

Federal Court



Cour fédérale

Date: 20150916

Docket: T-1736-13

Citation: 2015 FC 1082

Ottawa, Ontario, September 16, 2015

PRESENT: The Honourable Mr. Justice Martineau

BETWEEN:

**VIRGINIA HILLIS AND
GWENDOLYN LOUISE DEEGAN**

Plaintiffs

and

**THE ATTORNEY GENERAL OF CANADA
AND
THE MINISTER OF NATIONAL REVENUE**

Defendants

JUDGMENT AND REASONS

[1] On August 11, 2014, the plaintiffs filed a statement of claim seeking a declaration that the *Canada-United States Enhanced Tax Information Exchange Agreement Implementation Act*, being section 99 and Schedule 3 of the *Economic Action Plan 2014 Act, No. 1*, SC 2014, c 20 [IGA Implementation Act], and sections 263 to 269 of the *Income Tax Act*, RSC 1985, c 1 (5th Suppl) [ITA] – collectively, the “impugned provisions” – are *ultra vires* or inoperative because

the impugned provisions are unconstitutional or otherwise unjustifiably infringe *Charter* rights [the constitutional issues].

[2] By the effect of section 3 of the IGA Implementation Act, the Agreement between the Government of Canada and the Government of the United States of America [US] set out in the schedule [Intergovernmental Agreement or IGA] of the IGA Implementation Act is approved and has the force of law in Canada during the period that the Intergovernmental Agreement, by its terms, is in force.

[3] On October 9, 2014, the plaintiffs filed an amended statement of claim adding non-constitutional arguments, which are examined and disposed of in the present judgment. This summary trial concerns the legality of the disclosure of the personal information of US persons (see paragraphs 17 and 27 below) collected for the year 2014 by Canadian financial institutions for the Canada Revenue Agency [CRA]. This information is scheduled to be disclosed on or around September 30, 2015 by the Minister of National Revenue [Minister] to the US tax authorities.

[4] In this respect, the plaintiffs seek a general declaration and a permanent prohibitive injunction preventing the collection and disclosure of taxpayer information to the US by the Minister where:

- (a) the taxpayer information relates to a taxable period in which the taxpayer was a citizen of Canada;

- (b) the taxpayer information is not shown to be relevant for carrying out the provisions of the Convention or the domestic tax laws of Canada or the US; or
- (c) the collection and disclosure of the taxpayer information subjects US nationals resident in Canada to taxation and requirements connected therewith that are more burdensome than the taxation and requirements connected therewith to which Canadian citizens resident in Canada are subjected.

[5] The plaintiffs generally assert that the automatic collection and disclosure of any such taxpayer information to the US as required by the impugned provisions would be contrary to the provisions of the *Convention between the United States and Canada with Respect to Taxes on Income and Capital* [Canada-US Tax Treaty] and/or to section 241 of the ITA. The Canada-US Tax Treaty has been approved by Parliament and has the force of law in Canada by the effect of the *Canada-United States Tax Convention Act, 1984*, SC 1984, c 20 [Tax Convention Act]. The plaintiffs have urged the Court to render its final decision and issue a permanent injunction before the taxpayer information is sent by the CRA to the Internal Revenue Service [IRS], otherwise the present action will become academic and the plaintiffs will suffer irreparable harm. Indeed, it is for this reason that the present motion for summary trial was specially scheduled by the Case Management Judge to be heard at a special sitting in Vancouver on August 4 and 5, 2015.

[6] On the contrary, the defendants submit that the collection of such relevant information is authorized by the IGA, and that its disclosure to the IRS is not inconsistent with the Canada-US Tax Treaty or in violation of section 241 of the ITA. Canada is required to transmit taxpayer information collected under the impugned provisions to the US for the year 2014 by September 30, 2015, and counsel for the defendants have indicated to the Court that to comply with this legal requirement, the CRA will in fact start to send such information to the IRS on or around September 23, 2015. Moreover, defendants' learned counsel indicated to the Court at the hearing of the present motion for summary trial that he had no instructions from the defendants to consent on a suspension of the contemplated exchange of information pending the time that the matter was in deliberation or that an appeal was pending (in case the Court would refuse the declaratory and injunctive relief requested by the plaintiffs in their motion for summary trial).

[7] I have read the motion records and supplementary motion records filed by the parties, and have considered all relevant and admissible evidence, and all the representations made at the hearing and in the written pleadings, including the relevant legal provisions and case law referred to by counsel. Parties agree that the issues raised by the plaintiffs in their motion are suitable for determination by summary trial and that the constitutional issues raised by the plaintiffs should be decided by the Court at a later date. In view of the urgency of the matter, the Court has accepted to render its final decision prior to September 23, 2015. That being said, measures are taken by the Court to have the present judgment translated in French on an urgent basis as well.

[8] In the event of any inconsistency between the provisions of the Tax Convention Act, or the Canada-US Tax Treaty, and the provisions of any other law, subsection 3(2) of the Tax

Convention Act provides that the provisions of the Tax Convention Act and the Canada-US Tax Treaty prevail to the extent of the inconsistency. Moreover, in the event of any inconsistency between the provisions of the IGA Implementation Act or the IGA and the provisions of any other law (other than Part XVIII of the ITA), subsection 4(1) of the IGA Implementation Act provides that the provisions of the IGA Implementation Act and the IGA prevail to the extent of the inconsistency.

[9] I have concluded that the collection and automatic disclosure of account holder information about US reportable accounts (see paragraphs 28 to 34 below) contemplated by Articles 2 and 3 of the IGA is legally authorized in Canada by the provisions of the IGA Implementation Act and Part XVIII of the ITA. Moreover, contrary to the assertions made by the plaintiffs, I find that the collection and automatic disclosure of any such information is not inconsistent with the provisions of the Canada-US Tax Treaty, and does not otherwise violate section 241 of the ITA. Basically, I endorse the general reasoning and the legal arguments submitted by the defendants in their written submissions and reasserted at the hearing by counsel.

Tax compliance and tax liability

[10] In every country and for every state, taxation fulfills its utilitarian and distributive purposes: to transfer money from the taxpayer's pocket to the public treasury, which will in turn satisfy the budgetary needs of the nation. Whether you see yourself as a conservative, a liberal or a libertarian, all taxpayers – natural or legal – must annually compute their income and declare it to the tax authorities. This is the law of the land: inescapable, inevitable and obligatory. But what

is the scope of one's fiscal liability, legally and practically speaking? Suppose no income is received during a particular year: is the taxpayer relieved of any statutory obligation to produce a declaration? What about persons having dual citizenship or multiple residences in different countries?

[11] The list of questions is endless as the particular situation of each taxpayer is infinitely variable. Not surprisingly, the answers will vary from one jurisdiction to another. It is all a matter of statutory construction and application. In a globalized world, practical reality, as well as political and economic considerations, will encourage countries to sign tax treaties.

[12] For example, whether a taxpayer can avail itself of a double taxation exception is a matter to be settled between the countries that have entered into a tax treaty. Indeed, Article XXIV of the Canada-US Tax Treaty exists for this specific purpose. At the time the Canada-US Tax Treaty was negotiated by the parties, it was deemed important to spare from double taxation a number of Canadian individuals working in the US (or vice versa), and Canadian companies operating in the US (or vice versa). As noted in 1995 by the Supreme Court of Canada (citing the US Senate (Foreign Relations Committee), Tax Convention and Proposed Protocols with Canada, at page 2): "The principal purposes of the proposed income tax treaty between the United States and Canada are to reduce or eliminate double taxation of income earned by citizens and residents of either country from sources within the other country, and to prevent avoidance or evasion of income taxes in the two countries". See *Crown Forest Industries v Canada*, [1995] 2 SCR 802 at page 823 [*Crown Forest Industries*].

[13] The Christians expert report provides examples of “Tax Treaty Gaps” with respect to the differential treatment accorded in Canada and in the US to the sale of a principal residence, lottery winnings or strike pay, passive income losses, non-US corporations, and non-US trusts, which can lead to “timing issues”, as well as certain other taxes that may not be eligible for offset by foreign taxes via credit (Christians expert report, pages 7-10). Be that as it may, while gaps or differences in the treatment of certain situations by the US and Canadian tax authorities have been raised by the parties, it is not a matter that needs to be addressed in this summary trial. In exercising its competent authority power to exchange taxpayer information with a treaty partner, the Minister – in practice the CRA – does not consider whether a Canadian taxpayer whose information is subject to exchange (whether automatic or otherwise) would have an impact on a tax liability in the receiving state (Murray affidavit, paragraph 18).

[14] The issue to be considered in this summary trial is notably whether the information exchanged under the IGA is “foreseeably relevant”. Under paragraph 1 of Article XXVII of the Canada-US Tax Treaty, “information may be exchanged for use in all phases of the taxation process including assessment, collection, enforcement or the determination of appeals”. See the technical explanation to the Fifth Protocol, dated September 21, 2007, article 23, page 47. According to the evidence submitted by the defendants, financial information from a foreign jurisdiction about individuals who are, or who display indicia of being, tax residents is useful to a tax administrator even if the information does not lead to increased tax liabilities in the receiving State for all taxpayers identified. Information that the CRA receives from treaty partners assists the CRA with its offshore compliance work, risk assessment, workload development, trend

analysis and other matters relevant to ensuring compliance with Canada's tax laws (Murray affidavit, paragraph 21).

[15] Determining the relevance of information exchanged under the Canada-US Tax Treaty is an administrative matter usually left to the discretion of the tax authorities themselves. From a practical point of view, relevance is mostly related to the identification of various "income sources" in the competent jurisdiction. Residency indicia (which may include citizenship status in the US) will be searched by the tax authorities (cross-examination of Sue Murray at pages 191 and following). The automatic exchange of information is valuable because of its usefulness in conducting risk assessment and in identifying taxpayers with potential compliance issues, and it is increasingly being used worldwide, as illustrated by the evidence submitted with the Smith affidavit. In the present case, the Court has been advised that IRS officials have communicated to CRA officials that the information that Canada will exchange with the US pursuant to the IGA will be highly relevant to the administration of US domestic tax laws for similar reasons (Murray affidavit, paragraph 22). Given the CRA's experience exchanging information with treaty partners, the Director of the Competent Authority Services Division of the CRA has sworn that she has no reason to doubt this IRS Assertion (Murray affidavit, paragraph 22).

Taxpayers' obligations under Canada and US Tax laws

[16] Under the ITA, an income tax shall be paid, as required by that Act, on the taxable income for each taxation year of *every person resident in Canada* at any time of year (subsection 2(1) of the ITA). Moreover, *a non-resident person in Canada* who was employed in Canada, carried on a business in Canada, or disposed of a taxable Canadian property at any time in the

year or a previous year, will pay tax on the taxable income determined in accordance with the particular rules found in Division D of the ITA. That being said, notwithstanding any provision of the ITA, where the Minister and another person have, under a provision contained in a tax convention or agreement with another country that has the force of law in Canada, entered into an agreement with respect to the taxation of that other person, all determinations made in accordance with the terms and conditions of the agreement shall be deemed in accordance with the ITA (subsection 115.1(1) of the ITA).

[17] On the other hand, under US domestic law, **all US citizens are deemed to be permanent tax residents in the US for federal income tax purposes – regardless of whether or not they actually reside in the US.** “US persons” who are subject to US tax laws also include other categories of persons who reside in the US such as green card holders. Accordingly, every Canadian resident who is a US citizen, even if he or she is also a Canadian citizen, is subject to US federal taxation on all of their income from all sources, wherever derived. US persons are also subject to various tax reporting obligations, which include registering for a taxpayer identification number [TIN], filing annual tax returns, reporting income and computing US tax payable. Under US tax laws, the obligation to file income tax returns and to comply with reporting requirements is not always dependent on the existence of an actual tax liability for a particular year.

[18] The IRS uses offshore voluntary disclosure programs targeting presumed hidden offshore wealth held by US residents as a soft administrative approach to combat tax evasion, but such programs may be ineffective in many cases. Should some type of “dragnet” approach be taken to

combat tax evasion instead? Obviously, the US Congress has investigated this direction in recent years. The *Foreign Account Tax Compliance Act* [FATCA], passed in 2010 as part of the *Hiring Incentives to Restore Employment Act*, Pub. L. No. 111-147, 124 Stat. 71, and codified in pertinent part as I.R.C. §6038D, imposes reporting obligations both on US persons directly, and on foreign financial institutions at which US persons hold certain types of accounts. More particularly, FATCA imposes a thirty percent withholding tax on foreign financial institutions that do not meet the reporting requirements.

[19] US citizens are required to report information regarding foreign bank and financial institution accounts in various forms. According to the expert report of John P. Steines, US persons are required to file an annual income tax return (Form 1040, as well as supporting schedules and forms), which includes the taxpayer's name, address, taxpayer identification number, items of income, deduction and credit, and resulting tax liability (Steines expert report, page 5). Schedule B of Form 1040 also requires the disclosure of information pertaining to foreign bank accounts, including: whether the taxpayer has a financial interest or signature authority over a financial account located in a foreign country; whether a taxpayer is required to file a *Report of Foreign Bank and Financial Accounts* – or Form 114 [FBAR]; the name of the country in which the foreign account is located; and other information related to foreign trusts. Schedule B of Form 1040 is an obligation that pre-dates FATCA (Steines expert report, pages 5-6).

[20] The Steines report also details the requirement for US persons who meet certain reporting thresholds to file Form 8938, created pursuant to FATCA, which also relates to foreign bank account information and must accompany Form 1040 (page 6). This information includes:

- The name, mailing address and identification number of the foreign financial institution;
- The name, address and US taxpayer identification number of the owner of the account;
- The account type and number or other designation;
- Whether the account was opened or closed during the year;
- Whether the account is held jointly with a spouse;
- The maximum account value during the year; and
- Whether a foreign exchange rate was used to convert the account value into US dollars (along with the rate and source of the rate).

[21] The failure to file Form 8938 in a timely manner can result in a financial penalty of \$10,000, which is increased by \$10,000 for each month the failure to file remains uncured after a 90-day written notice period (up to a maximum of \$50,000) (*Internal Revenue Code* §6038D(d)-(e)).

[22] In addition to the requirement to file annual income tax returns, the Steines report notes that US citizens who hold or have signatory power over a financial account in excess of \$10,000 at any time during the year are required to file an FBAR. The FBAR also pre-dates FATCA. The FBAR must be filed to the Financial Crimes Enforcement Network of the US Treasury Department. It must disclose (Steines expert report, page 7):

- The name, mailing address, and identification number of the foreign financial institution;
- The type of filer, name, mailing address, US taxpayer identification number, birthdate, and whether the account is jointly owned;
- Whether the filer has a financial interest in 25 or more financial accounts;
- Whether the filer has signatory power but no financial interest in 25 or more financial accounts;
- The account number or other designation;
- The type of account; and
- The maximum value of the account during the calendar year.

[23] If failure to file an FBAR is willful, the maximum penalty will be the greater of \$100,000 or 50% of the account balance that was not disclosed (31 U.S. Code §5321(a)(5)(C)-(D); Steines expert report, footnote 22). In addition, penalties are for each violation, and multiple violations can occur if they involve multiple offices, branches or places of business (31 U.S. Code §5321(a)(1); Steines expert report, footnote 22).

[24] As Professor Christians notes in her expert report, Canadian residents who have US person status and who contribute to or are beneficiaries of certain savings vehicles (including some RESPs, RDSPs and TFSAs) may also be required to file an “Annual Information Return of Foreign Trust with a US Owner” (Form 3520A) or an “Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts” (Form 3520), or both (Christians expert report, para 13). Failure to file these forms attracts financial penalties, whether or not any tax is due (IRC §6048(b)(1) and IRC §6677; (Christians expert report, paragraph 13).

[25] Canadian residents who have US person status and who invest in certain Canadian mutual fund companies or who are directly or indirectly controlling shareholders of Canadian corporations (including small business corporations) may also be required to file Form 5471 (IRC §6038, 6046 and regulations thereunder; Christians expert report, paragraph 13). Canadian residents who have US person status and who own interests in certain Canadian mutual funds and other investment vehicles may be required to annually file Form 8621 (IRC §1298(f); Christians expert report, paragraph 13). Finally, Canadian residents with US person status and who own interests in, make transfers to, or receive income, dispose of, or change their interests in certain Canadian partnerships may be required to file Form 8865. Failure to file in each of these cases may lead to financial penalties (IRC §6038; 6038B; 6046A; Christians expert report, paragraph 13).

[26] As can be seen, under US laws, a failure to comply with reporting obligations exposes a US person to penalties. Nor do the filing obligations mentioned above constitute an exhaustive list. Indeed, “[r]egardless of whether any tax is due, the US requires extensive tax and asset reporting documentation, for which noncompliance attracts extensive penalties” (Christians expert report, paragraph 10). The US Government is not a party to the present proceeding. The Court is not in a position at the present time to determine whether the US tax authorities will in fact take action against the plaintiffs or other US persons having dual citizenship or residing in Canada if the taxpayer information mentioned in the IGA is disclosed by the CRA to the IRS. Furthermore, before any collection step is taken, the amount of income tax, penalties or interest due must be first assessed (possibly leading to a particular request for information under the Canada-US Tax Treaty). Accordingly, in the absence of concrete evidence, it is speculative to

suggest that the automatic collection and disclosure of taxpayer information mentioned in the IGA is tantamount to providing help to the US authorities in the collection of taxes.

Scope and effect of the impugned provisions

[27] Under the Intergovernmental Agreement concluded in 2014 by the governments of Canada and the US, for the purpose of implementing the obligations to obtain and exchange information with respect to reportable accounts, as specified in Article 1 (subparagraph 1(ee)) of the IGA, the term “US person” means:

“The term “U.S. Person” means:	Le terme « personne des États-Unis » désigne :
(1) a U.S. citizen or resident individual,	(1) une personne physique qui est un citoyen ou un résident des États-Unis;
(2) a partnership or corporation organized in the United States or under the laws of the United States or any State thereof,	(2) une société de personnes ou une société constituée aux États-Unis ou selon la législation de ce pays ou d’un de ses États;
(3) a trust if	(3) une fiducie si, à la fois :
(A) a court within the United States would have authority under applicable law to render orders or judgments concerning substantially all issues regarding administration of the trust, and	(A) un tribunal des États-Unis aurait la compétence, selon le droit applicable, de rendre des ordonnances ou des jugements concernant la presque totalité des questions liées à l’administration de la fiducie,
(B) one or more U.S. persons have the authority to control all substantial decisions of the trust, or	(B) une ou plusieurs personnes des États-Unis jouissent d’un droit de contrôle sur toutes les décisions importantes de la fiducie;

(4) an estate of a decedent that is a citizen or resident of the United States.	(4) la succession d'un défunt qui est citoyen ou résident des États-Unis.
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This subparagraph 1(ee) shall be interpreted in accordance with the U.S. Internal Revenue Code.	Le présent alinéa ee) est interprété conformément à l'Internal Revenue Code des États-Unis.
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[28] Article 2 of the IGA imposes reciprocal obligations on each party, requiring the governments of Canada and the US to collect account holder information about reportable accounts at both Canadian and US reporting financial institutions. On the Canadian side, Part XVIII of the ITA – sections 263 through 269 – imposes obligations on certain Canadian financial institutions [reporting institutions] to implement the due diligence procedures outlined in Annex I of the IGA in order to identify US reportable accounts for the purposes of the IGA. The due diligence procedures followed by Canadian financial institutions require them to search their account records for indications that the account holder is a US person [US person indicia]. US person indicia include a US place of birth or a current US mailing or residential address.

[29] The list of Canadian financial institutions is comprehensive and is defined in Article 1 (paragraph 1)) of the IGA as meaning:

(1) any Financial Institution that is resident in Canada, but excluding any branch of such Financial Institution that is located outside Canada, and	(1) toute institution financière qui réside au Canada, à l'exclusion de ses succursales situées à l'extérieur du Canada;
(2) any branch of a Financial Institution that is not resident in Canada, if such branch is located in Canada.	(2) toute succursale, située au Canada, d'une institution financière qui ne réside pas au Canada.

[30] In practice, the due diligence and reporting requirements found in the IGA (and correlatively in Part XVIII of the ITA) affect provincially and federally regulated financial institutions. Paragraph 263(1) of the ITA defines a “listed financial institution” as meaning:

“listed financial institution” means a financial institution that is	« institution financière particulière » Institution financière qui est, selon le cas :
(a) an authorized foreign bank within the meaning of section 2 of the <i>Bank Act</i> in respect of its business in Canada, or a bank to which that Act applies;	a) une banque régie par la Loi sur les banques ou une banque étrangère autorisée, au sens de l’article 2 de cette loi, dans le cadre des activités que cette dernière exerce au Canada;
(b) a cooperative credit society, a savings and credit union or a caisse populaire regulated by a provincial Act;	b) une coopérative de crédit, une caisse d’épargne et de crédit ou une caisse populaire régie par une loi provinciale;
(c) an association regulated by the <i>Cooperative Credit Associations Act</i> ;	c) une association régie par la <i>Loi sur les associations coopératives de crédit</i> ;
(d) a central cooperative credit society, as defined in section 2 of the <i>Cooperative Credit Associations Act</i> , or a credit union central or a federation of credit unions or caisses populaires that is regulated by a provincial Act other than one enacted by the legislature of Quebec;	d) une coopérative de crédit centrale, au sens de l’article 2 de la <i>Loi sur les associations coopératives de crédit</i> , ou une centrale de caisses de crédit ou une fédération de caisses de crédit ou de caisses populaires régie par une loi provinciale autre qu’une loi édictée par la législature du Québec;
(e) a financial services cooperative regulated by <i>An Act respecting financial services cooperatives</i> , R.S.Q., c. C-67.3, or <i>An Act respecting the Mouvement Desjardins</i> , S.Q. 2000, c. 77;	e) une coopérative de services financiers régie par la <i>Loi sur les coopératives de services financiers</i> , L.R.Q., ch. C-67.3, ou la <i>Loi sur le Mouvement Desjardins</i> , L.Q. 2000, ch. 77;
(f) a life company or a foreign	f) une société d’assurance-vie

life company to which the <i>Insurance Companies Act</i> applies or a life insurance company regulated by a provincial Act;	ou une société d'assurance-vie étrangère régie par la <i>Loi sur les sociétés d'assurances</i> ou une société d'assurance-vie régie par une loi provinciale;
(g) a company to which the <i>Trust and Loan Companies Act</i> applies;	g) une société régie par la <i>Loi sur les sociétés de fiducie et de prêt</i> ;
(h) a trust company regulated by a provincial Act;	h) une société de fiducie régie par une loi provinciale;
(i) a loan company regulated by a provincial Act;	i) une société de prêt régie par une loi provinciale;
(j) an entity authorized under provincial legislation to engage in the business of dealing in securities or any other financial instruments, or to provide portfolio management, investment advising, fund administration, or fund management, services;	j) une entité autorisée en vertu de la législation provinciale à se livrer au commerce des valeurs mobilières ou d'autres instruments financiers ou à fournir des services de gestion de portefeuille, de conseils en placement, d'administration de fonds ou de gestion de fonds;
(k) an entity that is represented or promoted to the public as a collective investment vehicle, mutual fund, exchange traded fund, private equity fund, hedge fund, venture capital fund, leveraged buyout fund or similar investment vehicle that is established to invest or trade in financial assets and that is managed by an entity referred to in paragraph (j);	k) une entité qui est présentée au public comme étant un mécanisme de placement collectif, un fonds commun de placement, un fonds négocié en bourse, un fonds de capital-investissement, un fonds spéculatif, un fonds de capital-risque, un fonds de rachat d'entreprise par effet de levier ou un mécanisme de placement similaire qui est établi pour faire des investissements dans des actifs financiers, ou le commerce de tels actifs, et qui est géré par une entité visée à l'alinéa j);
(l) an entity that is a clearing house or clearing agency; or	l) une entité qui est une chambre ou une agence de

compensation;

<p>(m) a department or an agent of Her Majesty in right of Canada or of a province that is engaged in the business of accepting deposit liabilities.</p>	<p>m) un ministère ou un mandataire de Sa Majesté du chef du Canada ou d'une province qui se livre à l'acceptation de dépôts.</p>
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[31] However, some categories of financial institutions have reduced requirements (such as small deposit-taking institutions and those that only serve local clients or only issue credit cards). In addition, very small deposit taking institutions with assets of less than \$175 million may be exempted from reporting. See the definition of “non-reporting Canadian financial institution”, paragraph 263(1) of the ITA and Annex II of the IGA.

[32] An account is not reportable if it falls within an exempt category (such as certain government registered plans) or if its value is below certain thresholds. With respect to each US reportable account, the information that Canada must collect under the IGA from Canadian financial institutions includes:

- (a) The name and address of each US person or person associated with a US person indicia that is an account holder;
- (b) The TIN of each US person or person associated with a US person indicia that is an account holder, or if a TIN is not in the records of the Canadian financial institution, the account holder's birthdate;
- (c) The name and identifying number of the Canadian financial institution;
- (d) The account number and balance of the account; and

- (e) The gross amount of interest, dividends and other income generated by the account or the assets held in the account, including the gross proceeds from the sale or redemption of any property held in the accounts.

[33] Every reporting Canadian financial institution is compelled by law to submit itself to the due diligence procedures set out in subsections 265(2) and (3) of the ITA which apply in respect of pre-existing and new individual accounts, and to designate any US reportable account (see sections 264 and 265 of the ITA). Financial institutions already have a legal responsibility to determine where an account holder resides for tax purposes. If a customer has an existing account and there is an indication that they may be a US person, or if they are opening new bank accounts, their financial institution may ask them to provide additional information or documentation to demonstrate that they are not a US person (or to self-certify that they are or are not a US person for tax purposes). Indeed, every reporting Canadian financial institution shall keep, at the institution's place of business (or at such other place as may be designated by the Minister), records that the institution obtains or creates for the purpose of complying with Part XVIII of the ITA, including self-certifications and records of documentary evidence.

[34] The reporting institutions must annually file with the Minister – that is, with the CRA – prescribed information about each reportable account maintained by the financial institution, as well as prescribed information relating to payments made to non-participating financial institutions that held accounts at the financial institution in the calendar year (for 2015 and 2016 only). The information must be reported in an information return filed for each calendar year by May 2 of the following year (section 266 of the ITA). Apparently, the CRA has not issued a

particular form for Canadian financial institutions to use (no such form was produced by the CRA affiants in this proceeding). The CRA will then annually turn the information it collects over to the IRS in bulk “on an automatic basis pursuant to the provisions of Article XXVII of the [US-Canada Tax Convention]” (Article 2, paragraph 1, of the IGA).

Facts directly leading to the present litigation

[35] The conclusion of the IGA between the Government of Canada and the US was announced to the public on February 5, 2014, along with a call for comments on the detailed draft legislative proposals and accompanying explanatory notes in respect of changes to the *Income Tax Act* to implement the IGA. The deadline for comments was March 10, 2014. The IGA Implementation Act was included as part of Bill C-31 (publicly announced by the Government of Canada as the "Harper Government Creating Jobs & Growth While Returning to Balanced Budgets With *Economic Action Plan 2014 Act, No. 1*") – an omnibus budget bill of some 360 pages. The first reading of Bill C-31 in the House of Commons occurred on March 28, 2014, and the bill received royal assent on June 19, 2014.

[36] The wisdom of the impugned provisions was questioned by the opposition and a number of players – including citizen groups, prominent legal scholars, and affected individuals – who made their objections or reservations public at the time Bill C-31 was debated in Parliament. Many expressed concern that the impugned provisions would unduly harm the privacy rights and interests of all Canadians; unduly raise compliance costs to all Canadian financial institutions and Canadian taxpayers; impede Canada’s efforts to enforce its own tax laws; and violate the spirit and potentially the letter of a number of Canadian laws and international treaties.

Opposition party members also called for the IGA Implementation Act to be removed from the omnibus budget bill to allow for greater scrutiny.

[37] On the other hand, the Canadian Bankers Association – who acts on behalf of 60 domestic banks, foreign bank subsidiaries and foreign bank branches operating in Canada – supported the policy choice made by the Government of Canada to sign the IGA and pass federal implementing legislation allowing financial institutions to legally collect taxpayer information in Canada to comply with FATCA requirements. Their motivation was simple. Many Canadian financial institutions (not only federal banks but also credit unions and other provincial institutions) were potentially facing various legal impediments in Canada to disclosing their client information to the IRS. Accordingly, those institutions were at risk of breaching Canadian domestic law in order to comply with FATCA and avoid the thirty percent withholding tax on any US source income and the sale of any US source investments (including Canadian source income due to so-called “foreign pass-through payments” provisions).

[38] The following excerpts from the Proceedings of the Standing Senate Committee on National Finance illustrate how the IGA was framed by Mr. Ernewein, the General Director, Tax Policy Branch, Department of Finance:

(Issue 10 - Evidence - April 29, 2014)

[Regarding the IGA]

Senator Bellemare: Did financial institutions have a positive reaction to that?

Senator Hervieux-Payette: No.

Senator Bellemare: Were they consulted?

Mr. Ernewein: Yes. I guess the answer is yes, but the reason for my hesitation is that I don't think they love it. I think they like it better than the alternative, that FATCA itself, as I described, would have put them in a difficult if not impossible situation with being required by U.S. law to provide information directly to the IRS that might have been in direct conflict with Canadian privacy laws, if not other laws.

If they were being direct, I think they would probably say they would rather not do this at all, but as between this and the FATCA itself, I think they consider it a much better setup in the sense that it carves out all the registered plans, it excludes the application of the rules to smaller financial institutions, and by virtue of the collection of information by our own Canadian revenue authorities and transmission to the U.S., it overcomes, in our view, some of the legal conflict concerns that would have otherwise existed.

(Issue 10 - Evidence - April 30, 2014)

[Regarding the withholding tax]

Senator Buth: Is it because Canadian banks have U.S. operations that they can do this? I guess I'm having a hard time understanding how a foreign country can regulate what a Canadian bank does.

Mr. Ernewein: As a policy matter, we very much share that question, and certainly former Finance Minister Flaherty was very public about criticizing it on that basis. I guess the second part of that answer is that what we were seeking to do with the intergovernmental agreement was to work around that approach and come at it a different way on exchange of information and not the threat of withholding. The U.S. has always maintained that this is about information exchange and not about trying to collect tax, at least through the withholding tax mechanism. It's an exchange of information and taxpayer compliance, and I think what we've got in this intergovernmental agreement is more consistent with that stated purpose than FATCA itself or the approach FATCA put forward.

Senator Buth: What would have happened if we had not done this agreement, then? Let me ask another question. Are the banks supportive of this legislation?

Mr. Ernewein: Yes. That's my summary answer, and I'll give the same sort of elaboration as I did yesterday, which is that I don't think they're tickled by any of this. I think they believe, even in what we've done, that it will introduce compliance burdens for

them and extra obligations for their clientele, but I think they are much more at peace, if I may put it that way, with this intergovernmental agreement and the approach it takes than with FATCA. Again, I'm hesitant to speak for them, but I have some confidence saying that I think they found FATCA essentially unworkable, and this was workable, although perhaps not what they would have designed for themselves.

[39] But what about Canadian taxpayers? How many have been or will be affected by the impugned provisions? An official figure has not been provided by the defendants and much depends on the extent of information being collected by Canadian financial institutions. How will Canadian financial institutions verify in practice if an individual account holder is a US citizen? Will they ask for proof of birth (showing birthplace), in addition to asking for proof of actual residency (like a driver's licence or other reliable evidence of permanent residence)? Under the IGA and Part XVIII of the ITA, there is no express requirement for a Canadian financial institution to provide notice to its consumers that this information is being collected on US persons for eventual sharing by the CRA with US tax authorities. Each Canadian financial institution has its own policies and procedures with respect to the collection and disclosure of personal information. Will they allow account holders to have access to the personal information that has been reported under the due diligence procedure outlined in the IGA? While we have no answers to these questions, Canadians will have a better idea of the impact of the impugned provisions after September 30, 2015. Before the Senate, a figure of 1 million potentially-impacted individuals was invoked in 2014. According to the cross-examination of Professor Christians (July 23, 2015), there are between 750,000 and 2 million individuals falling within the definition of "US persons" currently present in Canada who could be affected by the impugned provisions. As the plaintiffs note, the impugned provisions also capture those persons who are

“accidental Americans”, “snowbirds”, “green card holders”, and those who hold joint accounts with their US spouses.

The plaintiffs’ perspective and how the Court must approach the present case

[40] The present plaintiffs, Gwendolyn Deegan [Gwen] and Virginia Hillis [Ginny], possess dual citizenship. Gwen was born in Washington State in 1962 to an American citizen and a Canadian citizen; she has not resided in the US since she was five years old. Ginny was born in Michigan in 1946 to two Canadian citizens; she has not resided in the US since she was six years old. They have never held a US passport and have never applied for one. When they travel to the US, they use the only passport they possess, which is Canadian. Neither one of them has ever worked in the US; all their employment has been in Canada where they have paid income tax every year. They do not hold a TIN and they have never declared or paid any taxes in the US. As far as they know, they do not owe any US taxes.

[41] The plaintiffs readily recognize that they are US persons. But they consider that they have “no real connection” with the US and that their US citizenship is “an accident of birth and of little significance”. However, they are not ready to apply for a certificate of loss of nationality in order to relinquish their US citizenship – firstly, because it would allegedly be extremely expensive, and secondly, because it would require them to complete years’ worth of disclosure statements and tax returns, and possibly be subject to various penalties for not having filed these statements and returns over the years.

[42] The plaintiffs do not challenge the fact that they hold US reportable accounts, but object to having their account holder information communicated by the CRA to the IRS. Instead of seeking a personal exemption directly from the CRA or the IRS, the plaintiffs have instituted the present action seeking some sort of general declaration for the benefit of all Canadian citizens or residents who are considered US persons under US domestic law, as well as a permanent prohibitive injunction to prevent the disclosure of any such account holder information. I doubt that such kind of judicial relief can be granted generally by the Court, but it is not necessary for me to deal specifically with this issue since the plaintiffs have not convinced me that the proposed disclosure of taxpayer information mentioned in the IGA is contrary to the provisions of the Canada-US Tax Treaty or in violation of section 241 of the ITA.

[43] The plaintiffs submit that the impugned provisions are unprecedented in Canadian history and represent a significant departure from long-standing tax treaties in the past. The plaintiffs consider that US citizens who are *bona fide* residents of Canada should bear no fiscal obligations to the US: there should be no taxation without representation. The plaintiffs stress that the US is apparently the only country in the world, and certainly the only country with a robust tax system such as Canada's, that comprehensively treats individuals as residents for tax purposes by virtue of their status as citizens or legal permanent residents. Eritrea – a country in the Horn of Africa that has been governed by an autocratic government since its independence in 1993 – is the only other country known for attempting to impose taxes on citizens who live permanently outside the country, although the US, Canada and other countries have rejected the right of Eritrea to collect this tax. During oral pleadings in this summary trial proceeding, counsel for the plaintiffs suggested that there may have been a historical justification for the US Government to tax its

citizens during the American Civil War, but argued that it is highly unjust to continue to do so today.

[44] According to the evidence on record, it is not true that under US domestic law US citizens who are *bona fide* residents of Canada bear no fiscal obligations to the US. Being a citizen of any state normally carries benefits (e.g. the right to enter or exit the country freely, diplomatic assistance, etc.). There are also obligations, some of which may be obvious and others less obvious, especially in the case of dual citizenship where an individual has never held a passport, worked, or declared revenues in their birth country. At this point in time, the Court is not in a position to make a general declaration having the legal effect of exempting all Canadian citizens from the application of US tax laws on the basis of the double taxation exception. That said, I fully appreciate the difficult situation that the plaintiffs – along with hundreds of thousands of dual citizens and permanent residents of Canada – may face after September 30, 2015.

[45] The plaintiffs may see themselves as “accidental Americans” but the application of fiscal law is not concerned with rhetoric: it focuses on the actual reality of each taxpayer and his or her taxable income. There cannot be a proper assessment of the situation if “relevant information” needed to decide whether an income is taxable or not is voluntarily withheld by taxpayers who have not produced their declaration or who have failed to declare all their sources of income worldwide, assuming that reporting obligations ensure compliance with fiscal laws. The environment created in Canada and the US by their respective domestic tax laws, including FATCA and the impugned provisions with all their reporting obligations, is certainly harsh, but it

is now the law of the land. Perhaps US persons will seriously consider abandoning or relinquishing their Canadian or US citizenship. This will be a voluntary choice. Still, the Court must apply the laws enacted by Parliament. The characteristics of these laws – whether wise or unjust – are a matter for political debate, not judicial scrutiny. Parliament is sovereign; the will of people in a democracy is also sovereign.

[46] Whether or not Canada is a destination for persons evading US taxes is not pertinent. Generally, FATCA imposes penalties on US persons, as well as a thirty percent withholding tax on foreign financial institutions, who do not comply with the reporting requirements. More particularly, FATCA requires US persons holding reportable accounts at foreign financial institutions to report information on Form 8938 attached to their annual tax return. The information includes details such as the name, address and TIN of the owner of the account, details as to whether the account is held jointly with a spouse, whether the account was opened or closed during the year, and the maximum account value during the year.

[47] For the time being, the US Government has not been willing to conclude bilateral agreements with other states exempting FATCA compliance based on the same country exception, which would have the effect of excluding financial accounts maintained by a financial institution in the country in which the US person is a *bona fide* resident. On the other hand, any private banking information respecting US persons covered by FATCA living in Canada (or elsewhere outside the US) could hardly be provided to the IRS legally in the absence of an agreement and domestic legislation allowing for its collection and automatic disclosure to a foreign authority.

[48] The threat of imposing a thirty percent withholding tax on US source income for financial institutions that do not comply with FATCA reporting obligations has certainly constituted an important instrument of persuasion in the international community. Not surprisingly, the financial implications of FATCA have incited sovereign states to conclude with the US agreements similar to the IGA. Indeed, intergovernmental agreements have apparently been reached with nearly 115 different states in order to facilitate FATCA compliance.

[49] I am ready to assume that the Canadian and OECD common reporting standards differ in two significant ways from the FATCA requirements: one, they are triggered by residency (versus citizenship); and two, they do not entail the same sanctions (i.e. withholding tax) in case of non-compliance. That said, automatic exchanges of information are not prohibited or unprecedented (see the examples cited in the Smith affidavit). In 2014, the Government of Canada made the political decision to participate in an automatic exchange of information scheme with the US Treasury Department, which imposes obligations for the reporting and exchange of relevant information largely based on the architecture of FATCA. These obligations have not been reciprocated in Canadian law, which continues to tax on the principles set out in section 2 of the ITA. For this reason, as suggested by professor Christians, the expression “asymmetrical exchange of information” would appear more adequate.

[50] Be that as it may, the stated purpose of FATCA is to improve US tax compliance by obtaining information from foreign financial institutions about accounts maintained by US taxpayers, directly or through intermediary entities. The American authorities were particularly concerned in 2010 with the issue of tax evasion. Nevertheless, a statute should not be interpreted

by politicians' statements used to rally public opinion, but rather by its object and the words used by the legislator. Legally speaking, it is apparent that FATCA has overreaching effects in practice. The CRA officials have the same understanding with respect to the collection and reporting requirements created by the IGA and Part XVIII of the IGA, which only mirror FATCA requirements. And so does this Court, after having examined the impugned provisions in light of US domestic laws referred to by the experts in their various reports and answers to questions by counsel during cross-examinations.

[51] Nor is it necessary to decide whether the IGA is a "treaty" under US law. While the status of the IGA as law in the US may be ambiguous – the US Treasury has decided to treat these types of intergovernmental agreements not as treaties but merely as interpretations of treaty terms – as far as Canada is concerned, by the effect of section 3 of the IGA, the IGA is approved by Parliament and has the force of law in Canada during all the period it is in force. In Canadian domestic law at least, the IGA constitutes a tax treaty or a listed agreement within the meaning of subsection 241(4) of the ITA. Detractors of the IGA may wish to question the legal application in the US of the IGA on the grounds that it has not been ratified by Congress – a point that the Court is not called upon to decide today. The IGA is certainly a treaty from the Canadian perspective. At worst, the IGA is still a binding agreement between the US and Canada respecting the interpretation or application of the Canada-US Tax Treaty, and as such may be considered in interpreting the latter, which is a treaty pursuant to the *Vienna Convention on the Law of Treaties*, Can. TS 1980 No. 37.

[52] Much has been said by Plaintiffs' learned counsel about the extraterritorial nature of US laws. It is also well settled "that in no circumstances will the Court directly or indirectly enforce the revenue laws of another country", unless expressly allowed to do so in the home country of the person in question (*United States of America v Harden*, [1963] SCR 366 at p 370, citing the relevant case law in this regard). It is true that through FATCA, Congress has attempted to make extraterritorial claims over individuals having the status of US persons. It is true that the IGA requires Canada's explicit assistance with a foreign sovereign's extraterritorial jurisdiction. And it is true that the threat of economic sanctions is a serious matter that deserves international scrutiny where it is exercised.

[53] In this respect, the parties to the Canada-US Tax Treaty are cognisant that Canada and the US are sovereign countries. Indeed, Part XVIII of the ITA has been enacted by Parliament and has been legally in force in Canada since June 19, 2014, the day on which the IGA Implementation Act came into force. Sections 266 to 269 of the ITA must be respected and the obligations contracted by Canada under Article 2 of the IGA must be carried out and enforced domestically. In the case of non-compliance, if the matter is not resolved in the 18 month delay mentioned in the IGA, the US shall treat the reporting Canadian financial institution as a non-participating financial institution (Article 5, subparagraph 2(b) of the IGA).

[54] The Government of Canada purports to legally authorize, under subsection 241(4)(e)(xii) of the ITA, the disclosure by the CRA to the IRS of all taxpayer information collected by financial institutions pursuant to Part XVIII of the ITA. The latter provision allows an official of the CRA – as defined in subsection 241(10) – to disclose information, allow access to

information, or allow the inspection of information pursuant to a provision “for the purposes of [...] a provision contained in a tax treaty with another country or in a listed international agreement” (ITA subsection 241(4)(e)(xii)). Is this exchange scheme legal?

The interpretation issue raised by the plaintiffs

[55] In exercising its competent authority power to exchange taxpayer information with a treaty partner, the CRA does not consider whether a Canadian taxpayer whose information is subject to exchange – whether automatic or otherwise – would have an impact on a tax liability in the receiving state. That being said, the defendants assured the Court that Canadian citizens or persons residing permanently in Canada will continue to enjoy the protections mentioned in the Canada-US Tax Treaty. Although this treaty does not prevent the collection and the automatic disclosure of taxpayer information mentioned in Article 2 of the IGA with respect to US reportable accounts mentioned in section 264 of the ITA, the defendants take the position that the IRS cannot use such information to administer non-tax laws (such as the *US Bank Secrecy Act*) or in its dealings with federal entities (such as the Financial Crimes Enforcement Network of the US Treasury Department) who are involved in money laundering repression. Indeed, the CRA will not assist the US in collecting non-tax related penalties such as penalties for failing to file the FBAR. Moreover, while the Canada-US treaty says that Canada may assist the US in collecting certain taxes, it also says that the Canadian authorities will not assist the US authorities in collecting a US tax liability if the person was a Canadian citizen when the liability arose.

[56] The plaintiffs respectfully disagree with the defendant's broad interpretation of the impugned provisions. Indeed, they consider that under the terms of the Canada-US Tax Treaty, the exceptions to the confidentiality rule found in section 241 of the ITA do not apply to the exchange of the information collected by Canadian financial institutions under Part XVIII of the ITA (sections 263 to 269). The plaintiffs' fundamental proposition is that the Canada-US Tax Treaty limits the collection and automatic disclosure of account holder information relating to a taxable period in which the taxpayer was a citizen of Canada. Overall, the plaintiffs submit that the terms of the IGA and the Canada-US Tax Treaty can be read in harmony. Thus, the paramountcy clauses contained in both the IGA Implementation Act and the Tax Treaty Act are not engaged because there is no conflict. The plaintiffs underline that the express terms of the IGA indicate that it is subject to the provisions of the Canada-US Tax Treaty. Accordingly, Canada can comply with both the impugned provisions and the Canada-US Tax Treaty by collecting account holder information pursuant to the IGA, and disclosing it pursuant to the terms of the Canada-US Tax Treaty. I have closely examined the plaintiffs' submissions in this regard, and, in final analysis, find them unfounded in law or in fact. For the sake of clarity, they can be briefly summarized as follows.

[57] First, the plaintiffs rely on Article XXVI A of the Canada-US Tax Treaty which states that Canada may not provide the US with assistance in the collection of revenue claims to the extent that the taxpayer in question was a citizen of Canada at the time the revenue claim arose. More particularly, they refer to paragraphs 1 and 8 which read as follows:

1. The Contracting States	Les États contractants
undertake to lend assistance to	s'engagent à se prêter
each other <u>in the collection of</u>	mutuellement assistance <u>pour</u>
<u>taxes</u> referred to in paragraph	<u>percevoir les impôts</u> visés au

9, together with interest, costs, additions to such taxes and civil penalties, referred to in this Article as a "revenue claim".

paragraphe 9, ainsi que les intérêts, frais, impôts supplémentaires et pénalités civiles, dénommés, « créances fiscales » dans le présent article.

[...]

[...]

8. No assistance shall be provided under this Article for a revenue claim in respect of a taxpayer to the extent that the taxpayer can demonstrate that

8. L'assistance prévue par le présent article n'est pas fournie à l'égard d'une créance fiscale concernant un contribuable si celui-ci peut établir que,

(a) where the taxpayer is an individual, the revenue claim relates either to a taxable period in which the taxpayer was a citizen of the requested State or, if the taxpayer became a citizen of the requested State at any time before November 9, 1995 and is such a citizen at the time the applicant State applies for collection of the claim, to a taxable period that ended before November 9, 1995; and

a) lorsque le contribuable est une personne physique, la créance fiscale concerne soit une période imposable au cours de laquelle le contribuable était un citoyen de l'État requis ou, si le contribuable est devenu citoyen de l'État requis avant le 9 novembre 1995 et est citoyen au moment où l'État requérant demande la perception de la créance, soit une période imposable qui a pris fin avant le 9 novembre 1995,

[...]

[...]

[Emphasis added.]

[Je souligne.]

[58] The plaintiffs therefore argue that to the extent that Canada's disclosure of account holder information to the US constitutes "assistance in collection", Canada is prohibited from disclosing such information as it relates to Canadian citizens. The plaintiffs submit that "lending assistance" should be construed as being broader than simply engaging in the mechanics of actually

collecting an amount owing; rather, the collection of information is a key component of the tax collection process. As a result, account holder information should not be disclosed in cases in which the taxpayer was a Canadian citizen at the time the revenue claim arose.

[59] Second, the plaintiffs further submit that it is not sufficient that the CRA be satisfied that the account holder information collected by the reporting institutions on US persons is authorized by the terms by the IGA. The plaintiffs submit that this information must also be shown to “be relevant” for carrying out the provisions of the Canada-US Tax Treaty or the domestic laws of Canada or the US. The “may be relevant” test mentioned in Article XXVII of the Canada-US Tax Treaty must be satisfied on a case by case basis; there may be no “fishing expeditions”. Thus, the automatic disclosure of taxpayer information in cases of *bona fide* residents of Canada who are US citizens is simply not authorized by Article XXVII as it has been interpreted in the past (or according to OECD interpretative instruments or extrinsic aids cited by counsel at the hearing). In its relevant portion, paragraph 1 of Article XXVII of the Canada-US Tax Treaty stipulates:

1. The competent authorities of the Contracting States shall exchange such information as may be relevant for carrying out the provisions of this Convention or of the domestic laws of the Contracting States concerning taxes to which this Convention applies insofar as the taxation thereunder is not contrary to this Convention.

[...]

1. Les autorités compétentes des États contractants échangent les renseignements pertinents à l'application des dispositions de la présente Convention ou à celles de la législation interne des États contractants relatives aux impôts auxquels s'applique la présente Convention dans la mesure où l'imposition qu'elle prévoit n'est pas contraire à la présente Convention.

[...]

[Emphasis added.]

[Je souligne.]

[60] Since paragraph 1 of Article XXVII limits the disclosure of information to circumstances in which the information “may be relevant” for carrying out the provisions of the Canada-US Tax Treaty, or of the domestic laws of Canada or the US, the plaintiffs claim that this provision would make the disclosure of taxpayer information mentioned in the IGA unlawful in relation to a vast majority of US persons resident in Canada, regardless of whether or not they are Canadian citizens. Since most US persons resident in Canada do not owe taxes to the US, the plaintiffs argue that their account holder information is of no relevance to the US in imposing its income tax, and therefore does not fall within the scope of information that may be disclosed pursuant to Article XXVII. In cases in which such information may be relevant, however, the plaintiffs argue that Canada has the ability to disclose such account holder information in a more selective manner. Such would be the case where there are Tax Treaty Gaps – that is, in cases where a Canadian citizen with US person status may be subject to US taxation on their Canadian-source income (Christians expert report, paragraph 10). In addition, the information that would be relevant to a US tax assessment of a collectible tax debt in Canada would generally be reported or disclosed to the CRA by the taxpayer or a third party charged with such reporting.

[61] Subject to the objection made by the defendants that expert evidence must be limited to the state of US domestic tax laws, Professor Christians goes on to state:

Accordingly, the type of information that may be relevant to the assessment of a US tax debt is already disclosed to the CRA in most cases by the taxpayer or by a third party with the exception of the sale of a personal residence. Canada and the United States are aware of the Tax Treaty Gaps. In cases involving such Gaps, the necessary tax reporting is required or if need be compelled by the

CRA. In virtually all cases in which US taxation would actually apply, information compiled by the CRA that identifies Canadian residents who have US Person status could be cross-referenced with the information received by the CRA that is relevant to the Tax Treaty Gaps. (paragraph 23)

[Emphasis added.]

In this way, the plaintiffs submit that Canada can satisfy the terms of the IGA while also acting within the bounds of Article XXVII of the Canada-US Tax Treaty.

[62] Third, the plaintiffs submit that the collection and disclosure of the taxpayer information contemplated by the IGA subjects US nationals resident in Canada to taxation and requirements connected therewith that are more burdensome than the taxation and requirements connected therewith to which Canadian citizens resident in Canada are subjected. The plaintiffs rely on Article XXV of the Canada-US Tax Treaty, notably paragraph 1, which reads as follows:

1. Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith that is more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, particularly with respect to taxation on worldwide income, are or may be subjected. This provision shall also apply to individuals who are not residents of one or both of the Contracting States.

[...]

[Emphasis added.]

1. Les nationaux d'un État contractant ne sont soumis dans l'autre État contractant à aucune imposition ou obligation y relative, qui est plus lourde que celles auxquelles sont ou pourront être assujettis les nationaux de cet autre État qui se trouvent dans la même situation, surtout à l'égard de l'impôt sur le revenu mondial. La présente disposition s'applique également aux personnes physiques qui ne sont pas des résidents d'un État contractant ou des deux États contractants.

[...]

[Je souligne.]

[63] According to Article XXV, Canada may not subject US nationals to “any taxation or requirement” therewith that is more burdensome than “the taxation and connected requirements” to which Canadian nationals are or may be subjected in the same circumstances. The plaintiffs note that the impugned provisions contemplate the provision by Canada of the account holder information of US persons to the US. Considering that such information would not be provided in relation to accounts held by Canadian nationals who are not considered US persons, the plaintiffs assert that the impugned provisions fall afoul of this Article. The plaintiffs submit that the differential impact of the impugned provisions on Canadian citizens who are US persons will include a loss of privacy under the provisions of the Canada-US Tax Treaty and the ITA with respect to the disclosed information (in this summary trial we are not dealing with privacy rights asserted by the plaintiffs on the basis of quasi-constitutional laws or the *Charter*). It will also include the increased financial burden of individuals having to file many tax related forms, or of having to provide financial institutions with additional documentation (for example, a “certificate of loss of citizenship”), as well as the legal and accounting costs associated with such documentation if individuals do not wish their accounts to be treated as US Reportable Accounts.

[64] The plaintiffs further submit that under section 241 of the ITA, Crown servants and other officials or representatives of government agencies are generally prohibited from knowingly providing or allowing to be provided any taxpayer information to any person. While subsection 241(4) creates exceptions to this rule, on the basis of which it would be lawful to provide or allow access to such information, the plaintiffs argue that the impugned provisions and the IGA are not a tax treaty or listed agreement within the definition of subsection 241(4), and therefore do not fall within these exceptions. Alternatively, even if the IGA did fall within the exception provided by section 241, the exchange of account holder information cannot occur pursuant to

Article XXVII of the Canada-US Tax Treaty because such taxpayer information does not meet the “may be relevant” standard. As a result, such an exchange would still violate section 241 of the ITA.

[65] All these arguments are unfounded in law or otherwise unconvincing in light of the evidence on record. I agree with the defendants that the plaintiffs misread the IGA and the Canada-US Tax Treaty in a way that frustrates the intention of the parties. It is manifest that the authority to exchange automatically on an annual basis the information obtained by Canada pursuant to the terms of the IGA indeed derives from Article XXVII of the Canada-US Tax Treaty, which does not expressly prohibit such disclosure. The provisions of the IGA are clear. The IGA has force of law in Canada. Sections 266 to 269 of the ITA are compulsory. While all information exchanged is protected by the confidentiality provisions of the Canada-Tax Convention and the ITA, the exceptions created under subsection 241(4) of the ITA are applicable to the impugned provisions and the IGA.

[66] The Canada-US Tax Treaty cannot be interpreted in a vacuum: the fact is that Canada and the US entered into an Intergovernmental Agreement in 2014, purportedly under the authority of the Canada-US Tax Treaty. “In interpreting a treaty, the paramount goal is to find the meaning of the words in question. This involves looking at the language used and the intentions of the parties” (*Crown Forest Industries*, above at page 814). In the present case, the words used by the parties to the IGA are explicit and the intention of the contracting governments is clear: they agree to obtain and exchange annually on an automatic basis all

relevant information respecting reportable accounts subject to the confidentiality and other provisions of the Canada-US Tax Treaty.

[67] This intention is apparent from Articles 2 and 3(7) of the IGA, which provide that:

[E]ach Party shall obtain the information specified in paragraph 2 of this Article with respect to all Reportable Accounts and shall annually exchange this information with the other Party on an automatic basis pursuant to the provisions of Article XXVII of the Convention.

[...]

All information exchanged shall be subject to the confidentiality and other provisions provided for in the Convention, including the provisions limited the use of the information exchanged.

[Emphasis added.]

[C]haque partie obtient les renseignements visés au paragraphe 2 du présent article pour tous les comptes déclarables et elle échange ces renseignements chaque année avec l'autre partie de manière automatique conformément aux dispositions de l'article XXVII de la Convention.

[...]

Tous les renseignements échangés sont assujettis aux obligations de confidentialité et autres garanties prévues par la Convention, y compris les dispositions qui en limitent l'utilisation.

[Je souligne.]

[68] The interpretation proposed by the defendants is also consistent with the goals and purposes of the Canada-US Tax Treaty and the intent expressed by the parties to the IGA. Compliance under the Canada-US Tax Treaty supposes that all US persons will file the required tax reports and declare their taxable income. Under US domestic tax laws, this includes the plaintiffs and other Canadian residents having dual citizenship. Overall, I am satisfied that the automatic collection and disclosure of the account holder information covered by the IGA meets

the standard of “may be relevant” under Article XXVII, having regard to the purposes of the Canada-US Tax Treaty, the language of Article XXVII, and the overall legal and factual context. The plaintiffs’ reading of the “may be relevant” standard is erroneous because it rests on fundamental misconceptions about the purpose of the Canada-US Tax Treaty, the purpose of FATCA, and the correct approach to treaty interpretation. Article XXVII does not provide Canada with an opportunity to object to US tax policy choices.

[69] At the risk of repeating myself, FATCA is about US tax compliance. In 2014, the US and Canadian governments, being both “supportive of applying the underlying policy goal of FATCA on a reciprocal basis to improve tax compliance”, signed the IGA. The IGA creates a framework whereby certain Canadian financial institutions obtain FATCA-compliant status, while others are exempted from FATCA disclosure requirements altogether (see Article 4 of the IGA). In addition, the IGA allows for the US to engage in reciprocal tax information exchange with Canada concerning financial accounts held by Canadian residents at US institutions (see Article 2, paragraph 2(b) of the IGA). According to the terms of the IGA, Canadian financial institutions are not permitted to opt out of these information-sharing requirements. If financial institutions do not or cannot agree to disclose US account holder information to the US, they may be subject to the thirty percent withholding tax described above. Indeed, the Canadian and US Governments are obliged to “implement as necessary requirements to prevent financial institutions from adopting practices intended to circumvent the reporting required under [the IGA]” (Article 5, section 4 of the IGA).

[70] The IGA establishes a special regime for information collection and reporting that the US government considers necessary to administer its income tax or tax liability system. The argument that relevance under Article XXVII of the Canada-US Tax Treaty is limited to situations in which a Canadian resident would owe tax in the US is wrong. It is impossible in practice to administer Article XXVII as the plaintiffs argue. It is also unreasonable to conclude that the governments of Canada and the US entered into an Intergovernmental Agreement which should be interpreted in a way that renders it practically impossible to perform. According to section 269 of the ITA, if a Canadian financial institution makes a reasonable determination that it is to be treated as a “deemed-compliant FFI” under Annex II of the IGA, Part XVIII applies to the institution, with such modifications as the circumstances require, to the extent that the IGA imposes due diligence and reporting obligations on the institution (section 269 of the ITA).

[71] I also accept that by analogy, the FATCA reporting requirements are similar in principle to certain Canadian reporting requirements under the ITA that also do not require information indicating income tax or tax liability. For example, section 233.3 of the ITA requires certain Canadian taxpayers to report holdings of a wide range of foreign property with a cost of more than \$100,000 – including funds deposited in foreign accounts – regardless of whether or not that property generates income that is taxable in Canada. These reporting requirements exist to assist the CRA in administering the Canadian tax system. It cannot reasonably be argued that similar kinds of information about US taxpayers is not relevant to carrying out the provisions of US tax laws in respect of Canadian residents who are US persons.

[72] I also fail to see the application of Article XXVI A of the Canada-US Tax Treaty at this point in time. It is not challenged by the defendants that Article XXVI A clearly prevents Canada from providing the US with assistance in the collection of revenue claims to the extent that the taxpayer in question was a citizen of Canada at the time the revenue claim arose. I agree with the defendant that Article XXVI A applies only to cases in which tax liability has been determined and is enforceable, and does not apply to the assessment of tax payable, the verification of taxpayer compliance, or related exchanges of information. Accordingly, I find that the automatic exchange of information allowed by the IGA does not amount at the present time to providing assistance in collection, and is thus not captured under this Article. The plaintiffs have conflated the assessment of taxes, verification of compliance, and collection of penalties possibly due by US persons for non-reporting. The arguments made in this respect are not relevant and are premature in any event.

[73] I also find that the non-discrimination provision of Article XXV is not applicable in the present case. The IGA and Part XVIII of the ITA do not impose more burdensome requirements connected with taxation on the plaintiffs; the burden of disclosing banking information is imposed by Part XVIII on financial institutions, who are resident in Canada, and on Canadian branches of non-resident financial institutions; and to the extent that the IGA and Part XVIII of the ITA impose burdensome requirements connected to taxation of US nationals resident in Canada, such burden is equally imposed on Canadian nationals in similar circumstances. Accordingly, this argument must also be dismissed.

[74] Finally, it is not challenged that according to Article 3(7) of the IGA, all information exchanged under the IGA is subject to safeguards provided for in the Canada-US Tax Treaty “including the provisions limiting the use of the information exchanged”. That being said, the CRA does not possess the necessary facts, nor the required expertise in US tax law, to determine the potential US tax liability of US persons residing in Canada – even less so this Court. Before the double taxation provisions of a tax treaty apply (see Article XXIV of the Canada-US Treaty, as well as tax treaties based on the OECD model), a contracting state must first be able to determine an initial tax liability against which relief from double taxation will ultimately be available.

[75] Perhaps, as suggested by the plaintiffs, there is little reason to view “accidental Americans” such as the plaintiffs as anything other than a largely law-abiding group who stand at risk of being punished by US authorities not for evading taxes, but for having failed to carefully study their form-filing obligations under what to them is the law of a foreign jurisdiction. The plaintiffs assert that this would be highly unjust on the part of the US authorities. The defendants’ learned counsel generally addressed this question in their oral arguments, stating:

Those are all policy issues for the U.S. government and the U.S. Congress. They’ve made their decision as to what their laws will be. We have committed to live with that within the treaty. The treaty does not give us an opportunity to say to them, we disagree with your policies, and we will not assist you to implement them. We have agreed to assist them to the extent that information is relevant to their laws, and that’s their realm. (Transcript, August 5, 2015 at page 133).

[76] True, a great number of Canadian taxpayers holding US reportable accounts are likely to be affected by a reporting system that in many quarters is considered unjust, costly and ineffective, considering that at the end of the day they are not likely to owe taxes to the US. In the absence of legislative provisions requiring all Canadian financial institutions (provincially and federally regulated) to automatically notify their account holders about reporting to the CRA under the IGA and Part XVIII of the ITA, these taxpayers may also be taken by surprise by any consequences that flow from such disclosure. The plaintiffs may find this deplorable, but apart from a constitutional invalidation of the impugned provisions or a change of heart by Parliament or Congress, or the governments of Canada or the US, there is nothing that this Court can judicially do today to change the situation. The impugned provisions have not been held to be *ultra vires* or inoperative. Judicial courage requires that judges uphold the Rule of Law.

Conclusion

[77] For all these reasons, the declaratory and injunctive relief requested by the plaintiffs in their motion for summary judgment shall be denied by the Court, without prejudice to the plaintiffs' right to pursue their claim that the impugned provisions are *ultra vires* or inoperative because they are unconstitutional or otherwise unjustifiably infringe *Charter* rights. There shall be no costs. This is a case where, in view of the nature of the issues and the public interest involved in clarifying the scope of novel provisions affecting hundreds of thousands of Canadian citizens, no costs should be ordered against the losing parties.

JUDGMENT

THIS COURT ORDERS AND ADJUDGES THAT:

1. The declaratory and injunctive relief requested by the plaintiffs in their motion for summary judgment is denied, without prejudice to the plaintiffs' right to pursue their claim that the impugned provisions are *ultra vires* or inoperative because they are unconstitutional or otherwise unjustifiably infringe *Charter* rights;
2. The present motion is dismissed without costs.

“Luc Martineau”

Judge

FEDERAL COURT

SOLICITORS OF RECORD

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