APPENDIX 40 (PENDING CASE OF VELCRO AND BENEFICIAL OWNERSHIP)

Material:

Velcro Canada Inc. and Her Majesty the Queen, Notice of Appeal, April 19, 2007

Velcro Canada Inc. and Her Majesty the Queen, Reply, August 10, 2007

TAX COURT OF CANADA
COUR CANADIENNE DE L'IMPÔT
FILED / DEPOSE
AVR APR 19 2007
DINA ZIGOMANIS
REGISTRY OFFICER / AGENT DU GREFFE
TORONTO

Court File No. 2007-1806(IT)G

TAX COURT OF CANADA

BETWEEN:

VELCRO CANADA INC.

the "Appellant"

and

HER MAJESTY THE QUEEN

the "Respondent"

NOTICE OF APPEAL

TAKE NOTICE THAT Velcro Canada Inc. (the "Appellant") hereby objects to a Notice of Confirmation (the "Confirmation") dated February 5, 2007 in respect of its 1995 through 2004 taxation years.

A. STATEMENT OF FACTS

1. Velcro Canada Inc. ("VCI") is a corporation incorporated under the laws of Canada with its registered office at 114 East Drive, Brampton, ON, L6T 1C1. VCI has non-resident remitter number NRX 288240.

2. VCI is in the business of manufacturing and selling Velcro® brand fastening products used in the automobile and other industries. VCI uses the following Velcro® brand fastener technology:

   (a) patents;

   (b) trade secrets;

   (c) copyrights;

   (d) know-how; and

   (e) confidential information (being any idea, improvement, invention, innovation, development, technical data, design, formula, device, pattern, concept, computer program, model, diagram, equipment, tool, training or service manual, product specification, plan for a new or revised product or service, compilation of information or work in process, and any and all revisions and improvements relating to any of the foregoing).

3. Velcro Industries B.V. ("VIBV") is a corporation created under the laws of the Netherlands. VIBV was resident in the Netherlands until December 29, 1995, on which date VIBV changed it residency to the Netherlands Antilles.

4. VIBV is the owner of the Velcro® brand and all of the technology referred to in paragraph 2 above (hereinafter the "Licensed IP").

5. VIBV files its corporate income tax returns, and pays its taxes, in the Netherlands Antilles.

6. Velcro Holdings B.V. ("VHBV") is a corporation created under the laws of the Netherlands and is resident in the Netherlands.

7. VHBV is the exclusive sublicensor of the Licensed IP in some jurisdictions. In addition, VHBV is in the business of lending funds within the Velcro group of companies.

8. VHBV files corporate income tax returns in the Netherlands and pays tax on its profits, including royalties described in paragraph 10 below, received as sublicensor in that jurisdiction.

9. Pursuant to a License Agreement dated October 1, 1987 between VIBV and VCI (under its former corporate name, Velcro Canada Ltd.) VCI obtained the following rights:

   (a) the exclusive right to manufacture within Canada the Licensed Products (as defined in the License Agreement, being products made using the Licensed IP);

   (b) the right to sell Licensed Products to VIBV's authorized importers, or, if there are no such importers, directly to end users in Canada;

   (c) the right to import and re-sell Licensed Products to VIBV's authorized distributors, or, if there are no such distributors, directly to end users in Canada; and

   (d) the right to distribute and sell Licensed Products in Canada.

10. The License Agreement provided for royalties payable by VCI to VIBV at different rates for "Established Technology Products" (as defined in the License Agreement) and for "New Technology Products" (as defined in the License Agreement).

11. Pursuant to an Assignment, Assumption and License Agreement dated October 27, 1995 (the "Assignment Agreement") VIBV assigned to VHBV VIBV's right to grant Licensed IP licenses and VIBV's rights to royalties and payments under the License Agreement. Under section 3 of the Assignment Agreement VIBV retained the rights of ownership in the Licensed IP.

12. Under the Assignment Agreement VHBV became entitled to the royalty payable by VCI in respect of the Licensed IP.

13. Pursuant to the Assignment Agreement VHBV agreed to pay to VIBV a royalty calculated as an arm's length percentage of "net sales" of "licensed products" as those terms are defined in the License Agreement (subject to approval by the Netherlands taxing authorities).

14. VHBV has a similar sublicensing arrangement with the European manufacturing affiliate in Spain.

15. Effective October 1, 2003 VIBV, VHBV and VCI concurrently entered into agreements that replace the License Agreement and the Assignment Agreement.

16. The terms and conditions of the replacement License Agreement and the replacement Assignment Agreement are similar to the previous agreements in most respects, other than in the calculation of the royalty. Hereafter, a reference to the "License Agreement" or to the "Assignment Agreement" will encompass the original Agreements, any amendments thereto, and the replacement agreements.

17. VHBV is a substantial corporation. It has over US$6 million in cash, more than US$30 million in investments in subsidiary companies, approximately US$5 million in outstanding loans to subsidiary companies, and approximately US$40 million in equity. In addition to receiving royalty income, VHBV also receives substantial interest income on outstanding loans to its subsidiaries, and substantial dividend income from its investments in subsidiary companies.

18. VHBV carries on its business using the services of an arm's length corporation, Amaco Management Services B.V. ("Amaco"). Amaco provides to VHBV numerous services, including the following:

    (a) office space (including telephone, fax and secretarial services);

    (b) legal compliance services;

    (c) management services;

    (d) administrative services;

    (e) the preparation of tax and financial information;

    (f) banking services;

    (g) bookkeeping and accounting services;

    (h) the provision of managing directors; and

    (i) the arranging for audit reports.

19. Amaco receives a substantial arm's length fee from VHBV to provide these services.

20. VHBV has control over the right to receive royalties and the payments received from VCI, and exercises the rights of ownership over such royalties and amounts paid.

21. On or about March 25, 1998 the Canada Revenue Agency (the "CRA") issued a non-resident Notice of Assessment to VCI in respect of royalties paid to VHBV in 1997. The Notice of Assessment showed no balance of tax payable and assessed a late-filing penalty in the amount of $4,943.00.

22. On March 30, 1999 the CRA issued a non-resident Notice of Assessment to VCI in respect of royalties paid to VHBV in 1998. The Notice of Assessment showed no balance of tax payable, and assessed a late-filing penalty in the amount of $31,627.00.

23. On or about September 3, 1999, the CRA issued a non-resident Notice of Assessment to VCI in respect of royalties paid to VHBV in 1999. The Notice of Assessment showed no balance of tax payable and assessed a late-filing penalty in the amount of $2,313.59.

24. On or about May 16, 2006 the CRA issued notices of assessment in respect of 2002 and 2003. While the assessments are issued in the name of "Velcro Canada Ltd.", VCI presumes that the notices of assessment are directed to VCI. For 2002, VCI was assessed non-resident tax in the amount of $1,362,484.75 (with corresponding penalty of $136,248.47). For 2003 VCI was assessed non-resident tax in the amount of $1,569,401.00 (with corresponding penalty of $156,940.10). Interest was also assessed.

25. On or about November 20, 2006, the CRA issued Notices of Assessment in respect of 1995, 1996, 1997, 1998, 1999, 2000, 2001 and 2004. While the assessments are issued in the name of "Velcro Canada Ltd.", VCI presumes that the Notices of Assessment are directed to VCI. The assessed amounts with corresponding penalty are as follows:

Year	Non-Resident Tax	Penalty
1995	$270,634	$27,063
1996	$231,787	$23,178
1997	$325,043	$32,504
1998	$448,844	$44,884
1999	$1,063,890	$106,389
2000	$1,299,000	$129,900
2001	$1,225,505	$122,550
2004	$740,350	$74,035

Interest was also assessed.

26. The CRA contends that the "beneficial owner" of the royalties is not the recipient thereof, being VHBV, but rather is VIBV.

B. ISSUES

27. Did VCI pay royalties to VHBV in the 1995 taxation year?

28. Was VHBV the "beneficial owner" of the royalties paid to it by VCI in 1996 through 2004, so that it was entitled to the elimination of withholding tax pursuant to paragraph 3(b) of Article 12 of the Convention between Canada and the Kingdom of the Netherlands (the "Convention")?

29. Are the reassessments for 1995 through 1999 statute-barred?

C. STATUTORY PROVISIONS RELIED UPON

30. VCI relies on the provisions of the Convention, the *Income Tax Conventions Interpretations Act* (Canada) and the *Income Tax Act* (Canada).

D. REASONS

The 1995 Taxation Year

31. VCI's 1995 taxation year ended on September 30, 1995. Throughout such fiscal year all royalties which were paid by VCI were paid to VIBV under the License Agreement, and not to VHBV.

32. The Appellant submits that the assessment relating to 1995 is improper, and that all required withholdings were made with respect to royalties paid to VIBV for the period ending September 30, 1995.

Was VHBV the "Beneficial Owner" of the Royalties?

(a) The Convention

33. Paragraph 2 of Article 12 of the Convention provides that the withholding tax rate on royalty income flowing between Canada and the Netherlands is 10% of the gross amount of the royalties.

34. Paragraph 3 of Article 12 provides as follows:

> Notwithstanding the provisions of paragraph 2:
>
> (a) copyright royalties and other like payments in respect of the production or reproduction of any literary, dramatic, musical or other artistic work (but not including royalties in respect of motion picture films nor royalties in respect of works on film or videotape or other means of reproduction for use in connection with television broadcasting), and
>
> (b) royalties for the use of, or the right to use, computer software or any patent or for information concerning industrial, commercial or scientific experience (but not including any such information provided in connection with a rental or franchise agreement)

arising in a State and paid to a resident of the other State who is the beneficial owner of the royalties shall be taxable only in that other State.

35. VCI submits that VHBV is the beneficial owner of royalties paid by VCI for VCI's right to use the Licensed IP. Thus paragraph 3(b) of Article 12 applies to eliminate the withholding tax on the royalties paid.

(b) The Meaning of the term "Beneficial Owner"

36. The CRA is of the view that the Assignment Agreement indicates that VIBV is organized and existing in the Curacao, Netherlands Antilles. In fact, VIBV is organized and existing under the laws of the Netherlands, and changed its residency to the Netherlands Antilles on December 29, 1995.

37. The term "beneficial owner" is not defined in the Convention.

38. Pursuant to Section 2 of Article 3 of the Convention and section 3 of the *Income Tax Conventions Interpretations Act* (Canada) the term should be given the meaning it has for Canadian domestic law purposes.

39. The term "beneficial owner" is not specifically defined in the *Income Tax Act* (Canada). However, the Supreme Court of Canada has held that a "beneficial owner" is a person who can ultimately exercise the rights of ownership over the property.

40. VCI submits that VHBV has control over the royalties paid to it by VCI, and that VHBV exercises the rights of ownership over such royalties. The fact that VHBV separately owes a royalty to VIBV does not derogate from the rights of ownership it has over the royalties received from VCI. The royalties received by VHBV from VCI are commingled with other income earned by VHBV, and are used to pay its obligations generally (including the royalty owed to VIBV).

41. If VHBV were to become insolvent and failed to pay royalties to VIBV, VIBV's only course of action would be as a creditor of VHBV. VIBV could not claim royalties which had been paid or are payable by VCI to VHBV as its own.

42. VHBV is also the "beneficial owner" of the royalties under the domestic law of the Netherlands.

43. If regard is to be made to international meanings (which the Appellant denies), under the Vienna Convention on the Law of Treaties that the ordinary meaning is to be given to terms of a treaty, and recourse may be made to supplementary means of interpretation available. One can infer that this means available at the time the treaty was entered into.

44. The Commentary to the 1977 OECD Model Convention states that a person will not be a "beneficial owner" if the person is a "nominee" or an "agent". Neither term is defined in such Commentary.

45. A "nominee" is a person who is designated to act in place of another, usually in a very limited way.

46. An "agent" is a person who is authorized to act for and in place of another, who is referred to as the principal.

47. There is nothing about the relationship of the parties that suggests that VHBV was acting, in any fashion, as nominee or agent of VIBV.

48. VHBV is a substantial corporation. It has over US$6 million in cash, more than US$30 million in investments in subsidiary companies, approximately US$5 million in outstanding loans to subsidiary companies, and approximately US$40 million in equity. In addition to receiving royalty income, VHBV also receives substantial interest income on outstanding loans to its subsidiaries, and substantial dividend income from its investments in subsidiary companies.

49. The CRA is required to respect the contractual relationships which have been established by the parties. The contractual relationship between VIBV, VHBV and VCI cannot be characterized as agency relationships.

50. VHBV exercises the rights of ownership over the royalties received. It uses those royalties in its lending business and to invest in its subsidiaries.

51. The royalties received by VHBV from VCI are commingled with other income and used to pay its obligations generally (including the royalty owed to VIBV).

Are the Assessments Statute-Barred?

52. Notices of Assessment were issued on or about March 25, 1998, March 30, 1999 and September 3, 1999 for the 1997,1998 and 1999 taxation years respectively. In all cases the 7-year limitation period commenced, expiring on or about March 25, 2005, March 30, 2006 and September 3, 2006, respectively. VCI states that any assessments for 1997, 1998 and 1999 are statute-barred.

53. Section 3 of Article 25 of the Convention states as follows:

> A State shall not, after the expiry of the time limits provided in its national laws and, in any case, after 6 years from the end of the taxable period in which the income concerned has accrued, increase the tax base of a resident by the States by including therein items of income which have also been charged to tax in the other State. This paragraph shall not apply in the case of fraud or wilful default.

54. VCI states that the 1995 through 1999 taxations years are statute-barred pursuant to section 3 of Article 25 of the Convention.

D. RELIEF SOUGHT

55. VCI requests:

(a) that its objection be allowed in full, and that the withholding tax assessments for 1995 through 2004 in the amounts noted in paragraphs 24 and 25 (together with penalties and interest) be reversed to show a nil balance. VCI further requests that the taxes, penalties and interest which have been paid on account be refunded to VCI with interest;

(b) its costs of this appeal; and

(c) such further or other relief as counsel may advise and this Honourable Court think just.

E. ADDRESS FOR SERVICE

56. The name and address for the solicitors for the Appellant are:

Aird & Berlis LLP
Barristers & Solicitors
BCE Place – Suite 1800
181 Bay Street, P.O. Box 754
Toronto, Ontario M5J 2T9

Attention: Louise R. Summerhill
LSUC#: 31312L

Phone: 416.863.1500
Fax: 416.863.1515

DATED at Toronto this 19th day of April, 2007.

Louise R Summerhill
Velcro Canada Inc.
by its solicitors, Aird & Berlis LLP

TO: Tax Court of Canada
180 Queen Street West
Suite 200
Toronto, ON M5V 3L6

Court File No.

TAX COURT OF CANADA

Between:

VELCRO CANADA INC.

- and -

HER MAJESTY THE QUEEN

NOTICE OF APPEAL

SERVICE OF A TRUE COPY HEREBY ACCEPTED
SIGNIFICATION DE COPIE CONFORME

Admitted this 0 day
Acceptée le jour
of 2007
de

for John H. Sims, Q.C.
pour Deputy Attorney General of Canada
Sous-procureur général du Canada

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TAX COURT OF CANADA

BETWEEN:

VELCRO CANADA INC.

Appellant

and

HER MAJESTY THE QUEEN

Respondent

REPLY

In reply to the Appellant's Notice of Appeal with respect to its appeals for 1995 to 2004, the Deputy Attorney General of Canada says:

A. STATEMENT OF FACTS

1. He admits the allegations of fact stated in paragraphs 1, 2, 4, 6, 9, 10, 24 and 25 of the Notice of Appeal.

2. He denies the allegations of fact stated in paragraph 20 of the Notice of Appeal.

3. He has no knowledge of and puts in issue the allegations of fact stated in paragraphs 5, 7, 8, 14, 15, 16, 17, 18 and 19 of the Notice of Appeal.

4. With respect to paragraph 3 of the Notice of Appeal, he says that during the relevant period, Velcro Industries B.V. ("VIBV") was resident of the Netherlands Antilles. He otherwise has no knowledge of the allegations of

facts as stated in paragraph 3 of the Notice of Appeal and puts those facts in issue.

5. With respect to paragraphs 11, 12 and 13 of the Notice of Appeal, he admits only that VIBV and Velcro Holdings B.V. ("VHBV") entered into an Assignment, Assumption and License Agreement ("Assignment Agreement"). He says the Assignment Agreement and its provisions speak for themselves. He otherwise denies the said paragraphs.

6. He denies the allegations of fact as stated in paragraphs 21, 22 and 23 of the Notice of Appeal, except that he says:

a) For the Appellant's 1997 taxation year, it was assessed a late remittance penalty in the amount of $4,943 pursuant to the provisions of subsection 227(9) of the *Income Tax Act*, R.S.C. 1985, c. 1 (as amended), (the "*Act*"). This notice of assessment was dated March 25, 1998;

b) For the Appellant's 1998 taxation year, it was assessed a late remittance penalty in the amount of $32,627 pursuant to the provisions of subsection 227(9) of the *Act*. This notice of assessment was dated March 30, 1999;

c) It was subsequently determined that the late remittance penalty assessed for the 1998 taxation year was assessed in error and the

penalty raised there-under was cancelled on September 1, 1999; and

d) No penalty assessment under subsection 227(9) was raised in respect of 1999.

7. With respect to paragraph 26 of the Notice of Appeal, he says that the Minister's position as to who is the beneficial owner of the royalty payments is set out below. He otherwise denies the said paragraph.

8. He denies all other facts as may be pleaded in the balance of the Notice of Appeal.

9. For the years 1995 to 2004 and pursuant to the Assignment Agreement, the Appellant paid royalties to VHVB and failed to deduct and withhold non resident income tax on those payments as required by sections 212 and 215 of the *Act*.

10. The Minister of National Revenue (the "Minister") assessed the Appellant to tax for 1995 to 2004 on the royalty payments paid by it to VHBV pursuant to the provisions of paragraphs 212(1)(d) and 227(10)(d) and subsections 215(1) and 215(6) of the *Act*. The Minister also assessed a penalty equal to 10% of the assessed tax pursuant to the provisions of paragraphs 227(8)(a) and 227(10)(a) of the *Act*. The notices of assessment for 1995 to 2001 and 2004 were dated November 20, 2006 and the notices of assessment for 2002 and 2003 were dated May 16,

2006. The amount of the tax assessed and penalty assessed for 1995 to 2004 is as follows:

Year	Non Resident Tax Assessed	Penalty Assessed
1995	$270,634	$27,063
1996	$231,787	$23,179
1997	$325,043	$32,504
1998	$448,844	$44,884
1999	$1,063,890	$106,389
2000	$1,299,000	$129,900
2001	$1,225,505	$122,552
2002	$1,362,484	$136,248
2003	$1,596,401	$156,940
2004	$740,350	74,035

11. The Appellant objected to the assessments. The Minister confirmed the assessments. The notification of confirmation was dated February 5, 2007.

12. In so assessing the Appellant for the 1995 to 2004 taxation years, and confirming the assessments, the Minister assumed the following facts:

The Appellant, VIBV and VHVB

a) The Appellant is incorporated under the laws of Canada and is resident in Canada;

b) At all relevant period, VIBV was a resident of the Netherlands Antilles;

c) At all relevant period, VHBV was a resident of the Kingdom of the Netherlands;

d) At all relevant times, Canada and the Kingdom of the Netherlands were party to the *Tax Convention Between Canada and the Kingdom of the Netherlands* (the "*Convention*");

e) There is no Tax Convention between Canada and the Netherlands Antilles;

Licence Agreement

f) The Appellant is in the business of manufacturing and selling Velcro® brand fastening products used in the automobile and other industries (the "Licensed Products");

g) VIBV is the owner or licensee of the technology, including all patents, trade secrets, copyrights, confidential information, know-how and other forms of intellectual or industrial property (the "Licensed Technology") used to make Licensed Products;

h) In 1987, the Appellant and VIBV entered into a licence agreement (the "Licence Agreement");

i) Under the Licence Agreement, VIBV granted to the Appellant the right use the Licensed Technology to manufacture, sell, import and resell and distribute and sell Licensed Products in a particular manufacturing territory or country;

j) In exchange, the Appellant agreed to pay to VIBV, a royalty based on the Appellant's 'Net Sales' of Licensed Products. There was one royalty rate for Licensed Products made using 'established technology' and another royalty rate for Licensed Products made using 'new technology' (the "Royalty Payments");

k) The Licence Agreement also provided that:

- all rights in the Licensed Technology belonged to VIBV;
- that the Appellant will not used the Licensed Technology for research and development;
- that the Appellant will cooperate with any request by VIBV to create, record or perfect VIBV's sole and exclusive ownership of the Licensed Technology; and
- that the Appellant will promptly advise VIBV of any misuse, infringement or possible infringement of the Licensed Technology;

l) The License Agreement also provided that VIBV may assign the License Agreement, and its rights and obligations at any time on notice to the Appellant;

<u>The Assignment Agreement</u>

m) In October 1995, VIBV assigned the Licence Agreement to VHBV;

n) The Assignment Agreement provided that:

- VIBV retained its ownership of the Licensed Technology licensed under the Assignment Agreement or the License Agreement;
- VHBV will pay a royalty to VIBV based on 'Net Sales' of 'Licensed Products' as those terms are defined in the License Agreement;
- VHBV assumed all obligations and duties of VIBV under the License Agreement;
- VHBV agreed to enforce the terms of the License Agreement and notify VIBV of any breach of the License Agreement, and unless directed otherwise by VIBV, to remedy any breach or unauthorized disclosure of confidential information, as that term was defined in the License Agreement;

o) The Assignment Agreement also provided that VIBV was an express third party beneficiary of the provisions of the License Agreement assigned to VHBV and that VIBV was entitled to exercise the rights of the licensor and enforce the obligations of the licensee, being the Appellant, under the License Agreement and have the right to enforce such rights on its own behalf in its sole discretion;

Royalty Payments

p) In the calendar years of 1995, 1996, 1997, 1998, 1999, 2000, 2001, 2002, 2003 and 2004, the Appellant paid royalty payments under the License Agreement (the "Royalty Payments");

q) In the calendar years of 1995, 1996, 1997, 1998, 1999, 2000, 2001, 2002, 2003 and 2004, the Appellant paid Royalty Payments to VHBV and in turn, VHBV paid Royalty Payments to VIBV, on the same or similar basis as the Royalty Payments paid by the Appellant to VHBV;

r) VHBV acted as conduit between the Appellant and VIBV with respect to the payment of the Royalty Payments under the License Agreement by the Appellant to VIBV;

s) At all relevant times, VIBV was the beneficial owner of the Royalty Payments;

t) At all relevant times, VHBV acted as 'agent' for VIBV with respect to the collection of the Royalty Payments from the Appellant under the License Agreement;

u) The purpose of the Assignment Agreement was to avoid the payment of Part XIII tax by VIBV on the Royalty Payments paid by the Appellant to VIBV under the License Agreement;

v) During the 1995 to 2004 calendar years, the Appellant made the Royalty Payments to VIBV through the conduit of VHBV as on account or in lieu of payment or, or in satisfaction of royalty under the Assignment Agreement for the used of the Licensed IP;

w) During the 1995 to 2004 calendar years, VIBV failed to pay an income tax equal to 25% of the Royalty Payments paid by the Appellant to it during those years;

x) During the 1995 to 2004 taxation years, the Appellant paid the Royalty Payments to VIBV and failed to deduct or withhold from those Royalty Payments, an income tax equal to 25% of the Royalty Payments paid by it to VIBV through VHBV and remit that income tax to the Receiver General of Canada on behalf of VIBV;

y) The Appellant is liable to a penalty equal to 10% of the income tax equal to 25% of Royalty Payments the Appellant failed to deduct or withhold and remit to the Receiver General of Canada.

B. ISSUES TO BE DECIDED

13. The issue is whether, for the 1995 to 2004 years, the Minister properly assessed the Appellant pursuant to sections 212, 215 and 227 of the *Act*:

a) To an income tax equal to 25% of the Royalty Payments paid by the Appellant and flowed through VHBV to VIBV; and

b) To penalties equal to 10% of the income tax equal to 25% of the Royalty Payments paid by the Appellant and flowed through VHBV to VIBV.

14. The issue is also whether the assessments of 1997 and 1998 are statute barred.

C. STATUTORY PROVISIONS, GROUNDS RELIED ON, AND RELIEF SOUGHT

15. He relies, *inter alia*, on sections, subsections and paragraphs 152, 212(1)(d), 215(1), 215(6), 227(8), 227(9), 227(10) and 227(10.1) of the *Act* and Articles 1, 3, 4, 12 and 25 of the *Convention*.

16. He respectfully submits that the Minister correctly assessed the Appellant for the 1995 to 2004 calendar years an income tax equal to 25% of the Royalty Payments paid by the Appellant to VIBV and flowed through VHBV pursuant to the provisions of paragraph 212(1)(d) and subsections 215(1), 215(6), 227(8) and 227(10) of the *Act*.

17. He respectfully submits that the Minister correctly assessed the Appellant for the 1995 to 2004 calendar years a penalty equal to 10% of the 25% non resident income tax on the Royalty Payments pursuant to the provisions of subsection 227(8) and paragraph 227(10)(a) of the *Act*.

18. He submits in 1995 to 2004, as a non resident and pursuant to paragraph 212(1)(d) of the *Act*, VIBV was liable to pay an income tax equal to 25% of the Royalty Payments received by it from the Appellant.

19. He submits that for 1995 to 2004 the Appellant was required by subsection 215(1) to deduct or withhold from the Royalty Payments, an income tax equal to 25% of the Royalty Payments paid to VIBV and forthwith remit that amount to the Receiver General of Canada.

20. He submits that under the terms of the Assignment Agreement, VIBV was the express third party beneficiary of the License Agreement, and therefore, was the beneficial owner of the Royalty Payments that were paid by the Appellant to VIBV, through VHBV.

21. He submits that as VHBV was not the beneficial owner of the Royalty Payments, the provisions of the *Convention*, including Article 12 of the *Convention*, do not apply as between the Appellant and VHBV. As the Appellant paid the Royalty Payments to the beneficial owner of the Royalty Payments, being VIBV, the Appellant was obligated pursuant to paragraph 212(1)(d) and section 215 of the *Act* to withhold or deduct and remit income tax equal to 25% of the Royalty Payments made to VIBV in 1995 to 2004.

22. He submits that under the Assignment Agreement, VIBV retained all rights of ownership of the Licensed Technology.

23. He submits that during the relevant period, VHBV acted as agent for VIBV in the collection of the Royalty Payments from the Appellant.

24. He submits that during the relevant period, VHBV was a conduit for VIBV with respect to the receipt of the Royalty Payments from the Appellant and flowed through to VIBV.

25. He submits that the purpose of the Assignment Agreement was to avoid the application of *Part XIII* of the *Act* on the Royalty Payments paid by the Appellant to VIBV.

26. He submits that pursuant to the provisions of 215(1) the Appellant is required to withhold or deduct and remit as a non resident income tax, 25% of the Royalty Payments paid in the 1995 to 2004 years to VIBV, the beneficial owner of the Royalty Payments. In failing to withhold or deduct and remit as a non resident income tax, 25% of the Royalty Payments, the Appellant is liable to pay as income tax on behalf of VIBV, the non resident income tax equal to 25% of the Royalty Payments that it should have deducted or withheld pursuant to the provisions of subsection 215(6) of the *Act*.

27. In failing to deduct or withhold the 25% non resident income tax on the Royalty Payments, the Appellant is liable to a penalty equal to 10% of the 25% non resident income tax on the Royalty Payments pursuant to the provisions of subsection 227(8) of the *Act*.

28. He submits that an assessment under 227(8) of the *Act* on account of a failure to deduct or withhold income tax on a payment made under subsection 212(1) of the *Act* to a non resident of Canada is raised for a calendar year and not a taxation year. The Minister correctly assessed the Appellant in respect of the 1995 calendar year even though its taxation year ended September 30, 1995.

Statute Barred

29. He submits that the Appellant was assessed non resident income tax under subsection 215(6) and paragraph 227(10)(d) of the *Act*, (a "Tax Assessment") and penalties under subsection 227(8) and paragraph 227(10)(a) of the *Act* (a "Penalty Assessment").

30. He submits that the Appellant was also assessed a late remittance penalty in respect of 1997 and 1998 pursuant to subsection 227(9) of the *Act* (the "Late Remittance Penalty Assessment"). The Late Remittance Penalty Assessment raised in respect of 1998 was subsequently cancelled.

31. A Tax Assessment is consequent on the failure of a resident of Canada to withhold or deduct and remit non resident income tax as required by *Part XIII* of the *Act*.

32. A Penalty Assessment applies a penalty equal to 10% of the non resident income tax the resident of Canada failed to withhold or deduct as required by section 215 of the *Act*.

33. A Late Remittance Penalty Assessment applies a penalty equal to 10% of any amount a person has in a calendar year failed to remit or pay as and when required by the *Act* or a regulation an amount deducted or withheld as required by the *Act* or a regulation.

34. Under paragraphs 227(10)(a) and 227(10)(d) and paragraph 227(10.1)(a) of the *Act*, a Tax Assessment, a Penalty Assessment and a Late

Remittance Penalty Assessment are each separate assessments. He submits that Tax Assessments on this appeal in respect of 1997 and 1998 are not statute barred as the notices of assessments issued for 1997 and dated March 25, 1998 and for 1998 and dated March 30, 1999 and September 1, 1999 are Late Remittance Penalty Assessments and not Tax Assessments or Penalty Assessments.

35. He submits that a Tax Assessment and a Penalty Assessment under paragraphs 227(10)(a) and 227(10)(d) of the *Act* may be raised at any time. A Late Remittance Penalty Assessment under paragraph 227(10.1)(a) may also be raised at any time. Once a Tax Assessment, Penalty Assessment or Late Remittance Penalty Assessment are raised, the provisions of section 152 of the *Act* apply with any modifications as the circumstances require.

Limitation Period under the *Convention*

36. He submits that the assessments at issue did not have the effect of increasing the tax base of the Appellant or VIBV or VHBV for 1995 to 2004 nor were they made on the basis of including an amount into the income of the Appellant such that limitation for raising assessments as set out in Article 23 of the *Convention* apply to the Minister to raising the assessments at issue.

37. He submits that if this Court should find that VIBV was the beneficial owner of the Royalty Payments, then the articles of the *Convention* respecting limitations period for raising assessments are not applicable.

He requests that the appeal be dismissed with costs.

DATED at the City of Toronto, Ontario, this August 10, 2007.

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2007-1806(IT)G

TAX COURT OF CANADA

BETWEEN:

VELCRO CANADA INC.

Appellant

and

HER MAJESTY THE QUEEN

Respondent

REPLY

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TORONTO, CANADA