RECENT TRANSACTIONS

IFA Canada Tax Conference 2022 | YIN Rapporteur Summary

Presented on May 16, 2022

Speakers: Mathieu Champagne, Deloitte LLP, Montréal
Derek Chiasson, Norton Rose Fulbright Canada, LLP, Montréal
Ken Saddington, Goodmans LLP, Toronto
Gwen Watson, Torys LLP, Toronto

Moderator: Alex Pankratz, *Baker McKenzie LLP,* Toronto

YIN Rapporteur: Kathryn Walker, McCarthy Tétrault LLP

This panel focused on tax considerations pertaining to recent cross-border transactions.

Outbound Transactions – The panel considered reasons why a company may want to emigrate from Canada and the potential benefits of doing so, including: substantial business operations in the US, access to entitlements or contracts provided by the US government, avoiding foreign accrual property income exposure, and eliminating the risk of being a passive foreign investment company for US tax purposes.

Recent Domestication Transactions - Describing several recent domestication transactions the panel discussed key tax issues that can arise when a corporation continues to the US, such as the importance of tracking paid up capital to manage tax liabilities arising on deemed dividends, loss carry-forwards, surplus calculations, section 128.1 departure tax, and the Part XIV emigration tax that may apply where the fair market value of assets are more than applicable liabilities and paid-up capital. In addition, the panel explained that domestication transactions can create sandwich structures that give rise to tax inefficiencies. Of note, where a structure includes an entity that is disregarded for US tax purposes, the structure may not be a sandwich for US tax purposes, but may be so for Canadian tax purposes.

Model transactions - The panel considered two model domestication transactions, one based on Maxar Canada's 2018 domestication and another based on Encana's 2020 plan. For both models, the panel observed the importance of protecting paid-up capital and avoiding any reduction in the adjusted cost base of shares in the emigrating corporation, as such attributes can help reduce tax liabilities arising on emigration or by virtue of the foreign affiliate dumping ("FAD") rules. In respect of these model transactions, the panel compared an inbound F reorganization with a share-for-share exchange followed by an out-from-under, noting that the former alleviates the need for an immediate valuation, involves a hybrid entity, may trigger the FAD rules, and provides less clarity on the repositioning of external debt, whereas the latter does not require a valuation of US entities, offers a clear pipeline for the repatriation of US profits to public shareholders and is likely easier for the repositioning of external debt.

Inbound Transactions – The panel discussed the 2021 Contact Gold transaction by which Contact Gold, originally a British Columbia corporation which had emigrated to Nevada, redomiciled back to British Columbia. The transaction involved two steps: a continuance and an amalgamation with Contact Gold surviving. The panel explained that while a cross-border amalgamation is possible in some provinces, it is not clear that the predecessor entities would qualify as taxable Canadian corporations for the purposes of subsection 87(1).

US Inversion - The panel considered US inverted entities, which can result when a US corporation redomiciles to Canada, and in certain other circumstances where a Canadian corporation acquires a US corporation or business. Such US inverted entities add tax complexity because they are subject to Canadian and US tax on their worldwide income, and cross-border payments can be subject to Canadian and US withholding tax rules. The panel noted that from a Canadian perspective it may be possible in certain circumstances to remove an acquired inverted entity from a structure if a bump is available.

Canopy/Acreage – The panel described the proposed acquisition of Acreage, a US inverted entity, by Canopy, a Canadian corporation. As proposed the acquisition will occur when US federal law changes to permit the cultivation, distribution and possession of marijuana. The transaction is of particular interest in that it involves the acquisition of a US inverted entity.

YIN RAPPORTEUR REPORT

CROSS-BORDER TOPICS OF INTEREST

IFA Canada Tax Conference 2022 | YIN Rapporteur Summary

Presented on May 16, 2022

Speakers:	Carrie Aiken, Blake, Cassels & Graydon LLP, Calgary
	Christopher Anderson, Davies Ward Phillips & Vineberg LLP, Toronto
	Nik Diksic, EY Law LLP, Montréal
	Francesco Gucciardo, Aird Berlis LLP, Toronto
Moderator:	Laura Gheorghiu, Gowling WLG (Canada) LLP, Montréal
YIN Rapporteur:	**Samantha D'Andrea, EY Law LLP, Montréal**

The panelists provided a discussion of various interesting and practical topics in the cross-border M&A context, including:

Foreign Affiliate Dumping Rules in M&A

The discussion focused on FAD rules that look at the concept of "series of transactions or events", which is particularly relevant in the context of an M&A transaction. The applicability of the FAD rules to certain pre-closing and post-closing transactions was discussed. Specific practical examples were also discussed including internal reorganizations, amalgamations, indirect investments, and preferred share investments.

111(4)(e) Planning – Impact of Proposed "Substantive CCPC" Rules

The panelists discussed the 111(4)(e) planning technique in the context of a cross-boarder acquisition and the impact of the proposed "Substantive CCPC" rules announced in Budget 2022 on such planning and what opportunities and strategies may remain.

Earnouts and other forms of non-share consideration in cross-border structures

The speakers provided a recent overview of CRA statements on earnouts paid to non-residents and discussed the treatment of earnouts on immigration/emigration. The panelists then discussed market trends in Contingent Value Rights (CVRs) and Tax Receivable Agreements (TRAs).

Canadian tax issues when dealing with Canadian companies that are treated as inverted for US tax purposes

The panel addressed the issues arising in circumstances where a business combination among a US and Canadian company triggers an inversion such that the Canadian company is treated as a US corporation for US tax purposes and subject to both US and Canadian income tax (as the tax treaty does not provide relief). The panel also addressed certain issues that need to be managed given foreign tax credit mismatches as well as some of the possible benefits (present and historical) of the Canadian company being treated as inverted. Finally, some possible Pillar II mismatch issues were discussed.

Update on tax provisions in transactional agreements

This practical discussion reviewed current trends in representations and warranties, tax indemnity provisions and insurance in the cross-border M&A context. The recent *Boliden* and *Glencore* cases were also discussed in regards to tax indemnity and break fees respectively.

TAX DIRECTORS ROUNDTABLE

IFA Canada Tax Conference 2022 | YIN Rapporteur Summary

Presented on May 16, 2022

Speakers: Alexander Chan, Investment Management Corporation of Ontario, Toronto
Larry Greer, Telesat Canada, Ottawa
Andrea Shreeram, Bank of Nova Scotia, Toronto

Moderator: Lynn Moen, Enbridge Inc., Calgary

YIN Rapporteur: Vanessa Zuchetto, Felesky Flynn LLP

The following topics were discussed in the Tax Directors Roundtable:

1. **Operational challenges in remote work environments**: Efficiencies can arise from working remotely as part of a global tax team provided frequent touch points are in place to ensure connectivity. Teams have adapted well to performing routine, process-driven work. Challenges remain when performing analytical and planning work, which requires teams to be more intentional to foster creative collaboration. There are particular issues associated with onboarding new employees.
2. **Hiring and retention**: Employees aren't just financially motivated. It has been difficult during the pandemic to ensure that employees have access to workplace culture and connection. Employers must be intentional to foster those connections. Strategies include ensuring all employees have a career development plan in place, broadening the net of possible hires, training existing employees to perform new tasks and deploying technology to perform routine work more efficiently, leaving resources available to perform tasks requiring greater analysis.

3. **Use of technology in workplace**: Strategies and considerations include automating routine functions (such as the completion of tax returns and other forms), sorting and scanning mail received based on urgency, data analytics and fostering innovation. A tax technology lead can identify routine tasks that can be automated or made more efficient with technology.
4. **Interactions with CRA**: Relationships of trust and cooperation should be built with tax authorities and other governmental departments. Some tax authorities have constant touchpoints with taxpayers (rather than just as part of the audit process), which may build a cooperative relationship. The pandemic has reinforced the financial services industry’s partnership with various parts of the government, including the CRA, notably in the administration of public relief programs. It has been time consuming and costly to manage certain administrative issues with the CRA during the pandemic.
5. **Developments in tax laws**: Fundamental and significant amendments have been made and are proposed to be made to existing Canadian tax laws. These amendments pose difficult but interesting challenges for tax teams. Tax directors focus on analysis, synthesis and open dialogue to ensure that these amendments are communicated within their organizations. Financial modelling may also be completed to understand the impact of certain amendments.
6. **Role of tax group within organization**: The rest of the organization should understand how the tax team provides value to the organization. “Roadshows” within the organization introduce the tax team and elevate non-tax members’ knowledge so that they can spot issues and bring them to the tax team’s attention. The tax team, while it may not be the heart or brains of the organization, should be viewed as analogous to the organization’s kidney or liver – *i.e.,* performing an essential and necessary function within the organization.

CURRENT CASES

IFA Canada Tax Conference 2022 | YIN Rapporteur Summary
Presented on May 16, 2022

Speakers: Al Meghji (Osler, Hoskin & Harcourt LLP, Toronto)
John Sorensen (Gowling WLG (Canada) LLP, Toronto)
Matt Williams (Thorsteinssons LLP, Toronto)

Moderator: Margaret Nixon (Stikeman Elliott LLP, Toronto)

YIN Rapporteur: Darren Joblonkay (Davies Ward Phillips & Vineberg LLP, Toronto)

This panel discussion focused on a review and discussion of the implications of current case law in the following categories: (i) cases dealing with the general anti-avoidance rule ("GAAR"); (ii) cases dealing with statutory interpretation; and (iii) recent cases dealing with, and proposed legislative responses to, the audit powers of the Canada Revenue Agency ("CRA").

1. GAAR

The panel considered two GAAR cases: *Canada v. Alta Energy Luxembourg S.A.R.L.*, 2021 SCC 49 ("*Alta Energy*) and *Canada v. Deans Knight Income Corporation*, 2021 FCA 160 ("*Deans Knight*"). *Deans Knight* was granted leave to appeal by the Supreme Court of Canada ("SCC") on March 10, 2022.

In respect of *Alta Energy*, the panel emphasized the findings of the majority, namely that the treaty represented a bargain between the parties and the ultimate result was a product of drafting decisions. The Supreme Court reiterated a cautionary word that tax disputes should avoid moral judgements and purely results-oriented analyses.

Regarding *Deans Knight*, the panelists emphasized the uncertainty and predictability that has been created as a result of the “actual control” test introduced by the Federal Court of Appeal (“FCA”). The panelists agreed that the uncertainty created is particularly concerning, provided that “control” goes to the very heart of the commercial world. By subsuming aspects of both *de jure* and *de facto* control into a new test, the FCA has created the need for clarification from Canada’s highest Court. In this respect the panel looks forward to the appeal.

A key theme present in both *Alta Energy* and *Deans Knight*, as identified by the panel, is a technique often utilized by the Crown, by which the Crown articulates a compelling narrative in respect of the transactions carried out by the taxpayer, that are meant to elicit an emotional response that Parliament could not have “intended” to allow for the tax results achieved. Phrases with largely negative connotations, such as “treaty shopping” and “loss sharing” are employed to give the impression that the tax result is objectionable and should be prohibited. The decision of the minority in *Alta Energy* and the FCA’s decision in *Deans Knight* appear to have been influenced to some extent by such advocacy. The cautionary words of the Majority in *Alta Energy*, should however, provide some comfort to taxpayers that such moral judgements and results-oriented analyses is to be resisted by the Courts.

2. Statutory Interpretation

Cases discussed involving statutory interpretation included the SCC decision, *Canada v. Loblaw Financial Holdings Inc.*, 2021 SCC 51 (“*Loblaw Financial*”) and *Bank of Nova Scotia v. R.*, 2021 TCC 70 (“*BNS*”).

In regards to recent decisions that dealt with issues of statutory interpretation, the panelist’s observed, similar to the trends observed in GAAR cases, that the Crown often employs purposive interpretation as a proxy for policy, which leads to a more narrative-focused, results-driven analysis to the interpretation of statutory provisions in the

Income Tax Act (the "Act")– as a result, the textual, contextual and purposive analysis of statutory provisions takes the form of a "GAAR-lite". Importantly, the Supreme Court of Canada in *Loblaw Financial* rejected such approach, drawing a clear distinction between the GAAR analysis and general statutory interpretation. The Court was clear, in non-GAAR cases, where the text is clear and complete, deference should be afforded to the text. Only where the text is unclear and ambiguous, should the Courts consider external, contextual factors. The panelists were in agreement that the text of the Act is meant to capture, and be reflective of, policy considerations, which they felt was departed from to some degree by the dissent in *Alta Energy* and in *BNS*.

3. CRA Audit Powers

Finally, the panel considered proposed legislative changes in response to the decisions in *Canada v. Cameco Corporation*, 2019 FCA 67 and *BP Canada Energy Company v. MNR*, 2017 FCA 61.

Based on the recent case law, the panelists concluded that the Courts have generally favoured providing the CRA with broad powers for administration and enforcement of the Act to ensure full compliance by taxpayers. The Courts appear unwilling to frustrate CRA's ability to fix a taxpayer's liability or undermine the statutory tools perceived by the tax administration as required to establish tax liability.

Conclusion

In concluding, the panelists look forward to the forthcoming decision of the Supreme Court of Canada in *Deans Knight*, which presents a unique opportunity to reconcile the majority and minority decisions in *Alta Energy* and clarify interpretative issues raised in *Loblaw Financial*. The prospect of potential revisions or amendments to the GAAR will remain top of mind for tax practitioners as such cases continue to flow through the Courts.

YIN RAPPORTEUR REPORT

EARNINGS STRIPPING AND HYBRID MISMATCH RULES

IFA Canada Tax Conference 2022 | YIN Rapporteur Summary

Presented on May 17, 2022

Speakers:	Byron Beswick, KPMG LLP, Calgary Ken Buttenham, PwC Canada, Toronto John Lorito, Stikeman Elliott LLP, Toronto Sabrina Wong, KPMG LLP, Toronto
Moderator:	Marie-Emmanuelle Vaillancourt, Davies Ward Phillips & Vineberg LLP, Montreal
YIN Rapporteur:	**Bryan Madorsky**

This panel discussion focused on the new draft legislation recently released in relation to excessive interest and financing expenses and hybrid mismatch arrangements.

<u>Excessive Interest and Financing Expenses Limitation (“EIFEL”) Rules</u>

The draft EIFEL rules were released on February 4, 2022 to implement the 2021 budget proposal to limit the deduction for interest and financing expenses. These rules are based on the recommendations of the OECD in BEPS Action Plan 4 and are generally applicable for taxation years that begin on or after January 1, 2023. In general, these rules will apply to limit the deduction of net interest and financing expenses of corporations and trusts to a fixed ratio of 30% of “adjusted taxable income” (“ATI”) (the “fixed ratio” rule) or higher percentage of ATI based on a “group ratio”.

The panel provided an overview of the legislative framework governing EIFEL, including key definitions, concepts, and exclusions. The panel emphasized the complexity of the

EIFEL rules and related anti-avoidance rules, which are drafted broadly, and may lead to potentially unintended negative consequences. These were illustrated with several examples, including:

1) An example showing how the "restricted interest and financing expenses" ("RIFE") and excess capacity carry-forward rules may interact in the group context.
2) An example showing how the EIFEL rules, including the decision on whether to make an "excluded interest" election, may operate in a typical loss consolidation arrangement.
3) An example showing how the EIFEL rules operate in a partnership structure.
4) An example showing how the new anti-avoidance rule in subsection 18.2(12) may lead to potentially unintended negative consequences in a situation where a taxpayer borrows to make loans to foreign affiliates.

With respect to foreign affiliates, the panel noted that it is not currently clear how the EIFEL rules are intended to apply in the foreign affiliate arena, and they are awaiting clarification on this.

Hybrid-Mismatch Rules

The first of two legislative packages in relation to hybrid-mismatch arrangement was released on April 29, 2022 and applies effective July 1, 2022.[1] The intent of these rules is to neutralize the deduction/non-inclusion outcomes associated with certain types of hybrid-mismatch arrangements as well as foreign deductions for notional interest expense. The panel provided a brief overview of the legislative framework governing hybrid-mismatch arrangements and provided examples of how the rules may operate in the context of inbound hybrid debt arrangements, non-interest-bearing loans to

[1] The rules in the second package (which has not be released) will apply no earlier than 2023.

controlled foreign affiliates resident in jurisdictions that allow for notional interest expense deductions, and REPO transactions.

The panel noted that the amount denied under the hybrid-mismatch rules may be a deemed to be a dividend and subject to Canadian withholding tax. Also, as this deeming rule may apply on accrual basis, the unwind of such arrangements before July 1 may become a necessity for some impacted taxpayers.

YIN RAPPORTEUR REPORT

RECENT CANADIAN AND INTERNATIONAL DEVELOPMENTS

IFA Canada Tax Conference 2022 | YIN Rapporteur Summary

Presented on May 17, 2022

Speakers:	Mark Kaplan
	Patrick Marley
	Stefanie Morand
	Andrew Spiro
	Taylor Cao
Moderator:	Christopher Montes
YIN Rapporteur:	**Taylor Cao**

This panel provided an update on recent international tax proposals by the OECD/G20 Inclusive Framework, and legislative proposals in Canada and the US.

Pillar One proposals by the OECD/G20 Inclusive Framework would give market jurisdictions additional taxing rights over excess profits of large multinational enterprises ("Amount A"), at the expense of residence and headquarter jurisdictions, in exchange for an agreement by countries to remove and not introduce any digital services taxes and other similar measures. Consultation documents have been released by the OECD, but there are significant obstacles to worldwide implementation of Pillar One proposals, since implementation would require amendments to both domestic legislation and existing tax treaties, and the US could lose significant revenue as a result of having to provide credit for taxes on Amount A in market jurisdictions. Pillar One also includes "Amount B" – which is intended to simplify transfer pricing by approximating the arm's length pricing of baseline marketing and distribution activities. Canada has introduced legislation to impose a 3% digital services tax, which will not come into force before January 1, 2024, and is only intended to apply if the Pillar One proposals have not come into force by that time (although it would then apply retrospectively to January 1, 2022).

Pillar Two proposals would impose a minimum tax of 15% in each jurisdiction based on financial accounting income. The OECD has released model rules, commentary and illustrative examples. In general terms, Pillar Two proposals would require taxpayers to calculate their "effective tax rate" ("ETR") in each jurisdiction based on "covered taxes" and adjusted financial accounting income. If the effective tax rate in any jurisdiction is lower than 15%, a top-up tax applies to income in that jurisdiction – at a rate equal to the difference between 15% and the ETR, multiplied by excess profit (*i.e.* income less a substance-based exclusion). Top-up taxes can be collected by the local jurisdiction itself (through a "Qualified Domestic Minimum Top-up Tax" or "QDMTT"), the jurisdiction of a parent entity (through an "Income Inclusion Rule" ("IIR") – starting from the top entity in an IIR jurisdiction), or the jurisdiction of other affiliates (through the UTPR), in that order. QDMTTs will likely be implemented by most jurisdictions, since without a QDMTT, other jurisdictions may collect top-up taxes from income earned in the local jurisdiction. As more jurisdictions impose QDMTTs, the amount of tax collected under the IIRs and UTPRs will decrease. Issues identified under Pillar Two proposals include:

- The interaction between QDMTTs and CFC taxes need to be clarified;
- The status of the US GILTI rules under the Pillar Two proposals will depend on certain amendments being made – and it is currently unclear whether the requisite changes will be made before the US elections in November;
- Top-up taxes under the UTPR can be collected from entities that have no connection with the entity earning the low-taxed income (other than being part of the same affiliated group) – which may be inconsistent with existing tax treaties;

- Top-up taxes can cause tax incentives (particularly non-refundable tax credits) to be less effective;
- Top-up taxes may also arise in some circumstances even where a company is in a loss position.

The EU has proposed to implement the Pillar Two model rules through an EU directive, although the latest attempt was vetoed by Poland. Canada has announced that it intends to implement Pillar Two proposals and a domestic minimum top-up tax.

In the "American Jobs Plan", the Biden Administration released international tax proposals that build upon the proposed Build Back Better Act ("BBBA"). Among other things, these proposals would increase the US corporate tax rate and the tax rates that would apply on GILTI, provide an incentive in favour of onshoring business activities and a disincentive against offshoring, impose a 15% minimum tax on corporations based on book income, and replace the BEAT with a UTPR. These proposals indicate that the Biden Administration intends to conform US tax rules to Pillar Two proposals.

The 2022 Canadian federal budget also included the following tax proposals, among others:

- New subsections 212(21) and 212(22) will target coupon-stripping arrangements that inappropriately reduce withholding tax on cross-border interest payments;
- The potential deferral advantage associated with Canadian-controlled private corporations ("CCPCs") earning investment income through foreign affiliates will be eliminated by applying the "relevant tax factor" currently applicable to individuals to CCPCs (and "substantive CCPCs"), with corresponding capital dividend account adjustments to preserve integration; and
- The GAAR will be amended to allow it to apply to transactions that affect tax attributes that have not yet become relevant to the computation of tax.