.6 percent in 2000 (12.8 percent in 2001 and future years) for capital gains and qualifying stock option benefits, lower than the effective 14.5 percent federal regular tax rate.

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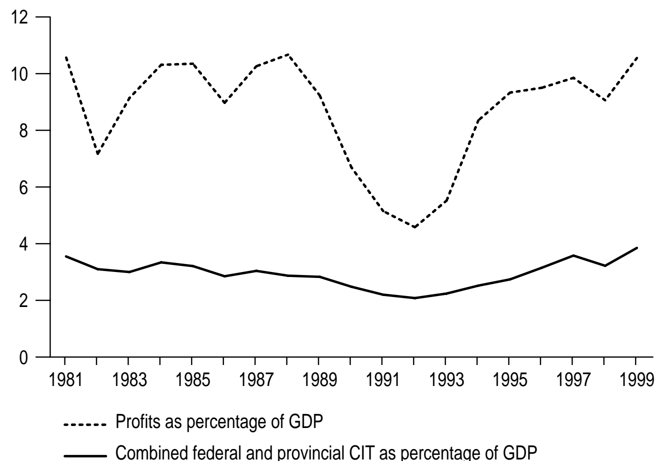
Simple Patterns

Recent numbers from Statistics Canada show that the ratio of federal and provincial corporate income tax to aggre-

gate operating profit increased from 17.3 percent in 1994 to 20.0 in 1998. This is a significant increase, but it is not the first time that the ratio has risen over a relatively short period. The new figures, however, may reflect basic changes in the taxation of profits.

The chart shows that profits have a definite cyclical pattern, reaching a high of nearly 11 percent of GDP in good times and falling during recessions. In 1981 profits fell from 10.6 percent of GDP to 7.2 percent in 1982. In 1988, the ratio hit a high of 10.7 percent, but fell to 4.6 percent in 1992 during the depths of the recession.



Corporate income tax followed the same trend: it fell from 3.6 percent of GDP in 1981 to only 3.1 percent the next year, but jumped from 33 percent of profits to 43 percent. The most recent recession experience shows corporate income taxes dropping to 2.1 percent of GDP in 1992 before rising to nearly 3.9 percent in 1999, the highest ratio since 1975. The chart shows that taxes follow the same pattern as profits in relation to GDP. But the relationship between taxes and profits has changed in the last four years. In the past, as the economy moved out of recession and into recovery, taxes declined relative to profits as defined in Statistics Canada's national accounts. During the latest recovery, however, taxes rose from a post-recession low of 29 percent of profits in 1995 to nearly 37 percent in 1999.

Details of corporate financial and taxation results have not yet been released for 1998 and 1999, but the chart clearly supports the StatsCan summary figures referred to in the opening paragraph. The tax reform exercise of 1988, straddled by a series of base-broadening measures, widened the tax net and increased the effective rate of tax on profits. Losses resulting from the deep 1991 recession delayed the recognition of the change that is only now evident.

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Canadian Targetco

The relative weakness of the Canadian dollar, coupled with geographic proximity to the United States, has made Canadian private and public companies attractive acquisition targets for US companies. Following are some salient points to consider in structuring such acquisitions.

■ A US limited liability company (LLC) should not act as the purchaser of a Canadian business. Revenue takes the position that an LLC is not entitled to the Canada-US treaty's capital gains exception, the reduction in withholding tax, or the permanent establishment requirement for the taxation of business profits in Canada.

■ It is generally preferable to operate a Canadian business through a Canadian subsidiary rather than a branch, which attracts both corporate tax and the 5 percent branch tax on profits over $500,000.

■ A Canadian acquisition company should be formed as the vehicle to purchase a Canco's shares or assets. Using a Canadian acquisition company permits the US purchaser to invest in a combination of shares and debt. The purchase price may subsequently be repaid free of withholding tax. The amount invested in a subscription for shares of the acquisition company may be repaid as a reduction of capital without attracting Canadian withholding tax.

■ Canada's thin capitalization rules operate to deny the interest deduction if the debt-to-equity ratio of a specified non-resident exceeds 2:1. A 10 percent withholding tax applies on interest paid to a US shareholder.

■ A US purchaser may take advantage of the US same-country related-party exception. The US purchaser and a US affiliate form a Canadian partnership and elect to treat it as a corporation for US tax purposes. Funds may be invested as capital contributions into the Canadian partnership, which loans funds to the target. Interest subsequently paid to the partnership is deductible to the Canadian borrower (subject to thin capitalization and other interest capitalization restrictions) and is not taxable to the US partners. A 10 percent Canadian withholding tax applies.

■ If the acquisition company is funded in part with debt, the target may be wound up into or amalgamate with it, making the interest expense deductible against operating profits.

■ A Nova Scotia unlimited liability company (NSULC) is a useful entity for Americans: it is regarded as a corporation for Canadian tax purposes and ignored for US tax purposes or treated as a partnership if there is more than one shareholder. It can be used as the acquisition company. Because a shareholder's liability is unlimited on an NSULC's dissolution, a US S corporation, C corporation, or limited partnership may own the NSULC shares; the first may be preferable because it provides limited liability and qualifies for the Canadian 5 percent dividend withholding tax.

■ An NSULC is also useful if the Canadian vendor wishes to sell shares and the US purchaser wishes to acquire assets. The target is converted to an NSULC either immediately before or after the acquisition by continuing under the laws of Nova Scotia and amalgamating with an NSULC. Because the amalgamation is treated as a liquidation for US tax purposes, there is a step-up in basis of the assets for US tax purposes that may permit the US purchaser to write off over 15 years the acquired goodwill of the Canadian business. If the amalgamation occurs after the target's acquisition, a US Code section 338 election may be filed to bump the assets' bases.

■ A Canadian shareholder currently does not benefit from a tax-deferred transfer on an exchange of shares of a Canco for a USco; the October 2000 federal mini-budget indicates that Revenue is considering an amendment to permit such transfers. Until then, the use of a Canadian exchangeable share may afford the Canadian shareholders a tax deferral until a share sale triggered by an exchange. The Canadian shareholders acquire exchangeable shares in a Canco, either on an exchange of common shares of the target, on a transfer of common shares to a new Canadian holdco, or on an amalgamation. The exchangeable shares mirror or track the US acquiror's shares. The Canadian shareholders take advantage of a domestic rollover and defer Canadian tax until the exchange.

■ An acquisition of a Canco results in a change of control, triggering a deemed year-end and affecting loss carryforwards, reserves, etc.

■ On a purchase of assets of a Canadian business, the vendor should participate in an election under section 167 of the Excise Tax Act to avoid GST.

■ Reasonable management fees may be paid by the target to the US purchaser. The fees are deductible in Canada and not subject to Canadian withholding tax. Canadian form T106 must be filed to report non-arm's-length cross-border fees.

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ONTARIO PROFESSIONAL CORPS

Ontario's Bill 152, introduced November 30, 2000, implements its 2000 budget proposal to allow regulated professionals to incorporate. The changes come into force on a date to be proclaimed.

Like their peers in Alberta and other provinces, certain Ontario professionals will be able to incorporate and enjoy many of the tax and non-tax advantages enjoyed by other self-employed individuals, such as claiming or sharing the small business deduction, allowing partners of multi-jurisdictional partnerships the option of sourcing all their income to their province of residence and paying tax only there, and determining a most beneficial salary-dividend mix. Professionals claiming the 10-year reserve for 1995 stub period income must consider incorporation's impact on the reserve.

A schedule to Bill 152 amends a number of statutes to permit incorporation of certain regulated professionals—lawyers, chartered accountants, certified general accountants, members of the regulated health professions, social workers and social service workers, and veterinarians. Regulations to the Ontario Business Corporations Act (OBCA) will permit the naming of other eligible professions. The Architects Act already allows architects and professional engineers to incorporate.

The regulation of the practice of professional corporations is left to the bylaws and regulations under each act, but every professional corporation must comply with Bill 152's amendments to the OBCA. For example, issued and outstanding shares must be legally and beneficially owned, directly and indirectly, by one or more members of the same profession; voting and shareholder agreements attempting to circumvent this requirement are void. All officers and directors of the corporation must also be shareholders. The corporate name must include the words "Professional Corporation" and cannot be a number name. The articles of incorporation must provide that the corporation may not carry on a business other than the practice of the profession, but not to the exclusion of activities related or ancillary to the profession, such as temporary investment of surplus funds earned. More than one shareholder is allowed, but multidisciplinary professional corporations are not permitted. As announced in the budget, incorporation does not limit the shareholders' professional liability.

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TAKEOVER COSTS

In the course of a takeover, the bidder often incurs substantial costs relating to acquisition of the target's shares, including fees paid to investment-banking institutions that specialize in giving general investment and deal-structuring advice. It is an interesting question whether fees paid for such services are deductible under paragraph 20(1)(bb) as investment counsel fees.

In *Symes*, the SCC observed that in a deductibility analysis "one's first recourse is to subsection 9(1) which embodies . . . a form of 'business test' for taxable profit" determined in accordance with "well accepted principles of business practice." This analysis is carried on simultaneously with a paragraph 18(1)(a) analysis: many of the

rules in section 18 are merely "analytically repetitive or confirmatory of prohibitions already embodied in subsection 9(1)." Costs incurred by the bidder that relate to the acquisition of a target's shares should normally satisfy subsection 9(1) because they are made for the purpose of earning income from property—future dividends from the target or a new corporation merging the target's and bidder's profitable operations. However, paragraph 18(1)(b) precludes a deduction for capital expenditures incurred to acquire or establish an asset of enduring benefit, and the amount of the capital expenditures must be added to the shares' cost base. Nonetheless, section 20 allows deductions for certain capital expenditures.

Provided that fees are reasonable and paid to a person whose principal business is advising others in respect of specified activities, a taxpayer may deduct fees (other than commissions) paid for advice on buying or selling a specific share or security of the taxpayer or for the administration or the management of the shares or securities of the taxpayer. "Shares of the taxpayer" in this context is generally regarded as meaning shares owned by the taxpayer rather than shares of its capital stock. Revenue says that generally a lawyer or accountant cannot meet the advisory principal business test vis-à-vis advice in respect of buying and selling shares etc., and fees paid for general investment financial counselling or planning are ineligible. Revenue regards administration and management of securities activities as including custodial services, accounting record maintenance, and collection and remittance of income if the principal business test is met. Fees paid to a stockbroker are generally not deductible under paragraph 20(1)(bb) if its principal business is not that of advising others regarding the buying and selling of stock and securities, but its main business may in fact be portfolio and administrative services.

It appears that fees paid by a bidder to an investment bank are deductible if they relate to the provision of advice as to the advisability of purchasing the target's shares and the principal business test is met. Otherwise, deductible fees that are not commissions are not disallowed solely because they are determined or computed with reference to the fair market value of a portfolio at a particular time. It should follow that success fees paid by bidders warrant similar treatment if the fees are within market norms. Some practitioners argue that fees paid to an investment banker by a bidder for negotiation and deal structuring should also be deductible because they are in respect of administering or managing shares owned by the taxpayer: the courts have said that the words "in respect of" must be given their widest possible meaning. Once a function has been labelled in a certain way, it sometimes takes a seismic shift in thinking to see the function's true import for tax purposes.

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US Tax Certificates

Many executors of Canadian estates are unaware that they must obtain IRS transfer certificates before selling US securities. Without a certificate, US corporations or transfer agents that sell US stocks and securities in the name of a non-resident decedent face liability for taxes and penalties and may thus be unwilling to accommodate an executor's request for a sale. The requirements and procedures can be cumbersome and time-consuming—and inconvenient when time is of the essence in a falling market—but planning opportunities exist.

To secure transfer certificates, an executor must list all the US securities of a non-resident non-US citizen in his or her US estate tax return on form 706-NA, due nine months after death. The transfer certificates are usually issued when the executor receives an estate tax closing letter indicating approval of the form; the executor may then provide them to the US corporation or transfer agent and direct the sale of the securities.

JEFF MACNELLY'S SHOE by Chris Cassatt and Gary Brookins

The IRS will issue transfer certificates before the estate tax closing letter, but only to allow the sale of specific securities necessary to pay estate tax, and will direct the corporation or transfer agent to release the funds only to the IRS. The executor must supply the IRS with the total value of the estate, a list of securities to be sold, and an estimate of the estate tax liability. The executor should plan on a two- to three-week turnaround from the IRS. Transfer certificates may be obtained by writing to Geoffrey C. Thomas, Esq., Internal Revenue Service, Office of Compliance (International), 950 L'Enfant Plaza SW, Washington, DC 20024; enclosing a return Federal Express envelope will expedite return receipt. The regs also empower the issue of transfer certificates for particular securities before the estate tax return's approval if the estate gives sufficient security as the IRS determines case by case.

There are two exceptions to the transfer certificate requirements: for US non-resident non-citizen decedents with US property valued at less than US$60,000 and for property administered by an executor or an administrator appointed, qualified, and acting within the United States. Canadians who hold substantial US securities may appoint a US co-executor or administrator, giving executors the ability to sell securities sans transfer certificates immediately upon that appointment. Additional potential commission costs of a US executor or administrator may be limited under the will.

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Ontario Tables Budget Bill

Ontario's new Bill 152 implements most measures remaining from its 2000 budget. Ontario also announced a change to the budget's proposed capital gains inclusion rate reduction for individuals and corporations—a reduction from 66.67 percent to 62 percent for 2001 and to 50 percent by 2004. A December 4, 2000 economic statement announced that the 50 percent capital gains inclusion rate in the October 18, 2000 federal mini-budget also applies for Ontario purposes, effective on that date.

Personal income tax changes. Ontario's 2000 budget proposed indexation of its tax brackets, surtax levels, and credits for 2001 and subsequent taxation years. The Bill 152 formula to determine the indexation factor is similar to the federal formula: the percentage change in the average inflation rate for the 12 months ending September 30 of the previous year relative to the preceding 12 months. Ontario will use a provincial, not a federal, consumer price index (CPI), yielding a higher 2001 Ontario indexation factor of 2.7 percent rather than the federal 2.5 percent. After indexation the 2001 thresholds for the two-tier surtax are set at 20 percent of the Ontario tax exceeding $3,560 ($3,466 indexed) and 36 percent of the tax exceeding $4,491 ($4,373 indexed).

Ontario research employee stock option "tax overpayment." Under the terms of the tax-on-income systems that all the provinces are implementing and under the federal-provincial tax collection agreement, the provinces (except Quebec) cannot allow an individual to calculate a provincial taxable income that differs from the federal. Because, as indicated in the December economic statement, the federal government did not agree to administer at a "fair and reasonable cost" the stock option incentive that Ontario had originally proposed as a deduction in its 2000 budget, Ontario will implement the incentive in the unusual form of a "tax overpayment." Under the new and complicated mechanism, for stock option agreements entered into after royal assent of Bill 152, a qualifying individual must calculate an Ontario "adjusted tax amount" on actual taxable income net of a deduction as was proposed. Excess Ontario tax otherwise payable is refunded as a tax overpayment. The deduction under this mechanism is the lesser of (1) $100,000 and (2) the section 7 stock option benefit less any paragraph 110(1)(d) or (d.1) deduction or the taxable capital gain from the disposition of shares so acquired. Eligible employees must be full-time or permanent part-time for at least six months, part of which falls in the year when the option is granted. Furthermore, their percentage of R & D "work-time"—the number of hours spent directly undertaking or supervising R & D in Ontario—and their percentage of R & D wages in the company's eligible R & D expenditures must be at least 30 percent. An eligible employer corporation must carry on R & D through an Ontario permanent establishment and have eligible R & D expenditures, for the taxation year before the year when the stock option agreement was made, of at least the lesser of $25 million and 10 percent of its revenue.

The provincial minister must approve the incentive for each employee and employer. The employer must apply for a certificate by the due date of its tax return for the year the stock option agreement was made; the employee must apply on or before September 30 of the second calendar year after the year to which the overpayment relates. It appears that the refund claim is approved and administered in Ontario and is not part of the regular T1 return; further announcements may clarify the working details of this cumbersome tax-overpayment mechanism.

Other measures. The bill also allows small businesses with gross revenue and total assets not exceeding $1.5 million to use the short-form corporations tax return for taxation years ending after 2000; amends the Employer Health Tax Act for certain stock option benefits; enacts the educational technology tax incentive; enhances and simplifies the Ontario film and television tax credit and the

Ontario production services tax credit; amends the Ontario book publishing tax credit and the Ontario interactive digital media tax credit; and extends the M & P credit to corporations that generate electrical energy for sale or produce steam for such use.

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Stock Option Terminated

The FCA recently held in *Buccini* that a payment received in compensation for the termination of a stock option agreement was not taxed, inter alia, as a disposition of the rights under such an agreement.

The taxpayer's employer, a public corporation, granted him an option to acquire 5,000 of its shares, to vest after two years of continuous employment. Nearly one year later, the employer amalgamated under an agreement that unilaterally terminated all employee options. The taxpayer took the position in his 1983 return that the settlement payment he received was not taxable. Revenue included the amount in income as proceeds for the disposition of the taxpayer's rights under the stock option agreement (paragraph 7(1)(b)); as an employment benefit (paragraph 6(1)(a)); as consideration for entering into a contract of employment (subsection 6(3)); or as a capital gain from the disposition of capital property. The TCC held that the amount could not reasonably be regarded as a windfall, and was taxable under paragraph 7(1)(b). In obiter, the TCC said that if that provision did not apply, the receipt would have been a capital gain (99 DTC 242).

The FCA said that paragraph 7(1)(b) did not apply. Based on *Bernier*, the unilateral repudiation of the option agreement was a fundamental breach of contract that terminated it immediately: signing a release could thus not have disposed of rights under the agreement as required by that paragraph. Subsection 6(1) did not apply: based on *Atkins*, damages for a breach of an employment contract are not taxable as employment benefits. Nor did the payment meet the conditions of subsection 6(3). The FCA ordered Revenue to reassess on the basis that none of those provisions applied. In contrast to the TCC, it appears that neither capital gains nor windfall treatment was argued, and the FCA did not address either issue (2000 DTC 6053 (FCA) and 76 DTC 6258 (FCA), respectively).

The basis for the direction to reassess is unclear, but capital gains treatment might be expected to apply: it was the only basis for the original assessment not rejected by the FCA. Paragraph 110(1)(d), which now effectively reduces the taxable amount of certain stock option benefits to capital gain levels, was not enacted at the relevant time in *Buccini*; the then capital gains inclusion rate of 50 percent provided strong motivation to avoid paragraph 7(1)(b) treatment. Today such motivation might not exist unless the taxpayer had capital losses. It is not yet known whether the Crown will appeal *Buccini*.

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Good for the Goose

Laws are frequently drafted so broadly that the true underlying tax policy principles are not readily apparent. Perhaps as a result, it sometimes seems that each litigant's focus is on winning without regard to those principles or to the technical issues. The taxpayer must clearly present the facts and reasons of its case, and Revenue must vigorously defend its interpretation of the law; but once a court has ruled, its decisions should be accepted unless an appeal is launched. Without well-researched and clearly articulated facts and arguments, a judge may come to the wrong decision. Two recent cases before the TCC dealing with tuition fees paid to the same post-secondary training institution illustrate that the administration of our tax laws is not always perfect.

In both cases Revenue argued that the tuition paid was not creditable for tax purposes because the location where the institution offered the courses was not certified by the minister of human resources (MHR). In *East*, heard on August 31, 2000, the judge noted that the Act only requires that the institution be certified, even though the MHR appeared to be attempting to limit certification to four locations of the institution exclusive of Calgary, where the taxpayer was enrolled. "There is nothing in the statute that talks about location . . . the Minister has no authority to limit the institution as to where [it teaches] the course." Regarding the relevant tax policy, the judge said, "It must be obvious to every living soul in the country that it is of benefit to the country as a whole for people to be upgraded in this day and age of marching technology and to find gainful employment. This is the reason and purpose of this section so that tax relief can be given to those people that have the courage, the gumption, the knowledge and the ability to upgrade themselves . . . . Why the Minister is even challenging this man's tax return is beyond me. Why the Minister would take the narrow position that the institution is only certified in certain areas, is beyond me. It is not fair, it is not just and it is not right."

Crown counsel was aware of the reasons in *East*—they were given orally from the bench—yet in November 2000, Revenue presented the same argument in *Kiprenko*, which involved the same institution, and convinced a different judge that it was not certified. It is clear that the court in *Kiprenko* received incomplete information. The taxpayer—unrepresented by counsel—did not present the principles in his favour that informed the *East* case.

Readers are invited to submit ideas or written material to *Canadian Tax Highlights*. Please write to Vivien Morgan in care of the Canadian Tax Foundation.

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It appears that Revenue pursued the matter in spite of knowing of the finding in *East* two months earlier; it also appears that the Crown did not inform the court, or perhaps even its own counsel, of that decision. One must assume that Crown counsel would have informed the court of the earlier case had he known of it: solicitors are officers of the court as well as representatives of their clients, and may be held accountable for misleading the court. Apart from the injustice perpetrated on the individual taxpayer, who creates a sympathetic picture, the taxpayers footing the bill for the Crown and for the entire process may be concerned about the less than optimal disposition of these matters. Perhaps a suggestion of an advisers' penalty for administrators might draw attention to reparable weaknesses in the system.

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Accounting for Tax Cuts

After a post-election meeting, the CICA Emerging Issues Committee revised its position: the October 2000 federal mini-budget proposals are considered substantively enacted from December 13, 2000, when the government announced that it would reintroduce related legislation. Relevant measures include corporate rate reductions of 1 percent in 2001 and 2 percent in each of 2002, 2003, and 2004. (See "Accounting for Tax Cuts," *Canadian Tax Highlights*, December 27, 2000, at 91.)

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Foreign Tax News

Australia

The treasurer released exposure drafts for the proposed new business tax system and for the uniform capital allowance (UCA) system; both systems are effective July 1, 2001. The new business tax system is a consolidation regime for corporate groups headed up by Australian entities that are not subs of Australian entities and not subject to any concessionary taxing regime. Once an irrevocable election to consolidate is made, the group is treated as a single entity; intragroup transactions are ignored; the group files a single tax return and pays consolidated instalments; assets, losses, franking credits, and foreign tax credits are pooled; the nature of transactions is determined by the overall group profile; and the overall tax liability is the head entity's responsibility. The UCA replaces 37 existing regimes; comments are requested by January 29, 2001.

OECD

On December 22, 2000, the Committee on Fiscal Affairs adopted changes to the model treaty commentary on article 5 dealing with the permanent establishment definition in the context of e-commerce. Donald J. Johnston will serve a second five-year term as secretary general. The **Slovak Republic** became an OECD member on December 14, 2000. (See "Foreign Tax News," *Canadian Tax Highlights*, September 26, 2000, at 72.) On January 8-9, 2001 in Barbados, senior policy makers from OECD members and Caribbean financial centres met for high-level consultations on tax and competition issues to develop universal measures to stem harmful tax practices.

Ireland

The 2001 budget reduces personal tax rates by 2 percent and VAT rates by 1 percent; removes the income limit for employer and self-employed social insurance contributions; implements final steps of a full tax credit system for personal income tax; accelerates a 12.5 percent tax rate for small companies' profits; shortens the tax life of plant machinery from seven to five years; and forecasts the likelihood of further VAT reductions.

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Canadian Tax Foundation, Toronto

NEW ON THE WEB

In February 2001, the Foundation's Web site (www.ctf.ca and www.acef.ca) will have a new look. In addition, some sections of the site will be accessible only by member ID and password. If you have not received an e-mail from the Foundation with your member ID and password, please contact Norma Forrester (nforrester@ctf.ca).

The audio presentation of the December 5, 2000 Breakfast Catch-Up is now available for purchase. Topics include Mini-Budget Impact, Joint Committee Update, Tax Harmonization Project, and Recent Cases.

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