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THE APPLICATION FOR RECTIFICATION BY THE COURT IS NOT A CURE FOR ALL ILLS: PREVENTION IS BETTER THAN (ATTEMPTING!) A CURE

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Last June 19, the Superior Court of Québec rendered an interesting judgment on tax rectification in the case of *Mac's Convenience Stores inc. c. Couche-Tard inc.*,[1] applying certain aspects of the teachings laid down by the Québec Court of Appeal in 2011 in the decisions in *Services environnementaux AES inc.*[2] ("**AES**") and *Riopel*.[3]

The facts of the case were as follows. During 2005, Mac's Convenience Store inc. ("**MAC's**") contracted an interest-bearing loan of about $185M from the US company, Sildel Corporation ("**SILDEL**"). Between 2006 and 2008, MAC's paid about $22M in interest to SILDEL, which MAC's deducted in accordance with the provisions of the *Income Tax Act* (Canada)[4] (the "**ITA**"). On April 25, 2006, MAC's declared and paid a dividend to Couche-Tard inc. ("**CTI**") in order to redistribute funds within the group, ultimately to allow a portion of MAC's debt to be repaid.

Briefly, under the rules of the ITA, when a Canadian corporation contracts an interest-bearing loan from a specified non-resident, the deductibility of interest on the loan is denied when the debt-to-equity ratio of the debtor corporation exceeds the maximum permitted ratio of 2:1 (henceforth 1.5:1[5]) (the "**Thin Capitalization Rules**"). The dividend of $136M declared and paid by MAC's to CTI reduced MAC's equity by the same amount, triggering the application of the Thin Capitalization Rules. Thus, MAC's was denied the entire amount of the deduction of interest paid on the loan. MAC's therefore sought to cancel the dividend of $136M declared and paid on April 25, 2006 by replacing it with a reduction in capital, which would not affect its equity capital or compromise the deductibility of the interest.

The judgments in AES and Riopel teach us that one of the criteria to be considered in order for an application for rectification to be granted is the existence of a difference between the common intention of the parties and their intention as reflected in the written legal instruments. In the cases of Riopel and AES, there was a significant divergence between the parties' true intention and the agreement supporting the transaction. This enabled the

1 2012 QCCS 2745.
2 *Québec (Sous-ministre du Revenu)* c. *Services environnementaux AES inc.*, 2011 QCCA 394.
3 *Riopel* c. *Agence du revenu du Canada*, 2011 QCCA 954.
4 R.S.C., 1985, c.1 (5th Supp.).
5 This measure applies to the taxation years of corporations which start after 2012.

(CONTINUED)

court, in both cases, to rule in favour of the taxpayers and rectify the legal instruments concluded by the parties.

In the MAC's case, the resolution by MAC's directors to declare a dividend of about $136M did accurately reflect MAC's intention to pay a dividend. The evidence showed that there had been no discussion between the parties involved regarding the consequences of the payment of a dividend and the potential application of the Thin Capitalization Rules. The negative tax consequences only occurred because the payment of the dividend took place in the year after the loan was granted, thereby strengthening the argument that there was no divergence between the taxpayer's intention and the documents giving effect to this intention. Without the deduction of the interest paid to SILDEL, Revenu Québec would never have issued a notice of assessment. The court concluded that the transactions completed on April 25, 2006 accurately reflected the parties' intention and therefore declined to grant the application for rectification on the grounds that such an application cannot be used to rewrite the tax history of a file.

This case has been appealed and its final outcome is therefore not known at this time. Nevertheless, it shows once again the preponderant role which professionals must play in certain transactions and the care they must exercise in doing so. ◂

REGISTER YOUR TRADE-MARKS!

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A trade-mark is worth much more than the word, image or slogan embodied in it. It serves to distinguish a business and is integral to its reputation. The choice of a trade-mark is the result of strategic planning and effort and reflects the philosophy advocated by the business, hence the importance of protecting it. Although the right of ownership in a trade-mark is acquired through the use thereof, and registration is not mandatory, a registered trade-mark has undeniable benefits for a business.

Registration gives the owner the exclusive right to use the trade-mark throughout Canada for a period of 15 years, even if, in practice, the trade-mark is solely used in Quebec. Thereafter, registration can be renewed indefinitely every 15 years. Furthermore, registration is a direct proof of the right of ownership. Thus, in any litigation aimed at establishing the right of ownership in a trade-mark, the registered owner is not required to prove his right — the burden of proof is on the applicant. On the other hand, the use of an unregistered trade-mark can lead to protracted litigation to determine the rights to the disputed trade-mark.

Upon registration, the trade-mark is automatically entered in the register of trade-marks at the Canadian Intellectual Property Office ("**CIPO**"), which is a way of publicizing the exclusive rights claimed in the trade-mark. Not only is this register accessible to the public, but CIPO examiners also refer to this tool when considering any new trade-mark registration application. Thus, the examiner will raise an objection, of his own motion, against a new application if it is likely to cause confusion with a trade-mark already on the register, thereby providing a degree of protection for existing registered trade-mark owners.

Trade-marks are one of the most important assets of a business from an economic standpoint, and the registration is valuable in itself for purposes of the sale of a business or when seeking financing.

While registration is optional, it is highly recommended. The process is not costly or tedious and is undoubtedly the best way to avoid litigation over the right of ownership to the trade-mark. An ounce of prevention is worth a pound of cure! ◂

THE IMPORTANCE OF HAVING A DETAILED POWER OF ATTORNEY IN THE EVENT OF A PERSON'S INCAPACITY

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The Superior Court of Québec rendered a decision worth considering at the beginning of 2012 in the matter of *R.B.* v. *F.B.* In that case,[1] a father, age 72, (the "**Applicant**"), acting as the attorney under a power of attorney for his son who became incapable of managing his own affairs, applied to the court for authorization to create a trust for his son's sole benefit and to transfer nearly all his son's property to the trust by way of a tax rollover. The Applicant was worried about the consequences, and the possibility of the public curator's intervention in relation to his son's property, if the Applicant should die or become incapable of acting. It should be noted that the power of attorney given in anticipation of the Applicant's son's incapacity only provided for one substitute attorney, the son's uncle, in the event of the Applicant's death or inability to act. This uncle had just been diagnosed with cancer and, furthermore, resided a distance of more than 750 km from the Applicant's son's residence. The Applicant's goal was therefore to ensure the continuity of the administration of his son's property by creating a trust, with the Applicant and Desjardins Trust as trustees. The substitute attorney, the uncle, did not object to the Applicant's application.

Therefore, the issue the court had to determine was whether an attorney appointed under a power of attorney given in anticipation of the principal's incapacity has the power to create a trust for the benefit of his principal and to transfer the property administered by him to the trust. The court answered in the negative and dismissed the Applicant's motion for the following reasons:

1) The attorney's obligation is a personal one which is *intuitu personae*, meaning that the attorney must personally fulfill the power of attorney given to him, unless the principal has authorized him to substitute another person in his stead to perform all or part of the power of attorney (article 2140 of the *Civil Code of Québec*).

   The power of attorney in the event of incapacity at issue here contained no such provision allowing the Applicant to delegate his powers to a third party.

2) The attorney does not have the power to transfer the principal's property which he is responsible for administering, and he cannot therefore act as the settlor of a trust. The court indicated that a general power of attorney does not, by itself, authorize the attorney to create a trust. The attorney must have the principal's express and specific authorization to do so, which he did not have in this case.

This decision, which is a severe one in our view, highlights the importance of drafting a detailed power of attorney in the event of incapacity. Indeed, it is easy to understand the Applicant's concerns and his desire to avoid that protective supervision (tutorship or curatorship) for his son be instituted in the event of the Applicant's death or inability to act. The Applicant's motion to the court showed his foresight and concern for adequately protecting his son in the long term by ensuring his property would continue to be managed by a professional trustee, for the sole benefit of his son, in the event the Applicant should die or become incapable of acting. However, these were not sufficient grounds for the court to grant his motion.

It is too soon to predict whether this decision will be followed by the courts in other cases. However, for the time being, it should serve as an incentive for some persons to revise the provisions of their powers of attorney given in anticipation of incapacity to include specific provisions concerning (i) the procedure for replacing the designated attorney, and the number of substitute attorneys designated in the power of attorney; (ii) the power of the attorney to delegate some or all of his powers; and (iii) where desired, the specific power to create a trust for the exclusive benefit of the incapable person in certain circumstances. ◂

1 *R.B.* c. *F.B.*, 2012 QCCS 247.

EFFECT OF A UNANIMOUS SHAREHOLDERS' AGREEMENT ON CCPC STATUS

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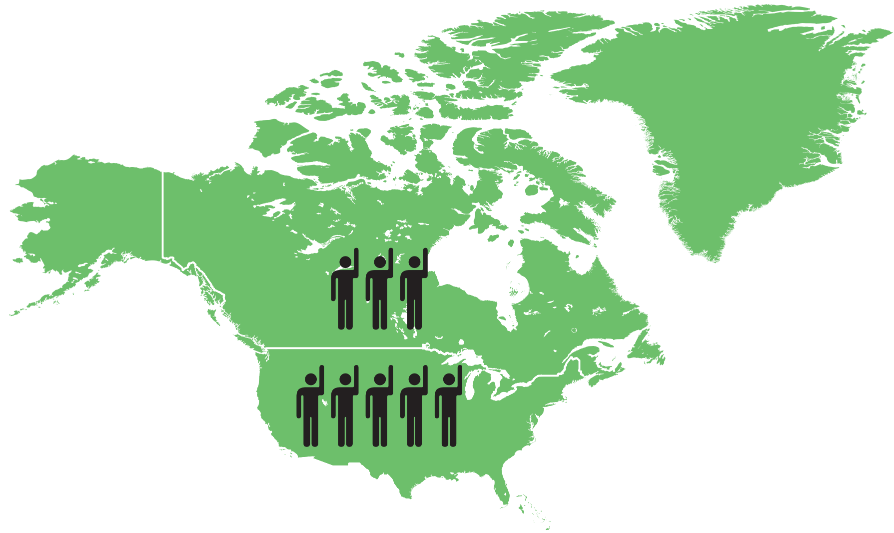

The Tax Court of Canada (the "**Court**") recently rendered a decision in the case of *PricewaterhouseCoopers Inc. agissant ès qualité de syndic à la faillite de BioArtificial Gel Technologies Inc. (Bagtech) c. Sa Majesté La Re*ine[1] on the impact of a unanimous shareholders' agreement ("**USA**") on the status of a corporation as a "Canadian-controlled private corporation" ("**CCPC**") within the meaning of the *Income Tax Act* (Canada) ("**ITA**").

The central issue before the Court was to determine what impact Bagtech's USA had on its status as a CCPC (under subsection 125(7) ITA). More specifically, the Court had to decide whether the provisions of the USA, which provided that the non-resident shareholders could not elect a majority of the members of the corporation's board of directors, were sufficient for Bagtech to be considered a CCPC despite the fact that its non-resident shareholders held a majority of the voting shares during the taxation years in question.

The Court concluded, for purposes of the definition of CCPC, that the clauses of a USA governing the election of a corporation's directors must be taken into account in determining the *de jure* control of the corporation. Relying on the decision of the Supreme Court of Canada in *Duha Printers*, the Court found that any restriction under a USA on the power of the majority shareholders to elect members of the board of directors must be taken into account for purposes of determining *de jure* control. Having so found, the Court concluded that Bagtech was a CCPC for the taxation years in question because the majority of the directors were appointed by resident Canadian shareholders according to the terms of the USA, despite the fact that the non-resident shareholders held a majority of the voting shares.

This decision is particularly interesting because of the new possibilities it creates for corporations having a majority of non-resident shareholders. For example, the conclusion by a corporation's shareholders of a USA with similar provisions to that in Bagtech will enable the corporation to claim refundable investment tax credits, among other things. This is a much simpler way of qualifying for tax incentives as compared with some of the other structures which have been developed over the years to get around the definition of CPCC. However, it should be noted that this decision has been appealed to the Federal Court of Appeal. ◄

1 Decision dated April 12, 2012, file 2009-3734(IT)G.

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