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Her Majesty the Queen (Appellant) v. MIL (Investments) S.A. (Respondent)

2007 DTC 5437

Federal Court of Appeal

June 13, 2007

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Court File No. A-416-06

Capital gains — Treaty exemptions from tax — General anti-avoidance rule ("GAAR") — Whether corporate taxpayer's capital gain on sale of shares of public corporation to another public corporation was exempt from tax under Canada–Luxembourg Tax Convention — Income Tax Act, R.S.C. 1985, c. 1 (5th Supp.), ss. 18.1(4), 245(1), 245(2), 245(3), 245(4), 245(5), 248(10) — Convention between Canada and the Grand Duchy of Luxembourg for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and on Capital, Articles 13(1), 13(4), 13 (5), 13(6).

Relying on the GAAR, the Minister assessed the corporate taxpayer, a non-resident corporation, for 1997 for tax on a capital gain realized by it on the sale of its shares of a public corporation ("DFR") to another public corporation following a bidding war. On its appeal to the Tax Court of Canada, the taxpayer argued that the assessed capital gain was exempt from tax under Article 13 of the Canada–Luxembourg Tax Convention (the "Treaty"). In allowing the taxpayer's appeal (2006 DTC 3307), the Tax Court concluded, in part, that the taxpayer's sale of its shares of DFR was not part of a series of transactions, and had a genuine purpose, so that an abuse analysis was not necessary. The Crown appealed to the Federal Court of Appeal.

Held: The Crown's appeal was dismissed. Evidence was put forward by both parties on the "series of transactions" issue. This made it unlikely that the Tax Court judge made a palpable and overriding error on this issue. It was not necessary to make a finding on this issue because the Crown's appeal would fail given the lack of evidence that the tax benefit received by the taxpayer was an abuse or misuse of the provisions of the Act or the Treaty. The Minister was ordered to reassess on the basis that the capital gain realized by the taxpayer on the sale of its DFR shares was exempt from tax under the Treaty.

Counsel: R. Carvalho for the appellant; W.J.A. Mitchell for the respondent.

Before: Décary, Sexton, and Pelletier, JJ.A.

PELLETIER, J.A. (orally for the Court):

[1] In order to succeed in this appeal, the appellant Her Majesty the Queen must persuade us that one transaction in the series of transactions in issue is an avoidance transaction, and that the tax benefit achieved by the respondent MIL (Investments) S.A. is an abuse or misuse of the object and purpose of article 13(4) of the *Convention between Canada and the Grand Duchy of Luxembourg for the Avoidance of Double Taxation and the Prevention of fiscal Evasion with respect to Taxes on Income and on Capital* (the Tax Treaty).

[2] The Tax Court judge found that the series of transactions consisted of the respondent's sale of 703,000 shares of Diamond Fields Resources Ltd. (DFR), the payment of the Final Dividend (as described in the Tax Court judge's reasons) and the continuance of the respondent as a Luxembourg corporation. The Tax Court judge found that the respondent's August 1996 sale of its remaining shares in DFR was not part of the series because "at the end of the series of transactions, DFR management, including co-chairman Boulle (the directing mind of the respondent) and therefore the appellant [respondent in the **[2007 DTC 5437 at 5438]** appeal] had no intention of selling": Reasons for

Decision, at para. 67.

[3] The appellant's task has been made easier by the respondent's admission that its continuance as a Luxembourg corporation was an avoidance transaction. As a result, and even though the Tax Court judge found that the respondent's August 1996 sale of its shares in DFR was not, in and of itself, an avoidance transaction, the tax benefit which the respondent ultimately obtained following that sale may be subject to the General Anti-Avoidance Rule (GAAR) if the sale was part of the series of transactions or was undertaken in contemplation of the series of transactions.

[4] Counsel for the appellant and counsel for the respondent, each in their turn, took us to the evidence in support of their position. The fact that there is evidence in support of each side's position makes it unlikely that the Tax Court judge's conclusion was the result of a palpable and overriding error.

[5] We do not have to answer that question as we are of the view that the appeal would fail in any event as we are unable to see in the specific provisions of the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) (the Act) and the Tax Treaty to which we were referred, interpreted purposively and contextually, any support for the argument that the tax benefit obtained by the respondent was an abuse or misuse of the object and purpose of any of those dispositions.

[6] It is clear that the Act intends to exempt non-residents from taxation on the gains from the disposition of treat exempt property. It is also clear that under the terms of the Tax Treaty, the respondent's stake in DFR was treaty exempt property. The appellant urged us to look behind this textual compliance with the relevant provisions to find an object or purpose whose abuse would justify our departure from the plain words of the disposition. We are unable to find such an object or purpose.

[7] If the object of the exempting provision was to be limited to portfolio investments, or to non-controlling interests in immoveable property (as defined in the Tax Treaty), as the appellant argues, it would have been easy enough to say so. Beyond that, and more importantly, the appellant was unable to explain how the fact that the respondent or Mr. Boulle had or retained influence of control over DFR, if indeed they did, was in itself a reason to subject the gain from the sale of the shares to Canadian taxation rather than taxation in Luxembourg.

[8] To the extent that the appellant argues that the Tax Treaty should not be interpreted so as to permit double non-taxation, the issue raised by GAAR is the incidence of Canadian taxation, not the foregoing of revenues by the Luxembourg fiscal authorities.

[9] As a result, the appeal will be dismissed with costs.

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