Tax Topics

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FOCUS ON CURRENT CASES

This is a regular monthly feature examining recent cases of special interest, coordinated by Ron Dueck of Dentons Canada LLP. The contributors to this feature are from Dentons Canada LLP, Montréal, Toronto, Calgary, Edmonton, and Vancouver.

His Majesty The King v. Margo Dianne Bowker, 2023 DTC 5049 (Federal Court of Appeal)

Introduction & Background

On June 8, 2023, the Federal Court of Appeal ("FCA") allowed the Minister of National Revenue's (the "Minister's") appeal from the Tax Court's decision *Bowker v. The Queen*,[1] setting aside said decision and returning the matter to the trial judge for a fresh determination of the costs payable to the respondent Margo Dianne Bowker (the "Taxpayer").

The Minister reassessed the Taxpayer's 2010 taxation year under the *Income Tax Act*[2] ("ITA"), disallowing losses and imposing a gross negligence penalty of $139,032.00. The Taxpayer's appeal of the penalty at the Tax Court was allowed, and the Taxpayer was awarded costs in the amount of $149,842.22.

In determining the costs, the Tax Court:

(1) found that partial indemnity costs in this case should fall in the range of 50% to 75%[3] of the Taxpayer's actual legal expenses, for consistency purposes;

(2) relied on the Taxpayer's success in persuading the Tax Court that she was not grossly negligent as a factor that could be taken into consideration which might favour an increase in the Taxpayer's costs based on Rule 147(3) of the *Tax Court of Canada Rules (General Procedure)*[4] (the "TCC Rules");

(3) concluded, after analyzing paragraph 162(7)(*b*) of the ITA and determining that the Taxpayer's offer to settle with the Minister was principled, that the Minister's failure to accept the Taxpayer's offer of settlement was a factor that justified an increase in costs; and

(4) found that the Minister's pre-litigation conduct was a factor that justified an increase in costs.

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[1] *Bowker v. The Queen* (2022), 2022 DTC 2041 (CCI), additional reasons to *Bowker v. The Queen* (2021), 2021 DTC 2042 (CCI), rendered by the honourable Sylvain Ouimet of the Tax Court of Canada.

[2] *An Act respecting Income Taxes*, RSC, 1985, c. 1 (5th Supp.), as amended.

[3] This range was discussed in *Guibord v. R.*, 2012 DTC 5030 (FCA).

[4] SOR/90-688a.

Wolters Kluwer

Issues

The issues before the FCA were whether the trial judge at the Tax Court erred:

(1) by fettering its discretion in deciding *a priori* that the costs should fall within a given range;

(2) in its treatment of three factors which are to be considered in the award of costs, namely the result of the proceeding, any settlement offer, and pre-litigation conduct which prolonged the proceedings; and

(3) in breaching the parties' right to procedural fairness in considering a factor that the parties had not raised in their submissions, without giving the parties the chance to make representations on that factor in coming to its conclusion.

Decision

The following findings were made by the FCA.

(1) **Range of costs:** The selection of a range of 50% to 75% for costs was made by the Tax Court in the name of consistency, but sources cited by the Tax Court showed no consistency and it was not demonstrated that the amount which it awarded was consistent with what had been done in other cases. A decision as to an appropriate award of costs must be grounded in the Tax Court's past practice and jurisprudence. A review of like cases undertaken after the Tax Court had addressed the various factors may have pointed to the possibility of a lower range, and the fact that the possibility of a lower range was precluded by the approach taken by the Tax Court is an indicator that the Tax Court had fettered its discretion and, in doing so, erred in law.

(2) **Result of the proceeding:** After establishing that the range of partial indemnity was 50% to 75% of a party's solicitor-client costs, the Tax Court reviewed the factors listed in Rule 147(3) of the TCC Rules, beginning with the factor found at Rule 147(3)(*a*) of the TCC Rules: the result of the proceeding. The FCA found that the Tax Court erred in awarding costs on the basis of the result of the proceeding and then enhancing those costs on the same basis. The FCA considered it to be double counting the same factor, and that the Tax Court therefore erred in law in defining the scope of said factors.

(3) **Settlement offer:** The Taxpayer's settlement offer was not a principled offer in the sense that it was not one which the Minister could accept, because notwithstanding the broad words of paragraph 162(7)(*b*) of the ITA, the operation of the paragraph is limited to obligations to file returns and provide information as and when it is required. This means that it would not apply to the situation where returns were filed when required but were negligently prepared. That being the case, the Taxpayer's settlement proposal was not one which the Minister could have accepted under paragraph 162(7)(*b*) of the ITA. As a result, failure to accept the offer of settlement was a neutral factor in the determination of the appropriate award of costs (and could not be considered a factor in supporting the increase in costs under Rule 147(3)(*d*) of the TCC Rules). The Tax Court's conclusion that the failure of the Minister to accept the offer of settlement of the Taxpayer justified an increase in costs contained an extricable error of law, namely the scope of section 162(7)(*b*) of the ITA, and was therefore reviewable on the standard of correctness.

(4) **Right to procedural fairness:** The Tax Court breached the parties' right to procedural fairness in not giving them notice of its intention to address pre-litigation conduct as a factor in awarding costs under Rule 147(3)(*g*) of the TCC Rules, which deprived the Minister of the opportunity to bring relevant facts to the Tax Court's attention. The FCA also noted that pre-litigation conduct is not a stage *in* the "proceeding," a defined term at Rule 2 of the TCC Rules, which means "an appeal or reference." While the issue of pre-litigation conduct was but one of several factors which the Tax Court considered in awarding costs, it was one of a smaller number of factors weighing heavily in favour of increased costs.

Conclusion

Amongst other considerations, such as the Tax court's use of discretion under Rule 147 of the TCC Rules, the FCA found that the trial judge had breached the parties' right to procedural fairness in failing to give them notice of its intention to address pre-litigation conduct as a factor in awarding costs.

In addition, the FCA found that the Tax Court also erred in law in fettering its discretion as to the range of partial indemnity costs, the effect of success at trial, and its conclusion that the Taxpayer's offer to settle was principled. The Minister's appeal was allowed with costs, the Tax Court's judgment was set aside, and the FCA returned the matter to the trial judge for a fresh determination of the costs payable to the Taxpayer.

— *Victor Qian and Marc Lesage*

Chen v. Canada, 2023 GTC 1008 (Federal Court of Appeal) — A Bare Trustee Purchaser of Newly Built Residential Property Without Beneficial Interest Constitutes a "Particular Individual" Within the Meaning of Subsection 254(2) of the *Excise Tax Act*

Background

When Ms. Chen was trying to purchase a newly-built residential property to live in, she was not able to get financing for the balance of the purchase price owed on the home. The financial institutions she contacted required that more people be added to the title of the new home. Ms. Chen asked her godparents to be added to the title and when they agreed, Ms. Chen was able to obtain financing. When Ms. Chen purchased the newly-built home, she applied for a $24,000 GST/HST rebate in relation to her purchase. The Minister of National Revenue (the "Minister") dismissed the application on the ground that the conditions set out in subsection 254(2) of the *Excise Tax Act* (the "ETA") for the new housing rebate were not met. Specifically, the Minister argued that Ms. Chen's godparents formed, with Ms. Chen, the "particular individual" referred to in paragraphs 254(2)(*a*), (*b*), and (*g*) of the ETA and were required to meet the preconditions set out in the provisions. The Minister held that Ms. Chen was not eligible for the new housing rebate since the godparents were not related to Ms. Chen, had no intention of occupying the newly-acquired house as their primary residence, and never occupied it when possession was granted.

Tax Court Decision

Ms. Chen appealed the Minister's reassessment to the Tax Court of Canada. She argued that her godparents should be excluded from the definition of "particular individual" such that she was the only "particular individual" within the meaning of subsection 254(2). In particular, Ms. Chen contended that a bare trust was created when she and her godparents signed a declaration of trust prior to the closing of the purchase agreement in relation to the new home. She claimed that her godparents held their interest in the property solely in their capacity as bare trustees for her. Ms. Chen argued that the bare trust agreement excluded her godparents from qualifying as "particular individuals" in relation to the property.

The Tax Court dismissed Ms. Chen's appeal. The Court held that it was bound by the decision of the Federal Court of Appeal in *Canada v. Cheema* (2018 GTC 1008).

Canada v. Cheema

In *Cheema*, Mr. Cheema and his friend signed an agreement of purchase and sale of a newly-built property. The friend of Mr. Cheema signed the purchase and sale agreement solely to assist Mr. Cheema in obtaining mortgage financing. Mr. Cheema acquired a 99% interest in the property and the friend acquired a 1% interest. A bare trust agreement was signed which stated that the 1% interest was held in trust for Mr. Cheema. Mr. Cheema applied for the new housing rebate, but the Minister reassessed him to deny the application. The Minister held that the application failed to meet the preconditions for the new housing rebate. One precondition at issue was paragraph 254(2)(*b*), which states that the "particular individual" must acquire the property for use as the primary place of residence of the particular person. The Minister claimed that the friend was also a "particular individual" with Mr. Cheema within the meaning of subsection 254(2), and because the friend did not intend to occupy the purchased property as his primary place of residence, the precondition of the rebate was not met.

In the Tax Court of Canada in *Cheema*, the trial judge found that the friend was an agent of Mr. Cheema as evidenced by the bare trust agreement. The Court found that the friend was a bare trustee and had no interest *per se* in the property itself. As such, the Court held that the friend was not a "particular individual" for the purposes of subsection 254(2). Because Mr. Cheema had satisfied the preconditions in subsection 254(2), the Court held that he should be qualified for the new housing rebate.

The Federal Court of Appeal in *Cheema* was a 2-1 split decision. The majority disagreed with the Tax Court and held that the rebate should be denied. The majority noted that section 254 sets out preconditions, written in very precise wording, for any taxpayer to claim the new housing rebate. Paragraph 254(2)(*b*) states that the "particular individual" must acquire the property for use as the primary place of residence of the particular person. The majority stated that when a supply of property is made to two or more individuals, the refence to "a particular individual" in section 254 must be read as references to all the individuals. Since the agreement of purchase and sale indicated that the supply of property was made to both Mr. Cheema and his friend, the preconditions in section 254 must be satisfied by both of them. Because the friend failed to use the property as his primary place of residence, the majority held that paragraph 254(2)(*b*) was not satisfied, thereby disqualifying Mr. Cheema from the rebate.

Mr. Cheema contended that the Court should have regard to the bare trust agreement which evidenced that the friend held his ownership interest in trust for the taxpayer. However, the majority stated that paragraph 254(2)(*b*) was written in a way that makes the bare trust relationship between the taxpayer and the friend irrelevant. In the majority's view, what was relevant for rebate purposes was the relationship between the purchaser and the builder of the new home, not the relationship between co-purchasers. As such, the majority held that the bare trust agreement was irrelevant for subsection 254(2) purposes.

On the other hand, the dissenting opinion held that the bare trustee factor should not be ignored for the purposes of subsection 254(2). The dissent stated that a "particular individual" for the purposes of subsection 254(2) should be an individual that actually receives the beneficial ownership or possession from the builder of the residential unit. The dissent stated that a co-purchaser of the newly-built home who does not acquire a beneficial interest in the home should not be a "particular individual" for the purposes of subsection 254(2). Because the friend of the taxpayer was merely a bare trustee who held the interest of the property for Mr. Cheema, the dissent held that the friend should not be a "particular individual". As such, the dissent held that Mr. Cheema should be entitled to the rebate as he met all the preconditions in subsection 254(2).

Back to *Chen v. Canada*

Although the Tax Court of Canada in *Chen* found Ms. Chen's circumstances regrettable and unfortunate, it felt bound by the majority's decision in *Cheema*. The Court held that Ms. Chen's godparents were "particular individuals" for the purposes of subsection 254(2) and that they failed to meet the requirements of paragraph 254(2)(*b*) as they did not acquire the property with the intention of using it for their primary place of residence. As such, the Court dismissed Ms. Chen's appeal.

Federal Court of Appeal Decision

Ms. Chen appealed to the Federal Court of Appeal. Ms. Chen claimed that the Tax Court erred in concluding her godparents were "particular individuals" for subsection 254(2) purposes. She also argued that the Tax Court committed a reviewable error by dismissing her appeal while acknowledging that the intent of section 254 was to help persons like her.

The Federal Court of Appeal held that Ms. Chen's appeal should be dismissed as the decision made by the majority in *Cheema* was conclusive regarding the issues she raised. The Court held that as a result of the principle of horizontal *stare decisis*, which states that future panels of an appellate court are bound by prior decisions of a panel of that court, the Court must follow the majority decision in *Cheema*. The Court noted that a panel may overrule a prior decision of another panel only when the previous decision is "manifestly wrong, in the sense that the Court overlooked a relevant statutory provision, or a case that ought to have been followed." It was up to Ms. Chen to persuade the Court that the majority decision in *Cheema* was manifestly wrong.

However, the Federal Court of Appeal found that Ms. Chen failed to demonstrate that the majority decision in *Cheema* was manifestly wrong. Ms. Chen argued that the majority's decision in *Cheema* was undermined by the amendments that were made in the ETA in 2021. The Court held that the majority's reasons in *Cheema* were not undermined by those amendments because *Cheema* was decided in light of the law as it applied at the time of the decision. Moreover, the Court did not find any error in the majority's interpretation of subsection 254(2) that would justify the Court in overruling the decision.

The Federal Court of Appeal in *Chen* also held that the Tax Court did not commit a reviewable error in dismissing the appeal while acknowledging that Ms. Chen was someone who the legislation was intended to benefit. While the Tax Court expressed sympathy to Ms. Chen, it was fully aware that it cannot allow the rebate to extend beyond the meaning and wording of the section. The Federal Court of Appeal held that it was not an error for the Tax Court to express sympathy to Ms. Chen in the judgment. In the end, the Federal Court of Appeal dismissed Ms. Chen's appeal.

Conclusion

The Tax Court of Canada and Federal Court of Appeal both held that a bare trustee who purchases a newly-built residential property in his or her capacity as a bare trustee with no beneficial interest in the property may constitute a "particular individual" for the purposes of subsection 254(2) of the ETA. Unless all particular individuals, including any bare trustee purchasers, can satisfy the preconditions in subsection 254(2), the new housing rebate application will be dismissed.

— *Shinjin Kang*

Royal Bank of Canada v. Commissioners for His Majesty's Revenue and Customs [2023] EWCA Civ 695 (England and Wales Court of Appeal) — An Interpretation of What Constitutes Income From "Immovable Property" for the Purposes of the UK/Canada Double Tax Convention

Background

Royal Bank of Canada ("RBC"), acting through its head office in Canada, lent monies to a Canadian oil company, Sulpetro Ltd. ("Sulpetro"), which, through its UK subsidiary, extracted oil from the Buchan Field in the UK pursuant to a licence granted to the UK subsidiary by the Crown.

Sulpetro subsequently went into receivership, and by virtue of the liquidation of its assets, BP Petroleum Development Ltd. (and subsequently Talisman Energy Inc.) were required to make certain contractual payments to Sulpetro in respect of oil produced and sold by them that was extracted from the Buchan Field (the "Royalties"). The right to receive the Royalties was eventually assigned to RBC as Sulpetro's creditor by a court order. On receipt of the Royalties, the Respondents (His Majesty's Revenue & Customs) contended that RBC was taxable in the UK as the recipient of income from "immovable property" in the UK.

Issue and Decision

RBC made a number of submissions through the various levels of courts that presided over this matter, but the primary issue that was required to be addressed was the proper interpretation of Article 6 of the UK/Canada Double Tax Convention (the "Treaty") with respect to the Royalties.

More precisely, the England and Wales Court of Appeal (the "Court") had to decide whether the Royalties constituted income from "immovable property" as that term is defined in Article 6(2) of the Treaty.

The Court relied on the Vienna Convention to guide its interpretation of the Treaty, which generally requires that Article 6 of the Treaty be examined in the context of:

(1) the purpose of the Article,

(2) the text of both operative languages,

(3) the Treaty as a whole, and

(4) international tax principles.

In accordance with the forgoing, the Court considered Article 13 of the Treaty, which deals with the taxation of capital gains. Article 13 differentiates between two types of gains — paragraph 13(1) applies to the taxation of gains from the alienation of immovable property, and paragraph 13(4) applies separately to the taxation of gains from the alienation of rights and licences to drill for oil, or the right to assets produced by such activities. Therefore, it should, according to the Court, follow that all or at least some of the assets listed in paragraph 13(4) would not otherwise fall within the definition of immovable property in paragraph 13(1). This differentiation was crucial to the decision because the Court found that the source of the Royalties was more closely aligned with those assets described in paragraph 13(4), so to include that source in the definition of immovable property for the purposes of Article 6 would render Article 13(4) meaningless (a result that should be avoided when interpreting the Treaty).

In addition to Article 13, the Court also focused on the French version of the Treaty, and found that the choice of language in that version of the Treaty (although not given any greater weight than the English version) did not support the narrow construction of Article 6 that the Respondent was attempting to impose, but instead was more aligned with RBC's interpretation.

Conclusion

In conclusion, applying the above interpretation to the facts, the Court held that RBC never held an interest in the Buchan Field, and therefore the Royalties could not be taxable under Article 6 of the Treaty. RBC only held a contractual right to receive payments calculated by reference to the sale proceeds derived from sales of oil, and that does not meet the definition of income from immovable property for the purposes of the Treaty.

— *Keaton Buchberger*

Amex Bank of Canada v. The King, 2023 GTC 14 (Tax Court of Canada) — Financial Institution Not Entitled To Claim Input Tax Credits on Expenses Incurred in Connection With Loyalty Program

On June 27, 2023, the Tax Court of Canada ("TCC") ruled[1] that Amex Bank of Canada ("Amex") was not entitled to claim back the goods and services tax/harmonized sales tax ("GST/HST") it paid on its expenses arising in connection with the administration and operation of its Membership Rewards Program as input tax credits ("ITCs"), including expenses incurred for providing rewards to its members upon the redemption of points ("MRP Expenses").

Issue

The key issue in this decision was whether the MRP Expenses, including the payment for travel certificates, had been incurred by Amex in the course of a commercial activity.

Indeed, under subsection 169(1) of the *Excise Tax Act* ("ETA"), a registrant is entitled to claim ITCs only to the extent that the expenses are incurred for consumption, use, or supply in the course of a commercial activity, which excludes the making of exempt supplies of financial services. Similarly, one of the conditions that must be met for a registrant to be able to claim ITCs under subsection 181(5) of the ETA is that the payment must have been made in the course of a commercial activity.

Factual Background[2]

Amex operated a Membership Rewards Program ("MRP") during its 2002 to 2012 annual reporting periods (the "Relevant Periods"). Amex was registered for GST/HST purposes during the Relevant Periods.

Amex issued American Express charge cards and credits cards (collectively, "Cards") to members of the public ("Cardholders"). Under the MRP, Cardholders accrued points for eligible purchases made with their Cards.

The MRP was exclusively available to Cardholders, offering various benefits and rewards to members of the MRP ("Members"). Some Cards automatically enrolled Cardholders into the MRP without any additional fee ("MRP-Inclusive Cards"), while others ("MRP-Extra Cards") provided the option to join the program by paying an enrollment fee ("MRP Enrollment Fee") (the MRP-Inclusive Cards and the MRP-Extra Cards are collectively referred to as "MRP Cards"). Amex charged GST/HST on the MRP Enrollment Fee. Furthermore, the Members had the option to pay an extra points accelerator fee allowing members to earn points at an accelerated rate ("Points Accelerator Fee"). Amex also charged Members GST/HST on the Points Accelerator Fee.

Members could redeem their accumulated points for various rewards, such as airline tickets, hotel stays, restaurant meals, gift cards, and tangible items ("Rewards"). Amex determined the number of points required for each Reward, and Members could purchase additional points for a fee ("Points Fee") if they didn't have enough for a specific Reward. Amex charged GST/HST on the Points Fee.

Amex entered into Participation Agreements with suppliers of various Rewards ("Participants"). Amex paid negotiated amounts to the Participants for the Rewards offered, and the Participants charged Amex GST/HST on their supplies used as Rewards ("Participant Costs").

Amex also entered into Participation Agreements ("ACI Participation Agreements") with Amex Canada Inc. ("ACI"). Under the ACI Agreements, Members could exchange their accumulated points for travel certificates of fixed face values (e.g., $100, $500). Members could use these travel certificates with ACI or ACI-franchised travel agencies to pay for travel products or services, with Amex paying ACI for the redeemed certificates ("Travel Certificate Payments"). Throughout the Relevant Periods, Amex and ACI were member of a "closely-related group" (as that term is defined in the ETA) and were parties to an election under section 150 of the ETA.

[1] *Amex Bank of Canada v. The King*, 2023 GTC 14.

[2] Amex and the Minister of National Revenue filed a Partial Agreed Statement of Facts, which was reproduced by The Honourable Justice Robert J. Hogan in his reasons.

Amex earned substantial revenue, primarily from credit card and charge card operations, with interest income, transaction charges, and discount revenue being the largest revenue sources.[3] The redemption of MRP points was recorded as an expense on Amex's income statement, and reserves were set aside on Amex's balance sheet to cover the estimated cost of future MRP points redemption.

In its GST/HST returns for the Relevant Periods, Amex claimed ITCs on the GST/HST paid on its overhead costs and Participant Costs based on the percentage of the MRP-Extra Cards to the total of all MRP Cards issued. In addition, Amex claimed ITCs under subsection 181(5) in respect of GST/HST ("NITCs") that it was deemed to have paid in respect of the Travel Certificate Payments.

Parties' Positions

Amex argued that it provided multiple supplies, some taxable and others exempt, and all the GST/HST paid on the MRP Expenses was incurred in the course of making taxable supplies, distinct from the exempt supplies made to its Cardholders.

On the other hand, the Minister of National Revenue argued that the MRP Expenses, including those related to purchasing Rewards, formed a single composite supply, the predominant element of which was an exempt "financial service".

Decision and Analysis

The first consideration of the TCC was whether Amex incurred the MRP Expenses in the course of a single composite supply made to its Members or in the course of distinct taxable supplies. If, indeed, the MRP Expenses were incurred in the course of making a single composite supply, the second consideration was to determine the predominant element of such single composite supply.

The TCC agreed that that the determination of whether a recipient receives a single supply or multiple supplies must be determined from the standpoint of the recipient of the supply.

Single Supply versus Multiple Supplies

In order to determine whether Amex made a "single composite supply" or multiple supplies, the TCC applied the "composite supply test" which examines whether an alleged separate supply is an integral part of the overall supply by assessing the degree of interconnection and interdependence between the elements or components of the supply.

The TCC closely examined the MRP terms and conditions to ascertain the relationship between the MRP and Amex's credit card business. It noted that while someone can be a Cardholder without MRP membership, the reverse is not possible. Indeed, becoming a Member is directly linked to holding an MRP Card and the MRP and points are intended exclusively for a Cardholder's benefit and use. Points are earned based on the MRP Card's usage, and Amex generates significant merchant discount revenue from these transactions.

The TCC stated that the multiple components of the supply made by Amex to a Member, notably extending credit to Cardholders, which is an exempt "financial service", and the accumulation of points were closely intertwined and linked.

The TCC also concluded that it was clear that Amex incurred the MRP Expenses to increase the volume of credit card transactions. Where a Cardholder spends more money by using an MRP Card, the Cardholder will earn more points and Amex will earn a greater amount of merchant discount revenue, which should be the commercial efficacy of the arrangement.

Addressing Amex's claims about other elements (e.g., MRP Enrollment Fee, Points Accelerator Fee) constituting separate taxable supplies, the court rejected them, stating that they are closely tied to the obtaining of Rewards by Members.

The TCC also reviewed the accounting treatment of the MRP Expenses by Amex, as it is based on the commercial reality of the components or elements of a single composite supply. It concluded that all the elements and components of the MRP were inherently intertwined and connected with the exempt supply of financial services made by Amex to its Members and merchants, notably because the MRP fees (i.e., the MRP Enrollment Fee and Points Accelerator Fee) represented less than 0.4% of Amex's total revenue.

Determination of the Predominant Element of the Single Composite Supply

Having concluded that the supply made by Amex to the Cardholders was a single composite supply, the TCC now had to determine what the predominant element was. By applying the two-prong test established by the Federal Court of Appeal ("FCA") in *Global Cash Access (Canada) Inc.*,[4] the TCC concluded that the predominant element of the single

[3] Revenue from MRP fees accounted for less than 0.75% of Amex's total revenue in 2009 and 2010.

[4] 2013 GTC 1030.

composite supply made by Amex was the extension of credit by Amex to a Member. Indeed, the commercial efficacy of the supply, from the Cardholder's perspective, is credit which is interest-free (provided the full amount of the monthly bill is paid on time) that allows the MRP Cardholders to procure goods and services without using cash savings or borrowing funds from a different source.

As the MRP Expenses were not incurred in the course of a commercial activity but rather in the course of making exempt supplies of financial services, subsection 169(1) of the ETA could not find application and therefore, Amex was not entitled to claim back the GST/HST it paid on the MRP Expenses as ITCs.

NITCs

With respect to the NITCs provided in subsection 181(5) of the ETA, the TCC concluded that, as the Travel Certificate Payments were incurred in respect of a liability that arose because of the single composite supply of an exempt financial service, Amex was not entitled to claim any NITCs.

Alternative Arguments of Amex

Lastly, the TCC rejected the alternative arguments of Amex that exclusionary paragraph (*r*.5) of the definition of "financial service", sections 138 and 139 of the ETA should apply.

Free Supplies of Rewards

Amex also argued that the "free supply rule" under subsection 141.01(4) of the ETA should find application with respect to the supply of Rewards in the MRP. Amex claimed that the Rewards are provided for no consideration, making it a free supply, and thus, they were entitled to ITCs for the related MRP Expenses.

The TCC concluded that Amex's claim of a free supply was not valid and emphasized that the nature of the supply must be determined based on the overall financial service supplies made by Amex. Whereas Amex claimed that the purpose of the free supply was to promote the activities of Participants, the TCC found that the promotional and marketing efforts of the Rewards primarily served Amex's own purposes rather than the promotion of Participants' activities.

The TCC also noted that even if the free supply rule were to apply, Amex did not provide sufficient evidence to demonstrate how the MRP Expenses should be allocated between the alleged promotion of the Participants' activities and the predominant purpose of providing a financial service.

Final Observations

Lastly, the TCC expressed its skepticism about Amex's position, stating that it is "akin to the task of swimming against a significant riptide", as if it was to agree with Amex's position, this would lead to a result which is contrary to the outcome of a number of decisions involving taxpayers that sought to grow the revenue from their credit card business by offering rewards to members of their loyalty programs calculated based on their card spending.

Justice Hogan, who also presided over *President's Choice Bank*[5] ("*PC Bank*"), highlighted that he concluded in *PC Bank* that redemption payments were linked to the provision of exempt financial services and, therefore, were not eligible for NITCs.

Finally, the TCC noted that both the TCC and FCA commented in other cases that under the general scheme of the ETA, financial institutions cannot claim ITCs for GST/HST related to loyalty programs used in the course of their financial services business.

— *Dragann Mallette*

CURRENT ITEMS OF INTEREST

Enhanced Canada Workers Benefit Payments

On July 28, millions of low- and modest-income Canadian workers will receive their first automatic advance payments of the newly enhanced Canada Workers Benefit.

Enhancements to the Canada Workers Benefit, first announced in 2021, expanded eligibility to an additional one million workers — and now, support from the enhanced Canada Workers Benefit will be available sooner. Prior to the recent passage of Bill C-47, people needed to wait until they filed their taxes to receive this support.

[5] *President's Choice Bank v. The Queen*, 2022 TCC 844.

The Canada Workers Benefit will provide up to $2,616 total for an eligible family, and $1,518 total for eligible single workers, split between three advance payments this fiscal year (in July 2023, October 2023, and January 2024), and a final payment after filing the 2023 tax return. Low- and modest-income Canadian workers who received the Canada Workers Benefit in 2022 will automatically receive their advance payments from the Canada Revenue Agency, with no need to apply.

Charities Impacted by Wildfires and Floods

As wildfire and flood activity continues to be higher than normal across Canada, some charities may be unable to meet their filing obligations due to extraordinary circumstances, such as a fire or flood. The Canada Revenue Agency issued a reminder on July 27 that in such cases it is important to contact the Charities Directorate as soon as possible to discuss your situation and ensure your charity remains in good standing. For more information, contact the Charities Directorate's client service team at 1-800-267-2384.

Inefficient Fossil Fuel Subsidies

On July 24, the Government of Canada released the *Inefficient Fossil Fuel Subsidies Government of Canada Self-Review Assessment Framework* and the *Inefficient Fossil Fuel Subsidies Government of Canada Guidelines*. The Assessment Framework and Guidelines support the decarbonization of Canada's oil and gas sector by eliminating inefficient fossil fuel subsidies.

The Assessment Framework will be used to determine which tax and non-tax measures constitute an inefficient fossil fuel subsidy. Subsidies will be considered inefficient unless they meet one or more of the following six criteria:

(1) Enable significant net greenhouse gas emissions reductions in Canada or internationally in alignment with article 6 of the *Paris Agreement*;

(2) Support clean energy, clean technology, or renewable energy;

(3) Provide essential energy service to a remote community;

(4) Provide short-term support for emergency response;

(5) Support Indigenous economic participation in fossil fuel activities; or

(6) Support abated production processes, such as carbon capture, utilization, and storage ("CCUS"), or projects that have a credible plan to achieve net-zero emissions by 2030.

The Guidelines are effective July 24 and apply to all federal departments and agencies. The Assessment Framework and Guidelines can be found at www.canada.ca/en/services/environment/weather/climatechange/climate-plan/inefficient-fossil-fuel-subsidies/assessment-framework.html and www.canada.ca/en/services/environment/weather/climatechange/climate-plan/inefficient-fossil-fuel-subsidies/guidelines.html.

Calls for Extension of CEBA Repayment Deadline[1]

During the pandemic, the Canada Emergency Business Account ("CEBA") program provided up to $60,000 in interest-free loans to small businesses and not-for-profits.

In a July 24 letter to Finance Minister Chrystia Freeland, the Canadian Chamber of Commerce and a coalition of industry associations joined calls for the federal government to extend the deadline for small businesses to repay pandemic loans received through the program by two years to the end of 2025, or at least by one year, while allowing businesses to maintain access to the forgivable portion of up to one-third of their loans. The current repayment deadline is December 31, 2023.

Mandatory Disclosure Rules

The following CRA publications and forms were recently updated/issued:

- Mandatory disclosure rules — Overview (www.canada.ca/en/revenue-agency/programs/about-canada-revenue-agency-cra/compliance/mandatory-disclosure-rules-overview.html);
- Mandatory disclosure rules — Guidance (www.canada.ca/en/revenue-agency/programs/about-canada-revenue-agency-cra/compliance/mandatory-disclosure-rules-overview/guidance-document.html);

[1] From the Toronto Star: www.thestar.com/business/2023/07/24/canadian-chamber-of-commerce-joins-calls-for-extension-of-ceba-repayment-deadline.html.

- RC312 *Reportable Transaction and Notifiable Transaction Information Return (2023 and later tax years)* (www.canada.ca/content/dam/cra-arc/formspubs/pbg/rc312/rc312-23e.pdf); and
- RC3133 *Reportable Uncertain Tax Treatments Information Return (2023 and later tax years)* (www.canada.ca/content/dam/cra-arc/formspubs/pbg/rc3133/rc3133-23e.pdf).

INTERNATIONAL NEWS

UK Legislates for Undertaxed Profits Rule

The UK Government has issued draft legislation to introduce into UK law the undertaxed profits rule ("UTPR") under Pillar Two of the OECD's two-pillar international tax reform plan.

Earlier, the Government introduced a multinational top-up tax ("MTT") and domestic top-up tax in Finance (No.2) Act 2023, which will have effect in respect of accounting periods beginning on or after December 31, 2023.

It has now proposed amendments to Part 3 of the Act to implement the UTPR, which will ensure that any top-up taxes that are not paid under another jurisdiction's income inclusion rule or domestic minimum top-up tax rule are brought into charge in the UK.

Other amendments seek to ensure that UK legislation remains consistent with the OECD model rules and administrative guidance items, as agreed by the BEPS Inclusive Framework. The UTPR provisions will have effect from a date to be appointed by the Treasury in regulations, which will not be before accounting periods beginning on or after December 31, 2024.

The two elements are intended to ensure that multinational groups whose annual group revenues exceed €750 million are taxed in each jurisdiction at a rate of at least 15%.

The Government has proposed the following amendments to Part 3 of Finance (No. 2) Act 2023 to implement the UTPR:

- Section 121 will be amended to extend multinational top-up tax to cover tax under the undertaxed profits rule;
- Section 122 will be amended to expand the chargeable persons from a responsible member to any member of the group;
- Section 123 will be amended to introduce a condition that a person is chargeable to multinational top-up tax where top-up amounts and additional top-up amounts of one or more group members are potentially undertaxed and the relevant member is not an investment entity;
- Section 123A will be added to allow the amount of any undertaxed profits multinational top-up tax charge to be set in accordance with Chapter 9A;
- Section 124 will be amended to provide for Chapter 9A, which sets out the provisions for determining whether top-up tax amounts are potentially undertaxed and how these amounts should be allocated to UK group members.

Chapter 9A will be added, which provides for the meaning of "potentially undertaxed" and "untaxed amounts". Chapter 9A will also set out the steps required to allocate untaxed amounts to qualifying members located in the UK. These steps require the group to determine the number of its employees and the value of its tangible assets located in the UK and other territories that have a qualifying undertaxed profits tax.

The filing member of the group will be able to elect that a specified member of the group is to be allocated the whole of the tax that is attributable to UK members through the undertaxed profits rule.

Chapter 9A also will determine the rules for allocating untaxed amounts in respect of joint ventures.

Schedule 16 will be amended to ensure that the transitional provision also applies to untaxed amounts under the undertaxed profits rule, and there will also be consequential amendments to Section 128 (responsible members), Section 257 (meaning of qualifying undertaxed profits tax), Section 259 (country-by-country reports), and Schedule 17 (definitions).

EU States Challenged on Public CbC Reporting Laws

The European Commission has sent letters of formal notice to 17 EU member states for failing to legislate for the provisions of Directive (EU) 2021/2101 as regards disclosure of income tax information by certain undertakings and branches.

Letters of formal notice have been sent to Belgium, Bulgaria, the Czech Republic, Estonia, Greece, Croatia, Italy, Cyprus, Latvia, Luxembourg, Malta, Netherlands, Austria, Poland, Portugal, Slovenia, and Finland. The member states were required to notify the Commission of domestic measures transposing the Directive into law by June 22, 2023.

Under the Directive, member states must introduce new reporting obligations on ultimate parent undertakings to draw up, publish, and make publicly accessible a report on income tax information regarding the last two consecutive financial years, where the group's consolidated revenue exceeded €750 million.

The requirement will apply from financial years starting on or after June 22, 2024.

The information that must be reported is as follows:

- The name of the ultimate parent undertaking or the standalone undertaking, the financial year concerned, the currency used for the presentation of the report, and, where applicable, a list of all subsidiary undertakings consolidated in the financial statements of the ultimate parent undertaking, in respect of the relevant financial year, established in the Union or in tax jurisdictions included in Annexes I and II to the Council conclusions on the revised EU list of non-cooperative jurisdictions for tax purposes;
- A brief description of the nature of their activities;
- The number of employees on a full-time equivalent basis;
- Revenues, which are to be calculated as,
  - the sum of the net turnover, other operating income, income from participating interests, excluding dividends received from affiliated undertakings, income from other investments and loans forming part of the fixed assets, other interest receivable, and similar income as listed in Annexes V and VI to the Directive, or
  - the income as defined by the financial reporting framework on the basis of which the financial statements are prepared, excluding value adjustments and dividends received from affiliated undertakings;
- The amount of profit or loss before income tax;
- The amount of income tax accrued during the relevant financial year, which is to be calculated as the current tax expense recognised on taxable profits or losses of the financial year by undertakings and branches in the relevant tax jurisdiction;
- The amount of income tax paid on a cash basis, which is to be calculated as the amount of income tax paid during the relevant financial year by undertakings and branches in the relevant tax jurisdiction; and
- The amount of accumulated earnings at the end of the relevant financial year.

US Republicans Table Legislation To Counter Global Minimum Tax

US Republicans have introduced the Unfair Tax Prevention Act, which would penalize countries introducing an Undertaxed Profit Rule ("UTPR") under the OECD's proposed Pillar Two framework.

Tabling the bill, Representative Ron Estes (R-KS) said:

> If a country moves forward with a UTPR surtax on American workers and businesses, the Unfair Tax Prevention Act imposes a reciprocal tax measure that will apply as long as the foreign country's unfair tax remains in place.

Estes said his Act would impose a reciprocal tax measure on any country imposing the UTPR to increase tax on a US entity. A summary released by Estes on the bill said it would:

- Define "foreign-owned exterritorial tax regime entities" ("FETR entities") as foreign-controlled entities connected with entities operating in jurisdictions with extraterritorial taxes aimed at US business operations, including the UTPR;
- Strengthen anti-avoidance rules in the US base erosion and anti-abuse tax ("BEAT") by eliminating the 3% base erosion percentage floor and the US$500 million gross receipts test for FETR entities;

- Revoke the ability of FETR entities to disregard certain service payments and payments subject to withholding taxes, and treat 50% of cost of goods sold as a base erosion tax benefit; and
- Accelerate the scheduled BEAT rate increase and tax credit changes for FETR entities.

"After repeated objections from policymakers, including myself, and business leaders, the Biden administration has negotiated a deal with the OECD that has a disproportionately negative effect on the United States and our economic competitiveness," he said. "Building on the Defending American Jobs and Investment Act, introduced by Ways and Means Republicans, this legislation protects the US tax base from unfair extraterritorial taxes by foreign countries — and imposes stiff penalties on those countries if they implement them. It's time for the OECD and foreign countries to abandon the UTPR surtax and its fundamental flaws."

US Businesses Urge Against Canadian DST

US businesses are calling on the Canadian Government to rule out a digital services tax.

The US Chamber of Commerce has expressed concerns about Canadian government proposals to implement a digital services tax, despite international pressure for an extended moratorium on the introduction of such levies.

Chamber Senior Vice President Watson McLeish said:

> The Chamber is disappointed by Canada's decision to oppose the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting's recent agreement to extend the moratorium on imposing digital services taxes (DSTs) on any company for another year. We urge the Government of Canada to make clear that they will not unilaterally act to impose a DST.
>
> Imposing a DST would not only be discriminatory but also contravene Canada's obligations under both the Canada-US-Mexico Agreement (CUSMA) and the World Trade Organization (WTO). It's for this reason that the prospect of unilateral Canadian DST action has elicited staunch bipartisan opposition in the US Congress and warnings of retaliatory measures from the Biden administration.
>
> The Chamber urges Canada to return to the OECD process and support extension of the DST moratorium to which nearly 140 countries have agreed.

TAX TOPICS

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