

## Canadian Bijuralism and the Concept of an Acquisition of Property in the Federal *Income Tax Act*

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Résumé de l'article

Dans la *Loi de l'impôt sur le revenu (LIR)*, l'acquisition de bien permet de déterminer l'éligibilité à un nombre d'avantages fiscaux, notamment au droit à la déduction pour amortissement, au crédit d'impôt à l'investissement et à la déductibilité des frais d'intérêts encourus relativement au bien éligible. Malgré son importance, le concept d'acquisition de bien n'est pas défini dans la *LIR* et a reçu des interprétations divergentes en *common law* et en droit civil.

L'auteur retrace les sources de droit éclairant le sens d'acquisition de bien en *common law* et en droit civil. Il conclut que la réalisation de certaines transactions dans une province de *common law* ou au Québec peut entraîner des conséquences fiscales différentes. L'auteur démontre que la référence principale en matière de détermination d'acquisition de bien par un contribuable (le test en deux parties de l'affaire *M.N.R. v. Wardean Drilling Ltd.*) est basée sur des concepts de *common law* et est incompatible avec les objectifs du bijuridisme canadien tel qu'exprimé dans la *Loi d'harmonisation n° 1 du droit fédéral avec le droit civil* et dans l'article 8.1 de la *Loi d'interprétation fédérale*. Afin de répondre à cette contradiction, l'auteur propose un nombre d'amendements législatifs pour assurer une application uniforme et prévisible de la *LIR* partout au Canada.

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# Canadian Bijuralism and the Concept of an Acquisition of Property in the Federal Income Tax Act

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David G. Duff\*

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The acquisition of property plays an important role in the federal *Income Tax Act (ITA)*, determining eligibility for a number of tax benefits, including entitlement to capital cost allowance, investment tax credits, and the deductibility of interest expenses incurred in respect of eligible property. In spite of its importance, the concept of an acquisition of property is not defined in the *ITA*, and it has been subject to divergent interpretations in the common law and the civil law.

The author traces the sources of law informing the meaning of an acquisition of property in the common law and the civil law, and concludes that certain transactions may be subject to different tax consequences depending on whether they occurred in a common law province or in Quebec. The author demonstrates that the primary reference for determining whether a taxpayer acquired property—the twofold test in *M.N.R. v. Wardean Drilling Ltd.*—is premised on common law concepts and is incompatible with the goals of Canadian bijuralism expressed in the *Federal Law—Civil Law Harmonization Act, No. 1* and section 8.1 of the federal *Interpretation Act*. In response to this contradiction, the author proposes a number of statutory amendments to ensure the uniform and predictable application of the *ITA* across Canada.

Dans la *Loi de l'impôt sur le revenu (LIR)*, l'acquisition de bien permet de déterminer l'éligibilité à un nombre d'avantages fiscaux, notamment au droit à la déduction pour amortissement, au crédit d'impôt à l'investissement et à la déductibilité des frais d'intérêts encourus relativement au bien éligible. Malgré son importance, le concept d'acquisition de bien n'est pas défini dans la *LIR* et a reçu des interprétations divergentes en *common law* et en droit civil.

L'auteur retrace les sources de droit éclairant le sens d'acquisition de bien en *common law* et en droit civil. Il conclut que la réalisation de certaines transactions dans une province de *common law* ou au Québec peut entraîner des conséquences fiscales différentes. L'auteur démontre que la référence principale en matière de détermination d'acquisition de bien par un contribuable (le test en deux parties de l'affaire *M.N.R. v. Wardean Drilling Ltd.*) est basée sur des concepts de *common law* et est incompatible avec les objectifs du bijuridisme canadien tel qu'exprimé dans la *Loi d'harmonisation n° 1 du droit fédéral avec le droit civil* et dans l'article 8.1 de la *Loi d'interprétation fédérale*. Afin de répondre à cette contradiction, l'auteur propose un nombre d'amendements législatifs pour assurer une application uniforme et prévisible de la *LIR* partout au Canada.

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## Introduction

The concept of an acquisition of property plays an important role in the federal *Income Tax Act*,<sup>1</sup> determining eligibility for a number of benefits. The ability to deduct capital cost allowance, for example, depends on the prior acquisition of depreciable property,<sup>2</sup> the definition of which requires that the property was “acquired by the taxpayer.”<sup>3</sup> Similarly, investment tax credits are available only where the taxpayer has “acquired” the property in that fiscal year,<sup>4</sup> while the deduction for interest expenses under subparagraph 20(1)(c)(ii) of the *ITA* applies to interest on an amount payable for property acquired by the taxpayer.<sup>5</sup> Despite its importance, the concept of an acquisition of property is not defined in the *ITA*, leaving its meaning to judicial interpretation.

For almost thirty years now, the meaning of this expression for Canadian income tax purposes has generally been governed by the judicial test set out in *M.N.R. v. Wardean Drilling Ltd.*, in which Justice Cattanach stated that “the proper test as to when property is acquired must relate to the title to the property in question or to the normal incidents of title, either actual or constructive, such as possession, use and risk.”<sup>6</sup> Regularly cited in subsequent tax cases involving the acquisition of property,<sup>7</sup> this twofold test stipulates that property is acquired by a taxpayer within the meaning of the *ITA* not only when the taxpayer obtains legal title to the property, but also when

<sup>1</sup> R.S.C. 1985 (5th Supp.), c. 1 [*ITA*].

<sup>2</sup> *Ibid.*, s. 13(21), s.v. “undepreciated capital cost”.

<sup>3</sup> *Ibid.*, s. 13(21), s.v. “depreciable property”.

<sup>4</sup> *Ibid.*, ss. 127(5)(a), 127(6)(a). See also *ibid.*, s. 127(9), s.v. “investment tax credit”, “certified property”, “qualified property” (all of which require the taxpayer to have acquired the property at specific times).

<sup>5</sup> *Ibid.* (permitting a deduction for interest on “an amount payable for property acquired for the purpose of gaining or producing income from the property or for the purpose of gaining or producing income from a business”).

<sup>6</sup> [1969] 2 Ex. C.R. 166 at 172, [1969] C.T.C. 265 [*Wardean Drilling*].

<sup>7</sup> See e.g. *Canada v. Henuset Brothers Ltd. (No. 2)*, [1977] C.T.C. 228, 31 D.T.C. 5169 (F.C.T.D.) [*Henuset Brothers* cited to C.T.C.]; *Schultz v. M.N.R.*, [1979] C.T.C. 2328, 33 D.T.C. 279 (T.R.B.) [*Schultz* cited to C.T.C.]; *Kirsch Construction Ltd. v. M.N.R.* (1988), 23 F.T.R. 67, 42 D.T.C. 6503 [*Kirsch* cited to F.T.R.]; *Browning Harvey Ltd. v. M.N.R.* (1990), 31 F.T.R. 229, 44 D.T.C. 6105 [*Browning Harvey* cited to F.T.R.]; *Borstad Welding Supplies (1972) Ltd. v. M.N.R.* (1993), 67 F.T.R. 118, 47 D.T.C. 5457 [*Borstad* cited to F.T.R.]; *Gartry (W.C.) v. Canada*, [1994] 2 C.T.C. 2021, 48 D.T.C. 1947 (T.C.C.) [*Gartry* cited to C.T.C.]; *Canada v. Construction Bérou* (1999), [2000] 2 C.T.C. 174, 53 D.T.C. 5868 (F.C.A.) [*Bérou* cited to C.T.C.]; *Mimetix Pharmaceuticals v. Canada*, [2002] 1 C.T.C. 2188, 55 D.T.C. 1026 (T.C.C.) [*Mimetix* cited to C.T.C.], aff’d 2003 FCA 106, [2003] 3 C.T.C. 72, 57 D.T.C. 5194; *Terexcavation Antoine Grant v. Canada* (2002), 59 D.T.C. 709 (T.C.C.) [*Terexcavation*].

the taxpayer obtains constructive or beneficial ownership of the property (i.e., through the “normal incidents of title” such as “possession, use and risk”).<sup>8</sup>

Although the concept of beneficial ownership is well established in common law systems, where the law of equity and trusts has long recognized a distinction between legal and beneficial ownership,<sup>9</sup> it does not exist in civilian systems, which regard ownership as absolute and indivisible.<sup>10</sup> For this reason, a number of tax cases in the Province of Quebec have established that lessee-purchasers under lease-option agreements do not acquire property within the meaning of the *ITA* if legal ownership is retained by the lessor-vendor, notwithstanding the fact that the lessee-purchaser has obtained possession and use of the property and has assumed the risks normally associated with ownership.<sup>11</sup> In *Bérou*, however, a majority of the Federal Court of Appeal rejected this line of reasoning, concluding that the test in *Wardean Drilling* governs the acquisition of property in Quebec as well as the rest of Canada.<sup>12</sup> In so doing, the decision effectively distinguished or “dissociated” the tax meaning of an acquisition of property from the civil law of Quebec.<sup>13</sup>

Because the judgment in *Bérou* was released on 15 November 1999, the court did not consider section 8.1 of the federal *Interpretation Act*,<sup>14</sup> which came into force on 1 June 2001. According to this provision:

Both the common law and the civil law are equally authoritative and recognized sources of the law of property and civil rights in Canada and, unless otherwise provided by law, if in interpreting an enactment it is necessary to refer to a province’s rules, principles or concepts forming part of the law of

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<sup>8</sup> See e.g. *Kinguk Trawl v. Canada*, [2002] 2 C.T.C. 2229 at para. 123, 56 D.T.C. 1399 (T.C.C.) (relying on *Wardean Drilling* for the proposition that “[t]he concept of beneficial ownership, which might differ from strict legal ownership, is well recognized in the case law”).

<sup>9</sup> Catherine Brown, “Symposium: Beneficial Ownership and the Income Tax Act” (2003) 51 Can. Tax J. 401 at 405-423.

<sup>10</sup> Further discussion of civilian systems will be found in Part II.B, below.

<sup>11</sup> *Fortin & Moreau v. M.N.R.* (1989), [1990] 1 C.T.C. 2583, 44 D.T.C. 1436 (T.C.C.) [*Fortin & Moreau* cited to C.T.C.]; *Canada v. Construction Bérou* (1996), 116 F.T.R. 267, 52 D.T.C. 6401 [*Bérou (F.C.T.D.)* cited to D.T.C.], rev’d *Bérou*, *supra* note 7; *Dumais (D.) et fils c. M.N.R.* (1990), [1991] 1 C.T.C. 2650, 46 D.T.C. 1107 (T.C.C.) [*Dumais* cited to C.T.C.]; *Location Gaétan Lévesque v. M.N.R.*, [1991] 2 C.T.C. 2795, 91 D.T.C. 1374 (T.C.C.) [*Gaétan Lévesque* cited to C.T.C.]; and *Laurent Goulet & Fils v. M.N.R.* (1991), [1992] 1 C.T.C. 2419, 46 D.T.C. 1605 (T.C.C.).

<sup>12</sup> *Supra* note 7.

<sup>13</sup> David G. Duff, “The Federal Income Tax Act and Private Law in Canada: Complementarity, Dissociation, and Canadian Bijuralism” (2003) 51 Can. Tax J. 1 at 40-41. On the concept of dissociation between federal law and provincial private law, see Louise Maguire Wellington, “Bijuralism in Canada: Harmonization Methodology and Terminology” in *The Harmonization of Federal Legislation with the Civil Law of the Province of Quebec and Canadian Bijuralism* (Ottawa: Department of Justice Canada, 2001) [*Harmonization*] fasc. 4, 1 at 5.

<sup>14</sup> R.S.C. 1985, c. I-21.

property and civil rights, reference must be made to the rules, principles or concepts in force in the province at the time the enactment is being applied.<sup>15</sup>

Thus, the test in *Wardean Drilling* may no longer apply within the Province of Quebec if the two conditions in section 8.1—the necessity of referring to provincial sources of law and the absence of a prohibition on doing so—are met in interpreting the meaning of an acquisition of property in the *ITA*. If so, it would be advantageous to amend the *ITA* to ensure that the meaning of an acquisition of property for tax purposes has uniform application throughout Canada.

This paper examines the concept of an acquisition of property for the purposes of the *ITA*, considering tax cases in which the concept has been addressed; private law rules, principles, and concepts that may be relevant to its interpretation; the impact of section 8.1 of the *Interpretation Act* on this interpretation; and the merits of a statutory amendment to ensure that the meaning of this expression is given uniform application throughout Canada. The first part of the paper reviews tax cases in which the concept of an acquisition of property has been interpreted and applied, beginning with the judgment in *Wardean Drilling* and then considering tax cases in common law provinces and the Province of Quebec. The second part of the paper examines the common law and civil law rules, principles, and concepts to which courts have implicitly or explicitly referred in order to interpret the meaning of an acquisition of property for tax purposes, with particular attention to conditional sales agreements and leasing transactions, the most common types of tax cases concerning the acquisition of property. The third part of the paper considers the impact of the *Interpretation Act* on the meaning of an acquisition of property in the *ITA*, arguing that the two conditions in section 8.1 for referring to provincial sources of law are met. Since this analysis suggests that the meaning of an acquisition of property may be subject to different interpretations in common law provinces and the Province of Quebec, the fourth part of the paper proposes that the *ITA* should be amended to include a statutory definition of this term to ensure that the concept is given a uniform interpretation throughout Canada. The fifth part of the paper summarizes the argument and offers concluding observations.

## I. The Acquisition of Property in Canadian Income Tax Law

In order to appreciate the possible effect of section 8.1 of the *Interpretation Act* on the meaning of an acquisition of property for tax purposes, it is essential to begin by examining the way in which Canadian courts have interpreted this concept thus far. The following sections review the interpretation of this concept in *Wardean Drilling* and subsequent tax cases in common law provinces and in Quebec.

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<sup>15</sup> *Ibid.*, s. 8.1.

### A. *Wardean Drilling*

The issue in *Wardean Drilling* concerned the date at which property was acquired by the taxpayer for the purpose of deducting capital cost allowance. The taxpayer had carried on a business of drilling oil wells in Alberta and Saskatchewan and had purchased a drilling rig and a substructure for the rig, in respect of which it deducted capital cost allowance in computing its business income for its 1963 taxation year. Although the taxpayer entered into an agreement to purchase the rig on 26 December 1963, the property required extensive modification for the taxpayer's purposes and delivery did not occur until 18 February 1964. According to the agreement, payment was to be made in thirty-six equal monthly instalments commencing on 1 June 1964, title was to pass upon shipment, and payment was to be secured by a chattel mortgage on the rig. While the taxpayer entered into the agreement to purchase the substructure on 23 December 1963, this item did not exist at the time and was neither constructed, delivered, nor paid for until "well into 1964."<sup>16</sup>

The minister disallowed the deductions on the grounds that the property in each case was not paid for or delivered until the following taxation year. The Tax Appeal Board allowed the taxpayer's appeal on the basis that the taxpayer had incurred expenditures in 1963 by entering into binding agreements to purchase the property.<sup>17</sup> The Exchequer Court reversed the decision and upheld the assessment on the grounds that the taxpayer had not acquired the rig and the substructure during its 1963 taxation year.

At the Exchequer Court, the taxpayer relied on the Tax Appeal Board decision, arguing that goods are acquired by a purchaser for tax purposes "when the vendor and the purchaser have entered into a binding and enforceable contract of sale and purchase."<sup>18</sup> Rejecting this interpretation, Justice Cattanach held that "the proper test" to determine when property is acquired "must relate to the title to the property in question or to the normal incidents of title, either actual or constructive, such as possession, use and risk."<sup>19</sup> Thus, he explained, a purchaser has acquired assets for the purpose of computing capital cost allowance either (1) "when title has passed, assuming that the assets exist at that time," or (2) "when the purchaser has all the incidents of title, such as possession, use and risk, although legal title may remain in the vendor as security for the purchase price as is the commercial practice under conditional sales agreements."<sup>20</sup> Applying the first branch of this twofold test, Justice Cattanach concluded that the taxpayer acquired neither the rig nor the substructure in 1963 on the grounds that the contract itself stipulated that title to the rig would not

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<sup>16</sup> *Wardean Drilling*, *supra* note 6 at 169-71.

<sup>17</sup> *Wardean Drilling Ltd. v. M.N.R.*, [1967] Tax A.B.C. 171 [*Wardean Drilling (T.A.B.)*].

<sup>18</sup> *Wardean Drilling*, *supra* note 6 at 172.

<sup>19</sup> *Ibid.*

<sup>20</sup> *Ibid.* at 173.

pass until shipment, which was not until February 1964,<sup>21</sup> while title to the substructure could not pass until it was actually constructed in 1964.<sup>22</sup>

Although Justice Cattanach did not cite any legal authority for the test that he adopted in *Wardean Drilling*, the distinction between “actual” or “legal” title and “constructive” title based on “all the incidents of title” is premised on the common law distinction between legal and beneficial ownership. As the Federal Court of Appeal observed in *Hewlett Packard (Canada) Ltd. v. Canada*,<sup>23</sup> the language and reasoning used by Justice Cattanach corresponds to the common law conception of property employed by the Supreme Court of Alberta in *Hendrickson v. Mid-City Motors Ltd.*, in which the court held that a conditional sale agreement resulted in a sale under the Alberta *Sale of Goods Act* on the basis that the agreement effectively transferred the “property” in the goods to the purchaser in the form of “beneficial ownership”, notwithstanding the fact that the vendor retained legal title until the purchase price was paid in full.<sup>24</sup> Therefore, it is clear that the test in *Wardean Drilling* is firmly rooted in principles and concepts specific to the common law, even though it is often viewed as an autonomous interpretation based on the language and purposes of the *ITA* alone.<sup>25</sup> As explained in the third part of this paper, it is this connection to private law principles and concepts that engages the interpretive rule in section 8.1 of the *Interpretation Act*.

## B. Subsequent Tax Cases in Common Law Provinces

Although the decision in *Wardean Drilling* ultimately turned on the first branch of Justice Cattanach’s test, subsequent cases in common law provinces have regularly looked to the second branch of the test to determine whether property has been acquired for the purposes of the *ITA*.<sup>26</sup> In *Henuset Brothers*, for example, the Federal Court concluded that the taxpayer, which entered into a conditional sales agreement to purchase several tractors on 30 December 1971, had acquired the tractors on that date notwithstanding the fact that legal title to the tractors was retained by the vendor

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<sup>21</sup> *Ibid.* at 174, citing the Alberta *Sale of Goods Act*, R.S.A. 1955, c. 295, ss. 20-21, as am. by R.S.A. 2000, c. S-2, s. 19(1) (stipulating that property in specific or ascertained goods passes at the moment that the parties intend).

<sup>22</sup> *Wardean Drilling*, *supra* note 6 at 174-75, citing the Alberta *Sale of Goods Act*, *ibid.*, s. 21(1) (now s. 20(3)): “Where there is a contract for the sale of specific goods and the seller is bound to do something to the goods for the purpose of putting them into a deliverable state, the property does not pass until the thing is done and the buyer has notice thereof.”

<sup>23</sup> 2004 FCA 240, 324 N.R. 201, 58 D.T.C. 6498 [*Hewlett Packard*].

<sup>24</sup> [1951] 3 D.L.R. 276 at 284, 1 W.W.R. (N.S.) 609 [*Hendrickson* cited to D.L.R.].

<sup>25</sup> See e.g. *Terexcavation*, *supra* note 7 at para. 35. This case is discussed at *infra* notes 86-88 and accompanying text.

<sup>26</sup> For another case applying the first branch of the twofold test in *Wardean Drilling*, see *Schultz*, *supra* note 7 (the taxpayer could not deduct capital cost allowance in respect of a building before it was completed since it did not have legal possession of the property).



and the tractors themselves remained at the vendor's premises.<sup>27</sup> Noting that the taxpayer had the right to use the tractors, could have taken delivery once the sale was completed, and that the contracts obliged the taxpayer to insure the tractors against risks specified by the vendor, Justice Bastin concluded that "all the incidents of ownership other than the legal title reserved in the vendor by the conditional sales agreements such as possession, risk and the right to use the tractors were acquired by the buyer on December 30, 1971."<sup>28</sup> In support of this conclusion, the court cited the twofold test in *Wardean Drilling*.

Likewise, in *Gartry*, the Tax Court of Canada relied on the second branch of the test in *Wardean Drilling* to conclude that the taxpayer, who had purchased a boat that sank in heavy seas before delivery and before title had passed, had acquired "sufficient of the incidents of ownership" to allow him to treat the boat as depreciable property in respect of which he could deduct a terminal loss under subsection 20(16) of the *ITA*.<sup>29</sup> According to Justice Bowman (as he then was), if a taxpayer "has exercised sufficient dominion" over property he has promised to purchase such that he "orders its modification for his specific purposes, and supervises and pays for those modifications," then he acquires "a sufficient interest in the property and *indicia* of title thereto," and the property "becomes depreciable property in his hands" even if transfer of actual title is deferred until full payment is received.<sup>30</sup> Therefore, even though legal title and possession remained with the vendor, the court concluded that the taxpayer had obtained constructive ownership of the boat under the second branch of the test in *Wardean Drilling*.

Furthermore, a number of other decisions in common law provinces have applied the second branch of the twofold test from *Wardean Drilling* to conclude that property was *not* acquired within the meaning of the *ITA*. In *Kirsch*, for example, the Federal Court considered both branches of the test to decide that the taxpayer, which entered into an agreement to purchase a road paver on 30 March 1977,<sup>31</sup> had not acquired the property before the end of its taxation year, ending 31 March 1977. Regarding the first branch of the test, the court held that the taxpayer did not have legal title to the road paver before 31 March 1977 because, among other things, the contract provided that title would not pass until full payment was made, which did not occur until 14 June 1977.<sup>32</sup> With respect to the second branch, the court concluded that the taxpayer did not have all the incidents of ownership before 31 March 1977 because it did not obtain possession or use of the property and did not assume any of

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<sup>27</sup> *Supra* note 7.

<sup>28</sup> *Ibid.* at 229.

<sup>29</sup> *Supra* note 7 at 2029.

<sup>30</sup> *Ibid.* at 2030 [emphasis added].

<sup>31</sup> *Supra* note 7 at para. 11.

<sup>32</sup> *Ibid.* at para. 8.

the risks associated with ownership until after the road paver was delivered on 25 May 1977.<sup>33</sup>

Similarly, in *Browning Harvey*, where a taxpayer sold coolers to shopkeepers for the exclusive display of its soft drinks under conditional sales agreements, the Federal Court held that the shopkeepers had not acquired the coolers when they obtained possession because they “did not have *all* the incidents of title.”<sup>34</sup> Despite obtaining possession, the court noted that the shopkeepers’ possession was limited by the taxpayer’s right to repossess the coolers if they failed to comply with the terms of the agreement and that their use of the coolers was limited to storage and display for sale of soft drinks manufactured by the taxpayer.<sup>35</sup> As well, while the shopkeepers were required to insure the coolers against loss, any insurance proceeds were payable to the taxpayer, who was obliged to pay for repairs to the coolers after the manufacturer’s warranty expired. Finally, the court observed that the shopkeepers “were not entitled to destroy the coolers, to dispose of them, or to use them as security for loans.”<sup>36</sup> Justice Martin concluded:

In my view it is clear from the terms of the agreement that the defendant reserved to itself ownership in and title to the coolers for the full seven year term of the agreement and by placing the limitations on the use of them which the defendant did in the agreement it refused to give to the shopkeepers sufficient of the essential incidents of ownership as would cause me to find that the parties to the agreement intended by its terms that property in the coolers would pass from the defendant to the shopkeepers at the time of the execution of the agreement.<sup>37</sup>

Because the shopkeepers had not acquired the coolers, the court concluded that the taxpayer could not deduct a terminal loss on their alleged disposition.

Although *Henuset Brothers*, *Gartry*, *Kirsch*, and *Browning Harvey* all involved conditional sales agreements, tax cases in common law provinces have also applied the second branch of the test in *Wardean Drilling* to determine whether a lessee has acquired property for tax purposes under the terms of a lease. In *Borstad*, for example, a taxpayer sold refillable gas cylinders over a five-year period, selling one-fifth of the cylinders each year and leasing the remainder to the purchaser until they were sold.<sup>38</sup> The Federal Court applied the second branch of the *Wardean Drilling* test to conclude that the purchaser did not acquire the leased cylinders until they were actually sold. Noting that the parties expressly contracted that the taxpayer was to retain ownership of the property during the term of the lease, that the purchaser was obliged to indemnify the taxpayer if the cylinders were not maintained, that the

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<sup>33</sup> *Ibid.* at para. 10.

<sup>34</sup> *Supra* note 7 at para. 23 [emphasis in original].

<sup>35</sup> *Ibid.* at para. 24.

<sup>36</sup> *Ibid.* at para. 28.

<sup>37</sup> *Ibid.* at para. 28.

<sup>38</sup> *Supra* note 7.

purchaser was required to retain possession and control of the cylinders, and that the taxpayer could terminate the agreement if the purchaser defaulted on any term of the contract, Justice Reed concluded that the provisions of the agreement were not consistent with the view that the purchaser had “acquired all the incidents of title to the cylinders except legal title.”<sup>39</sup> On this basis, she rejected the minister’s argument that the taxpayer had disposed of the cylinders when the parties entered into a master agreement governing their lease and sale.

Likewise, in *Mimetix*, the Tax Court of Canada employed the second branch of the *Wardean Drilling* test to conclude that the taxpayer, which purchased a mixing machine after leasing it for eighteen months, did not acquire the property for tax purposes until it was actually purchased.<sup>40</sup> Observing that the lease agreement did not include an option to purchase the mixing machine for a price less than its expected fair market value at the purchase date, that the lessor continued to bear risks associated with ownership, and that the contract required the lessee to pay the lessor cost plus 10 per cent for the repair or replacement of damaged or missing components, Justice Lamarre concluded that the taxpayer was ineligible for an investment tax credit in respect of the mixer, since the property had already been used before the taxpayer acquired it in October 1996.<sup>41</sup>

While the judgments in *Borstad* and *Mimetix* held that the lessees in question *did not* acquire property under the terms of the respective lease-purchase agreements, other cases in common law provinces have held that lessees *did* acquire property pursuant to financing or capital leases. In *Kamsel Leasing v. M.N.R.*, for example, the Tax Court of Canada accepted the taxpayer’s argument that the lease agreements that it had entered into in the course of its lease financing business “effectively transferred substantially all of the benefits and risks of ownership” to the lessees.<sup>42</sup> Of particular relevance to its conclusion that the transactions were properly characterized as sales rather than leases, the court noted that (1) the lessees had “the right at the expiration of the lease to acquire the property at a price which at the inception of the lease could be said to be substantially less than the probable fair market value of the property at the time of permitted acquisition,” and (2) “the option permitted a lessee to acquire the property at a price which at the inception of the lease was such that no reasonable person would fail to exercise” and “a substantial percentage of the lessees exercised the option.”<sup>43</sup> Similarly, in *M.N.R. v. Moore*, the Federal Court concluded that the taxpayer and other investors had acquired capital property under a sixty-year lease with an option to purchase, for which they had prepaid rent for the entire term. The

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<sup>39</sup> *Ibid.* at para. 26.

<sup>40</sup> *Supra* note 7.

<sup>41</sup> *Ibid.* at 2212.

<sup>42</sup> [1993] 1 C.T.C. 2279 at 2282, 47 D.T.C. 250 (T.C.C.) [*Kamsel Leasing*].

<sup>43</sup> *Ibid.* at 2283. Sarchuk J. added that “[t]hese two findings ... mirror the circumstances under which, according to IT-233R, Revenue Canada would consider a transaction to be a sale rather than a lease” (*ibid.*). This Interpretation Bulletin is discussed at *infra* notes 80 and 109.

court noted that “they acquired substantially all the benefits and risks incidental to ownership of property” and there was “reasonable assurance” that they would “exercise their option to purchase the land in view of the fact that they were to construct a 33-unit apartment building on the site.”<sup>44</sup> Although neither of these judgments cited the twofold test for an acquisition of property in *Wardean Drilling*, the language and reasoning in each case is similar to the second branch of this test.

In marked contrast to all of these judgments, the Federal Court of Appeal in *Kowdrysh v. Canada* concluded that in the context of a temporary investment tax credit, the taxpayer in question had acquired farming equipment “when the equipment in an ascertained form was purchased by means of a binding and enforceable contract.”<sup>45</sup> Rejecting the minister’s argument that the taxpayer had not acquired the equipment until he obtained legal title or beneficial ownership of the property, the court held that the meaning of an acquisition of property must be understood in the context of the specific provision which employs this concept. According to Justice Létourneau (with Justices Desjardins and Décary concurring):

In my view, in the context of this temporary investment tax credit, especially in the farming industry where substantial investments are made with respect to costly, large, sophisticated and specialized equipment which requires a considerable amount of time for production, verification, approbation, transportation and delivery, the term “acquired” and the time of “acquisition” take a different meaning and connotation.<sup>46</sup>

For this purpose, therefore, the court gave the concept of an acquisition of property a similar meaning to the interpretation adopted by the Tax Appeal Board in *Wardean Drilling (T.A.B.)*.<sup>47</sup> Since this interpretation was explicitly rejected on appeal to the Exchequer Court,<sup>48</sup> it is surprising that it should reappear over thirty years later, even if only in the context of a special investment tax credit.

### C. Subsequent Tax Cases in Quebec

While judicial decisions involving transactions in common law provinces have generally applied the second branch of the twofold test in *Wardean Drilling* to determine whether a taxpayer has acquired property for tax purposes, cases involving transactions in Quebec have generally ignored or rejected the test for this purpose; that is, until the Federal Court of Appeal decision in *Bérou*.<sup>49</sup> In *Canada v. Lagueux & Frères*, for example, a taxpayer leased logging equipment from loan and rental companies that had purchased the equipment directly from manufacturers for the sole

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<sup>44</sup> (1986), 3 F.T.R. 173 at para. 52, 86 D.T.C. 6325.

<sup>45</sup> 2001 FCA 34, 267 N.R. 180 at para. 13, 55 D.T.C. 5221 [*Kowdrysh*].

<sup>46</sup> *Ibid.*

<sup>47</sup> *Supra* note 17. See Part I.A, above.

<sup>48</sup> *Wardean Drilling*, *supra* note 6.

<sup>49</sup> *Supra* note 7.

purpose of leasing the property to the taxpayer, under terms that allowed the taxpayer to purchase the equipment at a price much lower than its market value when the option was exercised. The Federal Court relied on the civil law of Quebec—not the twofold test in *Wardean Drilling*—to determine whether the taxpayer had acquired the property within the meaning of the *ITA*.<sup>50</sup> Explaining that “the nature of the rights and obligations created by the contracts [at issue] must be arrived at by reference to the provisions of the *Civil Code*,”<sup>51</sup> Justice Décary cited the *Civil Code of Lower Canada*, the views of French commentators, and jurisprudence on Quebec law to conclude that the contracts were properly characterized as “conditional sales, on a suspensive condition, and not leases.”<sup>52</sup> On this basis, he held that the taxpayer had acquired the logging equipment for tax purposes and could therefore deduct only capital cost allowance, not rental payments.

Similarly, in *Chibougamau Lumber ltée v. M.N.R.*,<sup>53</sup> a taxpayer entered into several agreements to lease equipment with an option to purchase the property for one dollar plus any unpaid amounts remaining under the terms of each lease. The judgment turned not on the judicial test in *Wardean Drilling* (which the Tax Review Board did not mention), but on the board’s conclusion as a matter of private law that the contracts at issue “were not, by any stretch of the imagination, leases in the true legal sense of the term,” but rather “represented no more than a purchase on a time payment plan.”<sup>54</sup> On this basis, as in *Lagueux & Frères*, the board disallowed the difference between the deduction of rental payments claimed by the taxpayer and capital cost allowance to which it was properly entitled.

Notwithstanding these decisions, the Federal Court *did* rely on the *Wardean Drilling* test in *Olympia and York Developments Ltd. v. Canada*, a case in which a

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<sup>50</sup> [1974] 2 F.C. 97, 74 D.T.C. 6569 (F.C.T.D.) [*Lagueux & Frères* cited to F.C.]:

[F]iscal law is an accessory system, which applies only to the effects produced by contracts. Once the nature of the contracts is determined by the civil law, the *Income Tax Act* comes into effect, but only then, to place fiscal consequences on those contracts. Without a contract, without a law and an obligation, there can be no fiscal levy. Application of the *Income Tax Act* is subject to a civil determination, whether such a determination be according to civil or common law (at 103).

<sup>51</sup> *Ibid.*

<sup>52</sup> *Ibid.* at 106, citing art. 1013 C.C.L.C. (“When the meaning of the parties in a contract is doubtful, their common intention must be determined by interpretation rather than by an adherence to the literal meaning of the words of the contract”); Marcel Planiol & Georges Ripert, *Traité pratique de droit civil français*, t. 10 by Joseph Hamel, François Givord & André Tunc, 2d ed. (Paris: Librairie générale de droit et de jurisprudence, 1956) No. 220; *Gravel c. Massicotte et Couillard* (1931), 52 B.R. 146; *Carey c. Carey* (1912), 42 C.S. 471; *A.R. Williams Machinery & Supply v. Morin*, [1933] S.C.R. 570, 4 D.L.R. 818.

<sup>53</sup> [1973] C.T.C. 2174, 27 D.T.C. 134 (T. Rev. B.) [*Chibougamau Lumber* cited to C.T.C.].

<sup>54</sup> *Ibid.* at 2178 (emphasizing that the contracts were “never intended ... to be a true reflection of the arrangement” and were therefore shams or artificial transactions subject to the anti-avoidance rule in then s. 137(1) of the *ITA*).

taxpayer conveyed possession of an apartment building in 1969 under an agreement and retained ownership until it received a stipulated amount through instalment payments.<sup>55</sup> Although concluding on the basis of civil law authorities that the taxpayer had not sold the property in 1969, Justice Addy nonetheless held that the taxpayer had disposed of the property in that year for two reasons: First, he explained, because the statutory definition of a disposition in then paragraph 20(5)(c) (now subsection 248(1)) was not “exhaustive or restrictive,”<sup>56</sup> the concept should be given its “broadest possible meaning.”<sup>57</sup> Second, he declared, since the concept of an acquisition is “obviously the direct opposite” of a disposition, the twofold test in *Wardean Drilling* should apply to determine the disposition of property as well as its acquisition.<sup>58</sup> On this basis, the court concluded that the taxpayer disposed of the property in 1969 when it “completely divested itself of all of the duties, responsibilities and charges of ownership and also all of the profits, benefits and incidents of ownership, except the legal title.”<sup>59</sup>

Although *Olympia and York* was followed in at least one subsequent decision involving a *disposition* of property in Quebec,<sup>60</sup> other decisions in the early 1990s continued to apply the civil law rather than *Wardean Drilling* to decide if a taxpayer had *acquired* property for the purposes of the *ITA*. In *Fortin & Moreau*, for example, a taxpayer sought to deduct capital cost allowance on garbage trucks and bins that it had leased for a sixty-five-month term with a purchase option after sixty months at a price less than the probable value of the equipment at that time.<sup>61</sup> The Tax Court of Canada relied on the civil law, not *Wardean Drilling*, to conclude that the taxpayer had not acquired depreciable property within the meaning of the *ITA*. Emphasizing that “the Code does not recognize [the] ... dismemberment of ownership rights” presumed by the second branch of the twofold test in *Wardean Drilling*,<sup>62</sup> Chief Justice Couture of the Tax Court of Canada characterized the contract as a “a conditional obligation on a suspensive condition,” which does not transfer ownership until the purchase option is exercised.<sup>63</sup> He thereby disallowed the deduction on the

<sup>55</sup> (1980), [1981] 1 F.C. 691, 34 D.T.C. 6184 (T.D.) [*Olympia and York* cited to F.C.].

<sup>56</sup> *Ibid.* at 709.

<sup>57</sup> *Ibid.*, citing *Canada v. Cie Immobilière BCN ltée* (1978), [1979] 1 S.C.R. 865 at 876, 97 D.L.R. (3d) 238 [*Cie Immobilière*].

<sup>58</sup> *Olympia and York*, *ibid.* (An acquisition within the meaning of the *ITA* “must contain substantially the same elements viewed from the side of the person acquiring the asset as opposed to the person disposing of it” at 709).

<sup>59</sup> *Ibid.* at 710.

<sup>60</sup> See *Robert Bédard auto ltée v. M.N.R.*, [1985] 2 C.T.C. 2354, 39 D.T.C. 643 (T.C.C.).

<sup>61</sup> *Supra* note 11.

<sup>62</sup> *Ibid.* at 2595, citing art. 406 C.C.L.C. (“Ownership is the right of enjoying and of disposing of things in the most absolute manner, provided that no use be made of them which is prohibited by law or by regulation”).

<sup>63</sup> *Ibid.* at 2596 (“Writers are of the opinion that the suspensive obligation does not transfer the right of ownership on the date of execution of the agreement. Ownership is only transferred to the purchaser when the condition is fulfilled, with retroactive effect to the date of the agreement”). The

ground that the applicable statutory definition of “depreciable property” required the taxpayer to own the property at the end of its taxation year in order to have acquired the property for tax purposes.<sup>64</sup> Notwithstanding this conclusion, however, Chief Justice Couture relied on the second branch of the twofold test in *Wardean Drilling* to conclude that the taxpayer had acquired property for the purpose of the interest deduction in paragraph 20(1)(c) and the investment tax credit in subsection 127(10) on the basis that these provisions, unlike the definition of depreciable property, did not require the taxpayer to own the property at the end of the year.<sup>65</sup>

*Fortin & Moreau* was followed in two subsequent tax cases in Quebec, each of which involved leasing agreements with an option to purchase during the term of the lease.<sup>66</sup> Chief Justice Couture’s conclusion that the taxpayer had not acquired depreciable property within the meaning of the *ITA* was also upheld on appeal by way of trial *de novo* at the Federal Court, Trial Division. The Federal Court affirmed his opinion that capital cost allowance may only be deducted by the owner of the property, and his determination that the contract did not transfer ownership of the property until the purchase option was exercised.<sup>67</sup> Unlike the Tax Court of Canada, however, the Federal Court also disallowed the deduction of the interest expenses and investment tax credits claimed by the taxpayer on the ground that it had not acquired the property for the purpose of these provisions, or fulfilled the statutory definition of depreciable property. Rejecting the taxpayer’s argument that it had acquired the property under the second branch of the twofold test in *Wardean Drilling*, Justice Tremblay-Lamer distinguished *Wardean Drilling* on the basis that it had not involved an option to purchase, and declined to apply its twofold test to the lease-option agreements because this would produce “a legal effect that fails to reflect the obligations created by the applicable private law, in this case the civil law.”<sup>68</sup> As a

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legal nature and effect of conditional obligations in civil law are examined more fully at *infra* notes 120ff. and accompanying text.

<sup>64</sup> *Ibid.* at 2597 (“Prior to the 1979 taxation year, the Act referred essentially to property acquired by a taxpayer during a fiscal year, but ... an amendment was made to the paragraph applicable to property acquired since December 11, 1979, requiring the taxpayer, from that date, to own such property, at the end of the year, that is, his taxation year”).

<sup>65</sup> *Ibid.* (“the agreement between the parties resulted, for the purposes of the Act, in the acquisition of property by the [taxpayer]. It had possession and use of the ... property and had assumed all the risks; furthermore it was almost certain [to] exercise the option to purchase when the agreement expired” at 2599).

<sup>66</sup> See *Dumais*, *supra* note 11 (the taxpayer could not deduct capital cost allowance because “it only had the rights of a lessee determined by the terms of the leasing contract” and was “therefore not the owner of this property” at 2658 [translated by author]). See also *Gaétan Lévesque*, *supra* note 11, Lamarre Proulx T.C.J. at para. 14 (ownership of property is “essential” for a taxpayer to deduct capital cost allowance).

<sup>67</sup> *Bérou (F.C.T.D.)*, *supra* note 11 at para. 22.

<sup>68</sup> *Ibid.* at para. 58. Tremblay-Lamer J. explained that because the taxpayer’s acquisition of property in the case before her depended on this future and uncertain event, it was “difficult to conclude” that the taxpayer had “acquired” the property prior to the exercise of this option, even if the term [was] given the expansive meaning of *M.N.R. v. Wardean Drilling Limited*” (at para. 57).

result, she concluded, “absent an irrevocable promise of purchase and sale, I am unable to conclude that there was an acquisition before the option was exercised.”<sup>69</sup>

On further appeal, however, a majority of the Federal Court of Appeal reversed the trial decision and allowed the deduction of capital cost allowance, interest expenses, and investment tax credits, on the ground that the taxpayer had acquired the property for the purposes of the *ITA* irrespective of its ownership under the civil law of Quebec.<sup>70</sup> For Justice Desjardins, this conclusion rested on three propositions: First, she explained, through subparagraph 54(c)(v) of the statutory definition of a disposition<sup>71</sup> and the interpretive rule in subsection 248(3),<sup>72</sup> as these provisions then read, Parliament had “devised, for tax purposes and for all of Canada, a common concept covering the ideas of ‘disposition’ (‘disposition des biens’) and ‘beneficial ownership’ (‘propriété effective’), both in civil and common law.”<sup>73</sup> Second, she emphasized, the parties themselves admitted that “the effect of s. 54(c)(v) was to incorporate into the Act the common law rule that property is subject to a disposition when there is a transfer of ‘beneficial ownership’, even though the ‘legal ownership’ remained unchanged.”<sup>74</sup> Third, she declared, “the corollary of these provisions” is that “when there was a ‘disposition’ for a party to a contract the other party made an ‘acquisition’ or obtained the ‘beneficial ownership’ of it.”<sup>75</sup> As a result, she concluded:

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<sup>69</sup> *Ibid.* at para. 62.

<sup>70</sup> *Bérou, supra* note 7.

<sup>71</sup> *Ibid.* at 182. According to this provision (an amended version of which now appears in ss. (e) and (f) of the definition of a “disposition” in s. 248(1) of the *ITA*), a disposition of property does not include “any transfer of property by virtue of which there is a change in the legal ownership of the property without any change in the beneficial ownership thereof” (*Income Tax Act*, S.C. 1970-71-72, c. 63, s. 54(c)(v)).

<sup>72</sup> *Bérou, ibid.* at 183. According to this provision, which was subsequently amended:

In its application in relation to the Province of Quebec, a reference in this Act to any property that is or was beneficially owned by any person shall be read as including a reference to property in relation to which any person has or had the full ownership whether or not the property is or was subject to a servitude, or has or had a right as a usufructuary, a lessee in an emphyteutic lease, an institute in a substitution or a beneficiary in a trust; and a reference in this Act to the beneficial owner of any property shall be read as including a reference to a person who has or had, accordingly as the context requires, such ownership as a right in relation to that property.

<sup>73</sup> *Bérou, ibid.*

<sup>74</sup> *Ibid.* Curiously, the provision does not actually state this, providing only that a transfer of legal ownership without a change in beneficial ownership does *not* constitute a disposition, not that a transfer of beneficial ownership without a change in legal ownership *does* constitute a disposition. For a similar observation, see Marie-Pierre Allard, “The Retroactive Effect of Conditional Obligations in Tax Law” (2001) 49 *Can. Tax J.* 1726 at 1796 [Marie-Pierre Allard, “Conditional Obligations”]. See also Duff, *supra* note 13 at 57-58.

<sup>75</sup> *Bérou, ibid.* at 183 (Desjardins J.A. cited *Olympia and York (supra* note 55) in support of this view). As explained in Part III of this paper, this proposition does not follow as a logical corollary of



[I]n so far as the leasing contracts in the case at bar may be seen as contracts recognizing “beneficial ownership” like the contracts given as examples in s. 248(3) of the Act, the beneficial ownership of the dump trucks was acquired by the appellant when the contracts were concluded in 1982. ... Since the appellant had the possession and use of the dump trucks in addition to assuming the risk and obligations pertaining to them, it obtained “beneficial ownership” of that property in 1982.<sup>76</sup>

Similarly, Justice Létourneau based his conclusion that the taxpayer had acquired the property for tax purposes on the legislative intent expressed in subsection 248(3) to harmonize the civil law of Quebec with the common law of other provinces,<sup>77</sup> on the judicial presumption that an acquisition of property is the counterpart of a disposition, and on the further proposition (which was admitted by the parties) that, under subparagraph 54(c)(v), there was “a disposition of property when there was a transfer of beneficial ownership even though the seller retained legal ownership.”<sup>78</sup> In addition, he suggested, this conclusion was consistent with developments in the civil law, which “[o]ver the years, ... gradually and from necessity, has been adapted to correspond to certain commercial situations and particular subdivisions of the ownership right which the common law had devised to meet the demands of these situations.”<sup>79</sup> As well, Justice Létourneau emphasized that these considerations provided a sound basis for the application in Quebec of the Canada Revenue Agency’s Interpretation Bulletin identifying circumstances in which it would consider a transaction to be a sale rather than a lease,<sup>80</sup> and that “it would be inappropriate for

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then ss. 54(c)(v) and 248(3), but depends on Desjardins J.A.’s second proposition that the effect of s. 54(c)(v) was to extend the definition of a disposition to include transfers of beneficial ownership, and on the judicial interpretation in *Olympia and York* that the concept of an acquisition is the “direct opposite” of a disposition and “must contain substantially the same elements from the side of the person acquiring the asset as opposed to the person disposing of it” (*supra* note 55 at 709).

<sup>76</sup> *Bérou*, *ibid.* at 184.

<sup>77</sup> *Ibid.* at 186 [footnotes omitted].

<sup>78</sup> *Ibid.* at 188.

<sup>79</sup> *Ibid.* at 187. See also *ibid.* at 189 (“the trend in the civil law is to approximate more closely to the common law”); *ibid.* at 191-92 (civil law courts have often characterized lease-option agreements as instalment sales “in which the normal incidents of ownership (beneficial ownership) were transferred to the purchaser,” and the Court of Appeal of Québec concluded that the lessee under a leasing agreement “had acquired the property when he obtained beneficial ownership of it, even though he lacked the real right conferred by legal ownership”).

<sup>80</sup> *Ibid.* at 186. Canada Revenue Agency, Interpretation Bulletin IT-233R, “Lease-Option Agreements; Sale-Leaseback Agreements” (11 February 1983) at para. 3. This Interpretation Bulletin replaced IT-233 (14 July 1975), and was cancelled by the Canada Revenue Agency in 2001 because it was inconsistent with the Supreme Court of Canada’s statement in *Shell Canada Ltd. v. Canada* that “the economic realities of a situation [cannot be used] to recharacterize a taxpayer’s *bona fide* legal relationships” ([1999] 3 S.C.R. 622 at 641, 178 D.L.R. (4th) 26). As a result, according to the Canada Revenue Agency, “the determination of whether a contract is a lease or sale is based on the legal relationships created by the terms of the agreement, rather than on any attempt to ascertain the underlying economic reality. Therefore, in the absence of a sham, it is our view that a lease is a lease and a sale is a sale” (Income Tax Technical News, No. 21 (14 June 2001)).

this Court to ignore or repudiate the content of the said Bulletin 17 years later, as the respondent is asking us to do in the case at bar.”<sup>81</sup> As a result, he concluded, the taxpayer had acquired the property within the meaning of the *ITA* when it “obtained the usual incidents of the right of ownership over the property, namely possession, use and risk of loss, together with the obligations resulting from those incidents.”<sup>82</sup>

Dissenting, Justice Noël would have disallowed the deductions for three reasons: First, in the absence of a statutory definition, the concept of an acquisition of property “must be understood in its ordinary sense that is as referring to the acquisition of *ownership* of property.”<sup>83</sup> Second, he emphasized, “in the absence of some indication to the contrary, ownership of property cannot be acquired otherwise than in accordance with the applicable private law.”<sup>84</sup> Third, since the parties did not intend ownership of the property to be transferred until the purchase option was exercised, it followed that the taxpayer did not acquire the property for the purposes of the *ITA* until the option was exercised.<sup>85</sup>

Three years later, in *Terexcavation*, the Tax Court of Canada considered yet another lease-option agreement involving a tractor that the taxpayer leased for six months with an option to purchase at the end of the lease.<sup>86</sup> Allowing the taxpayer’s appeal from an assessment disallowing the deduction of an investment tax credit on the grounds that the tractor was no longer new when the taxpayer acquired it at the end of the lease, Justice Lamarre Proulx relied on the second branch of the twofold test in *Wardean Drilling* to conclude that the taxpayer had acquired the tractor at the outset of the lease, which she characterized as “a financial lease for the purpose of acquiring property.”<sup>87</sup> Significantly, Justice Lamarre Proulx declared:

[I]t is a mistake to see the issue of the interpretation to be given to the term “acquired” as a debate between civil law and common law on the concept of ownership. In the Court’s view, *Wardean* interpreted the meaning of the term “acquired” on the basis of the tax legislation. That interpretation may or may not correspond to the common law concept of ownership; that is not the point. The point is that this interpretation was made on the basis of the tax legislation.<sup>88</sup>

As a result, she suggested, the concept of an acquisition of property has a tax meaning that is effectively dissociated from all private law concepts, even if its interpretation happens to correspond to the common law distinction between legal and beneficial

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<sup>81</sup> *Bérou*, *ibid.* at 193.

<sup>82</sup> *Ibid.* at 186-87.

<sup>83</sup> *Ibid.* at 221 [emphasis in original].

<sup>84</sup> *Ibid.*

<sup>85</sup> *Ibid.* at 225.

<sup>86</sup> *Supra* note 7.

<sup>87</sup> *Ibid.* at para. 39.

<sup>88</sup> *Ibid.* at para. 35.

ownership. As argued in Part III of this paper, it is doubtful that this conclusion can survive the enactment of section 8.1 of the *Interpretation Act*.

## II. The Ownership and Transfer of Property in Common Law and Civil Law

As the tax cases in the first part of this paper demonstrate, courts have generally referred to common law or civil law concepts in order to interpret the meaning of an acquisition of property for tax purposes—either explicitly as in *Lagueux & Frères*, *Fortin & Moreau*, the trial decision in *Bérou (F.C.T.D.)*, and Justice Noël’s dissenting opinion on appeal, or implicitly as in Justice Cattanach’s twofold test in *Wardean Drilling* and subsequent cases that have relied on this test. Before considering the impact of section 8.1 of the *Interpretation Act* on the meaning of this concept, it is useful to review the rules, principles, and concepts governing the ownership and transfer of property in common law and civil law in order to understand their possible impact on the meaning of an acquisition of property for tax purposes.

### A. The Ownership and Transfer of Property in Common Law

The concept of ownership in the common law tradition is generally understood as “an enforceable bundle of rights that links a person to a thing.”<sup>89</sup> As A.M. Honoré explains in a much-cited article on the subject: “Ownership comprises the right to possess, the right to use, the right to manage, the right to the income of the thing, the right to the capital, the right to security, the rights or incidents of transmissibility and absence of term, the prohibition of harmful use, liability to execution, and the incident of residuary.”<sup>90</sup> For Bruce Ziff, these rights may be reduced to the following four: (1) possession, management, and control; (2) income and capital; (3) transmission *inter vivos* and on death; and (4) protection under the law.<sup>91</sup>

In addition to this bundle of rights concept, the common law generally distinguishes between “legal” and “beneficial” ownership—a distinction that originates in the common law of trusts, but has developed a legal meaning that extends beyond the relationship between trustees and beneficiaries.<sup>92</sup> Most property in common law jurisdictions is held both legally and beneficially, such that the person with legal title also has the right to use and enjoyment.<sup>93</sup> However, the concepts are widely used, as one commentator explains, “to distinguish a right or power one

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<sup>89</sup> Derek Mendes da Costa & Richard J. Balfour, *Property Law: Cases, Text and Materials*, 2nd ed. by Eileen E. Gillese (Toronto: Emond Montgomery, 1990) at 2:1.

<sup>90</sup> “Ownership” in A.G. Guest, ed., *Oxford Essays in Jurisprudence: A Collaborative Work* (London: Oxford University Press, 1961) 107 at 113.

<sup>91</sup> *Principles of Property Law*, 4th ed. (Toronto: Carswell, 2006) at 2-3.

<sup>92</sup> Brown, *supra* note 9 at 452.

<sup>93</sup> Arthur Allen Leff, “The Leff Dictionary of Law: A Fragment” (1985) 94 Yale L.J. 1855, s.v. “beneficial”.

possesses for his own use and enjoyment from one possessed for the use and enjoyment of another.”<sup>94</sup> In these circumstances, the common law regards the person who holds legal title to the property as its “legal owner” and the person who possesses the bundle of rights comprising the “normal incident” of ownership as the “beneficial owner” of the property.<sup>95</sup> Since the common law conceptualizes ownership as a bundle of rights, moreover, the beneficial owner is generally regarded as the “real” or “true” owner of the property.<sup>96</sup>

Where two parties enter into a contract to sell property, common law jurisdictions generally provide that the property is transferred to the buyer “at such time as the parties to the contract intend it to be transferred.”<sup>97</sup> For this purpose, according to provincial sale of goods statutes, “regard shall be had to the terms of the contract, the conduct of the parties and the circumstances of the case.”<sup>98</sup> In addition, these statutes contain several rules “for ascertaining the intention of the parties as to the time at which the property in goods is to pass to the buyer,” which generally apply “[u]nless a different intention appears.”<sup>99</sup> In *Wardean Drilling*, the court relied on one of these rules to help determine when the taxpayer had acquired the property for tax purposes.<sup>100</sup> In other cases, courts have relied on more general principles to determine if, and when, property has passed to a purchaser of goods. The most difficult of these cases involve conditional sales agreements and lease-option agreements—in each of which legal title to the property remains with the vendor or lessor until the conditions are satisfied or the purchase option is exercised.

Where conditional sales agreements are involved, courts in common law provinces have generally held that the purchaser acquires either property in the goods, or equitable ownership, once possession, use, and risk are transferred.<sup>101</sup> In

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<sup>94</sup> *Ibid.*

<sup>95</sup> *Black’s Law Dictionary*, 8th ed., s.v. “beneficial owner”.

<sup>96</sup> See e.g. *Csak v. Aumon* (1990), 69 D.L.R. (4th) 567 (Ont. H.C.J.) (the beneficial owner of property is “the real owner of the property even though it is in someone else’s name” at 567); *MacKeen Estate v. Nova Scotia* (1977), 25 N.S.R. (2d) 572, (*sub nom. Cowan v. Nova Scotia (Minister of Finance)*) 78 D.L.R. (3d) 66 (S.C.(T.D.)) (“the plain ordinary meaning of the expression ‘beneficial owner’ is the real or true owner of the property” N.S.R. at para. 46, *aff’d* (1978), 28 N.S.R. (2d) 3, 89 D.L.R. (3d) 426.

<sup>97</sup> See e.g. the Alberta *Sale of Goods Act*, *supra* note 21, ss. 19(1)-(2). Identical provisions appear in sale of goods statutes in other common law provinces.

<sup>98</sup> *Ibid.*, s. 198(2).

<sup>99</sup> *Ibid.*, s. 20(1).

<sup>100</sup> *Supra* note 6. See especially *supra* note 21 and accompanying text.

<sup>101</sup> See e.g. *R. v. Hemingway*, [1955] S.C.R. 712 at para. 38, 1 D.L.R. (2d) 34, Estey J. (the accused was found guilty of obtaining goods by false pretences on the basis that he had “acquired possession of the goods and a special property or interest therein” pursuant to a conditional sales agreement with the vendor); *C.C. Motor Sales Ltd. v. Chan*, [1926] S.C.R. 485 at 491, [1926] 3 D.L.R. 712 (the plaintiff, who had purchased an automobile under a conditional sales agreement, was entitled to the excess of proceeds over unpaid instalment payments after the defendant took possession of the vehicle

*Hendrickson*, for example, the plaintiff sued the defendant for conversion after the defendant purchased and resold an automobile from an individual who acquired it under a false name from the plaintiff pursuant to a conditional sales agreement.<sup>102</sup> The Alberta Supreme Court found for the defendant on the basis that the conditional sales agreement had transferred property in the goods to the individual, notwithstanding that the vendor retained title to the goods until all amounts owing were paid. According to the court:

It will be observed that what is reserved to the vendor until payment in full is “title” to the said goods. Nowhere in the agreement is it stated that “property” in the goods shall remain in the vendor until payment in full. Now, I conceive “title” and “property” to be two entirely different things. One person may hold bare title to property while the whole beneficial ownership rests in some other person. A reservation of title does not necessarily imply that no property shall pass to the purchaser, and indeed the agreement itself contemplates that some property interest will pass to this purchaser.<sup>103</sup>

As Justice Noël observed in *Hewlett Packard*, the language and reasoning that Justice Cattanach employed in *Wardean Drilling* is similar to that in *Hendrickson*.<sup>104</sup>

Where possession is conveyed under a lease with a purchase option, courts in common law provinces have generally distinguished between “true leases” under which the essential incidents of ownership remain with the lessor, and “financing leases” or “security leases,” under which the lessee acquires beneficial ownership while the lessor retains legal title as a form of security interest.<sup>105</sup> Although the distinction between these two kinds of leases is often difficult to draw in practice,<sup>106</sup> factors favouring characterization as a financing or security lease include: (1) automatic vesting of ownership in the lessee at the end of the lease or upon payment of a stipulated amount, or an obligation to purchase the property at the end of the lease; (2) a lease term that corresponds to the property’s useful life; (3) lease payments that are equal to or greater than the sum of the property’s capital and finance costs; (4) an option price lower than the expected value of the property when the option may be exercised; (5) lease terms allocating the loss or gain from a subsequent disposition of the property to the lessee; (6) transactions in which the lessor purchases property from a supplier selected by the lessee for the purpose of

and sold it under the provisions of the agreement, on the grounds that the plaintiff had acquired equitable ownership of the property, notwithstanding that the defendant retained legal ownership).

<sup>102</sup> *Supra* note 24.

<sup>103</sup> *Ibid.* at 283-84.

<sup>104</sup> *Supra* note 23.

<sup>105</sup> See Ronald C.C. Cuming, Catherine Walsh & Roderick J. Wood, *Personal Property Security Law* (Toronto: Irwin Law, 2005) at 67-75.

<sup>106</sup> See e.g. *Re Philip Services Corp.* (1999), 15 C.B.R. (4th) 107, 94 A.C.W.S. (3d) 13 (Ont. Sup. Ct. J.), Farley J. (“the task involves a weighing of the various material matters involved. It is not a simple analysis of determining between black and white but rather the shade of grey where all factors are weighed in the balance as to whether the scales would tip towards a true lease relationship—or alternatively against being a true lease relationship” at 109).

leasing the property to the lessee; and (7) contractual remedies characteristic of a financing transaction, such as acceleration of payments in the event of default.<sup>107</sup> Although none of the tax cases in common law provinces involving lease-option agreements have cited any of the common law judgments in which these factors have been applied, most have considered similar factors in order to determine whether lessees have acquired property for tax purposes under the terms of the agreement.<sup>108</sup> These factors may also have influenced the Canada Revenue Agency's administrative practice, as they correspond to the circumstances under which the Canada Revenue Agency was formerly prepared to characterize lease-option agreements as sales rather than as leases.<sup>109</sup>

### **B. The Ownership and Transfer of Property in Civil Law**

Unlike the common law, the civil law of Quebec regards ownership as absolute and indivisible. According to the *Civil Code of Québec*, ownership is defined as “the right to use, enjoy and dispose of property *fully* and freely, subject to the limits and conditions for doing so determined by law.”<sup>110</sup> In addition, the C.C.Q. continues, ownership of property “gives a right to what it produces and to what is united to it,”<sup>111</sup> so that the “fruits and revenues of property belong to the owner.”<sup>112</sup> As Henri Mazeaud explains, while the right of ownership under the civil law comprises three attributes—“the *jus utendi*, or right to make use of the thing, the *jus fruendi*, or right to receive income produced by it, and the *jus abutendi*, or right to dispose of the thing: to preserve, give, sell, destroy or abandon it”—this right is a “*total right*”

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<sup>107</sup> See Cuming, Walsh & Wood, *supra* note 105 at 70-75.

<sup>108</sup> See e.g. *Mimetix*, *supra* note 7 (where the definitive factor was the absence of an option to purchase “at a price substantially less than the probable fair market value of the property at the time of exercising the option” at 2211); *Kamsel Leasing*, *supra* note 42 (lessees have the right to acquire the property at the expiration of the lease “at a price which at the inception of the lease could be said to be substantially less than the probable fair market value of the property at the time of permitted acquisition” at 2283).

<sup>109</sup> See Interpretation Bulletin IT-233R, *supra* note 80. The Canada Revenue Agency cancelled this Interpretation Bulletin on the grounds that “the determination of whether a contract is a lease or sale is based on the legal relationships created by the terms of the agreement, rather than on any attempt to ascertain the underlying economic reality” (Income Tax Technical News, No. 21, *supra* note 80). The apparent correspondence between the factors used by common law courts to distinguish true leases from financing and security leases and the factors listed in the Interpretation Bulletin suggest that this decision may have been misconceived. These factors can determine the legal relationships created by the agreement as well as the economic reality.

<sup>110</sup> Art. 947 C.C.Q. [emphasis added].

<sup>111</sup> *Ibid.*, art. 948.

<sup>112</sup> *Ibid.*, art. 949 (adding that the owner “bears the costs he incurred to produce” these fruits and revenues). See also *ibid.*, art. 950 (the owner of the property “assumes the risks of loss”).

giving the owner “complete powers over the thing.”<sup>113</sup> As a result, it follows, while the C.C.Q. contemplates various “dismemberments” of ownership in the form of a usufruct, use, servitude, or emphyteusis, these dismemberments do not transfer ownership itself, which remains with the original owner subject to the right or charge created by the dismemberment.<sup>114</sup> Nor does the civil law of Quebec recognize the common law distinction between legal and beneficial ownership, since these concepts are merged within a unitary conception of ownership.<sup>115</sup>

Despite these differences between the civil law and the common law, both legal systems share the principle that contracts for the sale of property are to be interpreted according to the intent of the parties.<sup>116</sup> According to the C.C.Q., “[t]he common intention of the parties rather than adherence to the literal meaning of the words shall be sought in interpreting a contract.”<sup>117</sup> Professor Jobin explains that even where the wording of a contract does not seem ambiguous, the judge may depart from the declared will of the parties and adopt an interpretation of the contract that is more consistent with their true intention. Thus, the formal qualification of a contract as a sale or as a lease does not oblige the judge to apply the rules relative to these types of contracts.<sup>118</sup> Similarly, the Superior Court of Québec ruled in *Thibault v. Auger* that in order to determine the legal effect of a contract, “one must look for the intention of the parties, whatever the name they may give it. ... if the contract that [the parties] call a lease displays all the characteristics of a sale, it will be governed not by the principles of lease but by those of sale.”<sup>119</sup>

With respect to the characterization of contracts, the C.C.Q. contemplates different kinds of sales and different kinds of leasing arrangements. Where a seller transfers possession, use, and risk to a buyer, but retains ownership pending full payment of the purchase price, the transaction is defined as an “instalment sale”.<sup>120</sup> While an instalment sale creates an existing obligation to transfer ownership once the purchase price is paid in full, this obligation constitutes an “obligation with a

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<sup>113</sup> Henri Mazeaud *et al.*, *Leçons de droit civil*, t. 2, vol. 2, 8th ed. by François Chabas (Paris: Montchrestien, 1994) No. 1332, cited in *Cie Immobilière*, *supra* note 57 at 876-877 [translated in *Cie Immobilière*, emphasis in original].

<sup>114</sup> See arts. 1119, 1120 (usufruct), 1172 (use), 1177 (servitude), 1195 (emphyteusis) C.C.Q.

<sup>115</sup> See e.g. *Laliberté v. LaRue* (1930), [1931] S.C.R. 7, [1931] 2 D.L.R. 12, Rinfret J. (“[T]he legal system in the Province of Quebec does not include the common law concept which recognizes beneficial ownership in one person and legal title in another. In Quebec, both are invariably combined in the same person. Ownership is unitary” S.C.R. at 16 [translated by author]). It follows that a civil law trust is conceptually unlike a common law trust. The civil law trust property is owned neither by the trustee nor the beneficiary but by an “autonomous and distinct” patrimony in which neither the trustee nor the beneficiary has rights as an owner (art. 1261 C.C.Q.).

<sup>116</sup> See *Bérou*, *supra* note 7 at 225.

<sup>117</sup> Art. 1425 C.C.Q.

<sup>118</sup> Pierre-Gabriel Jobin with the collaboration of Nathalie Vézina, *Les obligations*, 6th ed. (Cowansville, Qc.: Yvon Blais, 2005) No. 435.

<sup>119</sup> [1950] C.S. 343 at 345 [translated by author].

<sup>120</sup> Art. 1745 C.C.Q.

suspensive term” that “does not become exigible until the occurrence of a future and certain event.”<sup>121</sup> As such, an instalment sale does not transfer ownership until the term is complete—when the buyer has paid the full amount of the purchase price.<sup>122</sup>

In contrast to instalment sales, which create obligations with a suspensive term, the C.C.Q. also contemplates transactions which create conditional obligations. According to article 1497, “[a]n obligation is conditional where it is made to depend upon a future and uncertain event, either by suspending it until the event occurs or is certain not to occur, or by making its extinction dependent on whether or not the event occurs.”

Where a conditional obligation is suspended until a future and uncertain event occurs or is certain not to occur, the condition is suspensive and the obligation comes into existence only when the event occurs or is certain not to occur.<sup>123</sup> Where a conditional obligation is extinguished by the occurrence of a future and uncertain event, the condition is resolutive and the obligation comes into existence when the contract is concluded, but ceases upon the occurrence of the future and uncertain event.<sup>124</sup> Although the C.C.Q. is not explicit on the matter, civil law authorities agree that the future and uncertain event upon which the conditional obligation depends must be “extrinsic to the legal relationship” between the parties,<sup>125</sup> which distinguishes this kind of transaction from an instalment sale in which the suspensive term that the price must be paid in full is intrinsic to the contract.<sup>126</sup> As well, since the C.C.Q. provides that “fulfillment of the condition has a retroactive effect, between the parties and with respect to third persons, to the day on which the debtor obligated himself conditionally,”<sup>127</sup> a sale on a suspensive condition is further distinguished from an instalment sale by making the transfer of ownership on fulfillment of the condition retroactive to when the agreement was executed.<sup>128</sup>

In addition to these different kinds of sales transactions, the C.C.Q. also contemplates different kinds of leasing arrangements. Under a conventional lease, ownership remains with the lessor, who “undertakes to provide ... the lessee, in return for a rent, with the enjoyment of a movable or immovable property for a certain time.”<sup>129</sup> Under a contract of leasing, on the other hand, the lessor “puts movable

<sup>121</sup> Art. 1508 C.C.Q.

<sup>122</sup> Marie-Pierre Allard, “Conditional Obligations”, *supra* note 74 at 1747.

<sup>123</sup> *Ibid.* at 1730.

<sup>124</sup> *Ibid.* at 1731.

<sup>125</sup> Henri Mazeaud *et al.*, *Leçons de droit civil*, t. 2, vol. 1, 9th ed. by François Chabas (Paris: Montchrestien, 1998) at 1078-79 [translated by author]. See also Jobin, *Les obligations*, *supra* note 118, No. 611.

<sup>126</sup> See e.g. *Commission de protection du territoire agricole du Québec v. Venne*, [1989] 1 S.C.R. 880 at 903-04, 95 N.R. 335, Beetz J. See also Jobin, *Les obligations*, *ibid.*, No. 605.

<sup>127</sup> Art. 1506 C.C.Q.

<sup>128</sup> Marie-Pierre Allard, “Conditional Obligations”, *supra* note 74 at 1730.

<sup>129</sup> Art. 1851 C.C.Q.



property at the disposal of ... the lessee, for a fixed term and in return for payment” after “acquir[ing] the property that is the subject of the leasing from a third person, at the demand and in accordance with the instructions of the lessee.”<sup>130</sup> Although some authorities suggest that a leasing agreement is “a financial operation tending to the acquisition of ownership by the user” when it is combined with an option to purchase the property,<sup>131</sup> the more accurate view is that the promise of a sale accompanied by yet unfulfilled conditions is not equivalent to a sale,<sup>132</sup> and that an option to purchase property subject to a leasing agreement cannot confer ownership until the option is exercised.<sup>133</sup> Indeed, although the lessee under a leasing arrangement may, as Justice Létourneau observed in *Bérou*, be “treated ... like an owner purchaser” in “economic terms”,<sup>134</sup> the C.C.Q. itself states that “[t]he lessor acquires the property that is the subject of the leasing,”<sup>135</sup> and Justice Létourneau himself acknowledged that a leasing agreement does not confer upon the lessee the real right to the property.<sup>136</sup>

Although most of the tax cases in Quebec involving lease-option agreements have considered these civil law rules and principles, they have reached widely different conclusions on the legal consequences of these rules and principles and on their implications for the acquisition of property under the *ITA*. For example, in

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<sup>130</sup> Art. 1842 C.C.Q.

<sup>131</sup> Claude Gilbert, “La nature et l’intérêt du crédit-bail en informatique” (1988) 29 C. de D. 815 at 819-20, cited in *Bérou*, *supra* note 7 at 190, Létourneau J.A. See also *Pacific National Leasing Corp. c. Rose*, [2001] R.J.Q. 78.

<sup>132</sup> Léon Faribault, *Traité de droit civil du Québec*, vol. 11 (Montreal: Wilson & Lafleur, 1961) No. 116, cited in *Bérou (F.C.T.D.)*, *supra* note 11 at para. 44: “even when it is accompanied by delivery, a promise to sell is not equivalent to a sale where it is made subject to a suspensive condition, or where the parties have agreed that the prospective vendor is to retain ownership of the *res* until the purchase price is paid in full or until the promisee has fulfilled all his obligations” [translated by author]. See also *Robertson v. Canada*, [1990] 2 F.C. 717, 105 N.R. 123, Marceau J. (“We cannot look at the taxpayer who exercises the option as if he had owned the shares all along; the power to acquire the shares should not be confused with ownership of the shares itself” F.C. at 726); *Mitsui & Co. (Canada) Ltd. v. Royal Bank of Canada*, [1995] 2 S.C.R. 187, 142 N.S.R. (2d) 1, Major J. (“An option contract is an antecedent contract because it precedes the contract of purchase and sale that will result if the opportunity provided by the option is ‘seized upon’ or exercised. Once an option is exercised, the parties discharge their obligations under the option contract by entering into the contract of purchase and sale” S.C.R. at 201). Article 1710 of the C.C.Q. states that “The promise of sale with delivery and actual possession is equivalent to sale,” but it is possible to depart from this presumption where the parties have established conditions to be fulfilled before the transfer of ownership. See e.g. *Nadeau c. Dulac*, [1953] 1 S.C.R. 164; *Matériaux J.C. Brunet c. Caron*, [2003] R.D.I. 18, 23 C.L.R. (3d) 198.

<sup>133</sup> Pierre-Gabriel Jobin, *Le louage*, 2d ed. (Cowansville, Qc.: Yvon Blais, 1996) at 52 (an option to purchase is a mere possibility. The essence of a leasing is to confer a *jus ad rem*, not a real right).

<sup>134</sup> *Supra* note 7 at para. 23. See e.g. arts. 1845 (the seller of the property is “directly bound towards the lessee by the legal and conventional warranties inherent in the contract of sale”), 1846 C.C.Q. (the lessee “assumes all the risks of loss of the property, even by superior force, from the time he takes possession of it” and “likewise assumes all maintenance and repair expenses”).

<sup>135</sup> Art. 1842 C.C.Q. [emphasis added].

<sup>136</sup> *Bérou*, *supra* note 7 at para. 23.

*Chibougamau Lumber*, the Tax Review Board characterized the agreement as “a purchase on a time payment plan” and concluded on this basis that the transaction transferred ownership of the property to the lessee.<sup>137</sup> In *Lagueux & Frères*, on the other hand, Justice Décary characterized the agreement as a sale on a suspensive condition, but also concluded that the transaction had transferred ownership of the property to the lessee.<sup>138</sup> In *Fortin & Moreau*, Chief Justice Couture also characterized the contract as a sale on a suspensive condition, but concluded that the transaction did not transfer ownership on the grounds that a suspensive obligation does not transfer ownership until the condition is fulfilled, with retroactive effect to the date of the agreement.<sup>139</sup> In *Bérou (F.C.T.D.)*, Justice Tremblay-Lamer concluded that the contract could not be characterized as a sale on a suspensive condition on the grounds that an option to purchase property is “a condition *intrinsic* to the contract, which depends on the will of one of the parties.”<sup>140</sup> He therefore held that the taxpayer had not obtained ownership under civil law or acquired the property for tax purposes until the purchase option was exercised.<sup>141</sup> On further appeal to the Federal Court of Appeal, Justice Noël concurred with this view, whereas Justices Desjardins and Létourneau dissociated the tax concept of an acquisition of property from civil law rules and principles governing the transfer of ownership, concluding instead that the taxpayer had acquired “beneficial ownership” of the property under the twofold test in *Wardean Drilling*.<sup>142</sup> Likewise, in *Terexcavation*, Justice Lamarre Proulx dissociated the tax concept of an acquisition of property from the civil law of Quebec, emphasizing that the meaning of an acquisition of property for tax purposes must be understood on the basis of the tax legislation rather than the private law of the province in which the relevant transaction occurs.<sup>143</sup>

As the next part of this paper explains, it is doubtful whether the Federal Court of Appeal decision in *Bérou* and the subsequent Tax Court of Canada judgment in *Terexcavation* remain valid after the enactment of section 8.1 of the *Interpretation Act*. If invalid, moreover, the cases decided prior to these two judgments suggest that the meaning of an acquisition of property may be subject to considerable uncertainty in the Province of Quebec.

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<sup>137</sup> *Supra* note 53 at 2178.

<sup>138</sup> *Supra* note 50 at 692-93. However, Décary J. is less specific elsewhere in his judgment. He states that the contracts resulted in “a sale on a suspensive condition, on instalment or by leasing” (at 691). As explained in this section, these alternatives are treated differently under the C.C.Q.

<sup>139</sup> *Supra* note 11 at 2596.

<sup>140</sup> *Supra* note 11 at para. 40 [emphasis added]. Tremblay-Lamer J. considered it unnecessary to determine whether the transaction should be characterized as an instalment sale (as opposed to a leasing with a purchase option), explaining that the legal consequences resulting from such a characterization would not affect the outcome, since “the contract would be formed upon the payment of the final fraction of the price” (*ibid.* at para. 48).

<sup>141</sup> *Ibid.* at para. 62.

<sup>142</sup> *Bérou*, *supra* note 7.

<sup>143</sup> *Supra* note 7 at para. 35.

### III. Canadian Bijuralism and the Meaning of an Acquisition of Property in the *Income Tax Act*

Although the Federal Court of Appeal decision in *Bérou* effectively dissociated the tax concept of an acquisition of property from the civil law of Quebec, the judgment was released on 15 November 1999, well before the introduction of section 8.1 of the federal *Interpretation Act*, which came into force on 1 June 2001.<sup>144</sup> Declaring the common law and the civil law to be “equally authoritative and recognized sources of the law of property and civil rights in Canada,” this provision stipulates that where it is necessary to refer to provincial law in interpreting an enactment, “unless otherwise provided by law ... reference must be made to the rules, principles or concepts in force in the province at the time [an] enactment is being applied.”<sup>145</sup> Therefore, to the extent that the interpretation of an acquisition of property under the *ITA* necessitates reference to provincial law, section 8.1 of the *Interpretation Act* may mandate a different result from that reached by a majority of the Federal Court of Appeal.

This part of this paper considers the impact of section 8.1 of the federal *Interpretation Act* on the meaning of an acquisition of property in the *ITA*, asking whether it is necessary to refer to provincial “rules, principles or concepts forming part of the law of property and civil rights” in order to interpret this concept and, if so, whether such a reference has been “otherwise provided by law.” In order to properly address these questions, however, it begins by reviewing section 8.1 more generally in light of the broader objectives of Canadian bijuralism.

#### A. Canadian Bijuralism and Section 8.1 of the Federal Interpretation Act<sup>146</sup>

Section 8.1 of the federal *Interpretation Act* was enacted in 2001 as part of the *Federal Law—Civil Law Harmonization Act, No. 1*,<sup>147</sup> the first in a series of legislative measures designed to advance the goals of Canadian bijuralism by harmonizing federal legislation with the civil law of Quebec. Defined narrowly as “the coexistence of two legal traditions within a single state,”<sup>148</sup> bijuralism may also be understood more broadly as “the sharing of values and traditions” associated with each of the two legal systems.<sup>149</sup> In Canada, bijuralism of the first kind is rooted in the *Quebec Act* of

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<sup>144</sup> *Terexcavation* was decided after this provision was enacted, but the court did not consider it.

<sup>145</sup> *Interpretation Act*, *supra* note 14.

<sup>146</sup> Part III.A is based on Duff, *supra* note 13.

<sup>147</sup> S.C. 2001, c. 4. For a detailed review of the origins and content of this legislation, see Marie-Noëlle Pourbaix, “S-4: A First Harmonization Bill” in *Harmonization*, *supra* note 13, fasc. 6 at 1-12.

<sup>148</sup> Marie-Claude Gervais & Marie-France Séguin, “Some Thoughts on Bijuralism in Canada and the World” in *Harmonization*, *ibid.*, fasc. 2 at 1.

<sup>149</sup> Justice Michel Bastarache, “Bijuralism in Canada” in *Harmonization*, *ibid.*, fasc. 1, 19 at 26.

1774,<sup>150</sup> which provided that French law would apply to matters of property and civil rights in the Province of Quebec, and is confirmed by the *Constitution Act, 1867*,<sup>151</sup> which grants exclusive authority to provincial governments to make laws in relation to “Property and Civil Rights”.<sup>152</sup> Bijuralism of the second kind is cultural and aspirational, but finds expression in federal policies and enactments, and in the evolving jurisprudence of Canadian courts.<sup>153</sup>

Although bijuralism as narrowly defined has existed in Canada since 1774, recognition of the civil law tradition at the federal level is a relatively recent development. Until the 1970s, federal legislation was typically drafted by English-speaking lawyers trained in the common law and then translated into French by translators with little or no legal training, with “makeshift” adjustments to accommodate the interaction of this legislation and the civil law of Quebec.<sup>154</sup> At the same time, Supreme Court of Canada decisions routinely ignored the distinctive character of the civil law of Quebec, interpreting provisions of the *Civil Code of Lower Canada* in light of English authorities and common law concepts.<sup>155</sup>

With the development of official bilingualism and biculturalism at the federal level in the 1960s and 1970s, these unijural approaches to legislative drafting and judicial decision-making became increasingly anachronistic and unacceptable. In 1975, the Supreme Court of Canada explicitly recognized the *Civil Code of Lower Canada* as “radically different” from the common law, and acknowledged that its provisions “must be interpreted in keeping with the whole of which it is a part.”<sup>156</sup> Over the next few years, the Court established the basis for a complementary relationship between federal legislation and provincial private law through a series of decisions interpreting the words “Laws of Canada” for the purpose of section 101 of the *Constitution Act, 1867* to require a federal statutory text.<sup>157</sup> In 1978 the federal

<sup>150</sup> *An Act for making more effectual Provision for the Government of the Province of Quebec in North America*, (U.K.) 14 Geo. III, c. 83.

<sup>151</sup> (U.K.), 30 & 31 Vict., c. 3, reprinted in R.S.C. 1985, App. II, No. 6.

<sup>152</sup> *Ibid.*, s. 92(13).

<sup>153</sup> On bijuralism in decisions of the Supreme Court of Canada, see France Allard, “The Supreme Court of Canada and its Impact on the Expression of Bijuralism” in *Harmonization*, *supra* note 13, fasc. 3 [France Allard, “The Expression of Bijuralism”]; Louise Lavallée, “Bijuralism in the Supreme Court of Canada since the Enactment of the *Civil Code of Quebec*” in *Harmonization*, *supra* note 13, fasc. 3. For a notable judicial expression of bijuralism, see *St-Hilaire v. Canada (A.G.)*, 2001 FCA 63, 4 F.C. 289, 204 D.L.R. (4th) 103, Déary J.A., dissenting in part [*St-Hilaire*].

<sup>154</sup> Lionel A. Levert, “The Cohabitation of Bilingualism and Bijuralism in Federal Legislation in Canada: Myth or Reality?” in *Harmonization*, *ibid.*, fasc. 1, 5 at 6.

<sup>155</sup> See France Allard, “The Expression of Bijuralism”, *supra* note 153 at 3-12.

<sup>156</sup> *Pantel v. Air Canada*, [1975] 1 S.C.R. 472 at 478, 48 D.L.R. (3d) 1.

<sup>157</sup> See *Quebec North Shore Paper v. Canadian Pacific Ltd.* (1976), [1977] 2 S.C.R. 1054, 71 D.L.R. (3d) 111; *Canada v. McNamara Construction (Western) Ltd.*, [1977] 2 S.C.R. 654, 75 D.L.R. (3d) 273; *Canada v. Thomas Fuller Construction (1958) Ltd.* (1979), [1980] 1 S.C.R. 695, 106 D.L.R. (3d) 193. For a useful discussion of these cases, see France Allard, “The Expression of Bijuralism”, *supra* note 153 at 22-26.

Department of Justice introduced a new method of drafting legislation, called “codrafting”, whereby all bills drafted by the Legislative Services Branch are prepared by two drafters—a francophone who is typically trained in the civil law, and an anglophone who is typically trained in the common law.<sup>158</sup>

Although bijural, this method of codrafting did not directly speak to francophone common law lawyers or anglophone civil law lawyers. Moreover, the new approach did not make bijuralism an explicit objective of the codrafting process. In June 1995, therefore, the Department of Justice adopted an explicit policy on legislative bijuralism, intended to “provid[e] Canadians with federal legislative texts that will reflect, in each linguistic version, the legal system in use in their province.”<sup>159</sup> In general, this policy is designed to promote equal access to justice by different legal and linguistic communities in Canada, equal recognition of the civil and common law traditions in federal legislation, and a harmonious relationship between federal legislative objectives and these legal traditions.<sup>160</sup> Moreover, given the historical dominance of common law concepts and principles in federal legislation, an important objective of this policy was also to ensure that federal legislation does not “treat Quebec Civil law as an inferior or subsidiary component of the Canadian legal tradition.”<sup>161</sup>

Three years after the adoption of this policy, the federal government introduced Bill C-50,<sup>162</sup> containing amendments to various federal statutes relating to provincial private law,<sup>163</sup> as well as to the federal *Interpretation Act*. Although Bill C-50 died on the Order Paper when the House of Commons was prorogued, and a subsequent version, Bill S-22,<sup>164</sup> died when Parliament dissolved in the autumn of 2000, it was

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<sup>158</sup> Levert, *supra* note 154 at 6.

<sup>159</sup> Department of Justice, *Policy on Legislative Bijuralism*, reproduced in Wellington, *supra* note 13 at 22, app. 3.

<sup>160</sup> See Marie-Claude Gervais, “Program to Harmonize Federal Legislation with the Civil Law of the Province of Quebec, Assumption of Complementarity and Methodological Issues” in *Harmonization*, *supra* note 13, fasc. 1, 10 at 11-12.

<sup>161</sup> Roderick A. Macdonald, “Harmonizing the Concepts and Vocabulary of Federal and Provincial Law: The Unique Situation of Quebec Civil Law” in *The Harmonization of Federal Legislation with Quebec Civil Law and Canadian Bijuralism: Collection of Studies* (Ottawa: Department of Justice Canada, 1999) [*Collection of Studies*] 27 at 69. See also Levert, *supra* note 154 (emphasizing Parliament’s “moral duty to take the two systems of law into account in its legislation ... when it sets out standards the application of which intersects with provincial private law” at 5).

<sup>162</sup> *A First Act to harmonize federal law with the civil law of the Province of Quebec and to amend certain Acts in order to ensure that each language version takes into account the common law and the civil law*, 1st Sess., 36th Parl., 1998 (tabled in the House of Commons 12 June 1998).

<sup>163</sup> See e.g. *Federal Real Property and Federal Immovables Act*, S.C. 1991, c. 50; *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3; *Crown Liability and Proceedings Act*, R.S.C. 1985, c. C-50.

<sup>164</sup> *A First Act to harmonize federal law with the civil law of the Province of Quebec and to amend certain Acts in order to ensure that each language version takes into account the common law and the civil law*, 2nd Sess., 36th Parl., 2000.

re-tabled at the opening of the subsequent Parliamentary session as Bill S-4,<sup>165</sup> and enacted into law as the *Federal Law—Civil Law Harmonization Act, No. 1*.<sup>166</sup> The preamble to this legislation repeats the basic goals of the Department of Justice’s *Policy on Legislative Bijuralism*, and affirms a principle of “complementarity” between federal legislation and provincial private law. According to this principle, the private law of the relevant province in which a federal statute is applied is, unless otherwise provided by law, recognized as the body of law that “completes federal legislation” if it is otherwise incomplete. More importantly, the legislation also codifies this principle of complementarity in section 8.1 of the federal *Interpretation Act*.<sup>167</sup>

As explained earlier, this provision declares that “[b]oth the common law and the civil law are equally authoritative and recognized sources of the law of property and civil rights in Canada.” It further stipulates that “unless otherwise provided by law, if in interpreting an enactment it is necessary to refer to a province’s rules, principles or concepts forming part of the law of property and civil rights, reference must be made to the rules, principles or concepts in force in the province at the time the enactment is being applied.” As a result, section 8.1 recognizes the equal status of common law and civil law as “sources of the law of property and civil rights in Canada,” mandates complementarity as the proper way to interpret federal legislation relating to provincial private law, and establishes an ambulatory principle according to which the relevant provincial source of reference is the private law “in force in the province at the time the enactment is being applied.” Crucially, however, the complementarity principle applies only if the two conditions set out in section 8.1 are met. Each of these conditions is itself a matter of statutory interpretation, which should presumably be guided by the broad aims and principles underlying Canadian bijuralism, particularly those expressed in the preamble to the *Federal Law—Civil Law Harmonization Act, No. 1*.

The first condition—that it must be “necessary” to refer to provincial sources of law concerning property and civil rights to interpret the enactment—seems to be satisfied where the legislation in question (1) employs a term that is not defined in federal legislation but has an established private law meaning, (2) relies on private law rules, principles, or concepts in order to define the legal relationships to which it

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<sup>165</sup> *A First Act to harmonize federal law with the civil law of the Province of Quebec and to amend certain Acts in order to ensure that each language version takes into account the common law and the civil law*, 1st Sess., 37th Parl., 2001.

<sup>166</sup> *Supra* note 152.

<sup>167</sup> 9041-6868 *Québec v. M.N.R.*, 2005 FCA 334, 350 N.R. 201, Décary J.A. (s. 8.1 “codified the principle that the private law of a province and a federal statute are complementary, which had been recognized [in *St-Hilaire* (*supra* note 153)] but had not always been put into practice.” The “immediate effect” of the provision was “to restore the role of the civil law in matters under the jurisdiction of this Court, to bring to light how the common law might have been borrowed from, over the years, in cases where Quebec civil law applied or should have applied, and to caution us against any such borrowing in the future” at para. 5).

applies, or (3) is silent on a matter that is governed by a specific provincial rule forming part of the law of property and civil rights. In these cases, since the enactment cannot be applied without relying on the private law rules, principles, or concepts that complete the federal legislation, it follows that these same rules, principles, or concepts are essential to the interpretation of the enactment.<sup>168</sup> Moreover, since the *Constitution Act, 1867* provides that provincial governments have exclusive authority to make laws in relation to property and civil rights,<sup>169</sup> the interpretation of the legislation must, unless it is otherwise provided by law, refer to *provincial* sources of law. Conversely, it is not necessary to refer to provincial private law to interpret concepts that are fully defined in federal legislation, statutory provisions that do not depend on “rules, principles or concepts forming part of the law of property or civil rights,” and legislation that explicitly precludes reliance on provincial private law.<sup>170</sup>

The second condition—which precludes what would otherwise be a necessary reference to provincial private law to interpret a federal enactment where it is “otherwise provided by law”—is clearly satisfied where the federal enactment explicitly dissociates the interpretation of a concept or provision from provincial private law.<sup>171</sup> More difficult, however, are circumstances in which dissociation from provincial private law is implicit in the language or purposes of the statutory text. Where federal legislation relies on common law terms, for example, a necessary implication may be raised that its interpretation must be based on common law principles and dissociated from the civil law of Quebec.<sup>172</sup> As well, with much federal legislation, it is a reasonable presumption that Parliament intends its laws to apply uniformly throughout Canada,<sup>173</sup> and this is particularly so in the field of taxation where equity and anti-avoidance considerations can weigh heavily.<sup>174</sup> As a result, it

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<sup>168</sup> For a concurring interpretation, see Henry L. Molot, “Clause 8 of Bill S-4: Amending the *Interpretation Act*” in *Harmonization*, *supra* note 13, fasc. 6, 1 at 16.

<sup>169</sup> *Supra* note 151, s. 92(13).

<sup>170</sup> Molot, *supra* note 168:

For example, [federal] legislation could so comprehensively define its terms as to implicitly exclude any reference to provincial private law as the external source of interpretation and application. Federal legislation could also expressly refer to some other external source of interpretation thereby demonstrating a contrary intent as regards it being “necessary to refer to a province’s rules ...” (at 18).

<sup>171</sup> See *ibid.* (suggesting that the expression “unless otherwise provided by law” is triggered only by an express “legislative provision to the contrary” at 19).

<sup>172</sup> See e.g. Jean-Maurice Brisson & André Morel, “Federal Law and Civil Law: Complementarity, Dissociation” in *Collection of Studies*, *supra* note 161, 217 at 235. See also André Morel, “Harmonizing Federal Legislation with the *Civil Code of Québec*: Why and Wherefore?” in *Collection of Studies*, *supra* note 161, 1 (explaining that this “helps create the impression that there is a sort of organic bond, an association inherent in the nature of things, between federal law and common law—and the language used in those statutes tends to reinforce that impression” at 6).

<sup>173</sup> See e.g. Brisson & Morel, *ibid.*; Bastarache, *supra* note 149 at 21.

<sup>174</sup> See e.g. Brisson & Morel, *ibid.* at 237; Morel, *supra* note 172 at 7.

might be argued, undefined private law concepts in federal legislation should be given their common law meanings in order to ensure conceptual coherence and uniformity throughout Canada.

Although the principle of Parliamentary supremacy dictates that courts should dissociate the interpretation of federal legislation from the private law of one or more provinces where Parliament's intention is clear, the goals of Canadian bijuralism suggest that this should be done only when this intention is stated explicitly or necessarily implied by the language of the statutory text.<sup>175</sup> As Professor Macdonald explains, "forcing Parliament itself to make its choices explicitly is the best guarantee that the distinctive civil law and common law traditions in Canada will be respected in any legislative reordering."<sup>176</sup> Nor should previous judicial decisions be regarded as "law" within the meaning of the exclusion in section 8.1 of the federal *Interpretation Act*, since this approach would render the provision largely meaningless.

### **B. Section 8.1 of the Federal Interpretation Act and the Concept of an Acquisition of Property in the Income Tax Act**

Returning to the concept of an acquisition of property in the *ITA*, the judicial decisions examined in the first part of this paper provide a number of arguments that are relevant to the two conditions in section 8.1 of the federal *Interpretation Act*. The following sections consider each of these conditions.

#### 1. The Need to Refer to Private Law

Beginning with the first of these conditions, the strongest arguments against any need to refer to private law rules, principles, or concepts in order to interpret the meaning of an acquisition of property for tax purposes are: (1) that this concept can be understood according to the ordinary meaning of these words; and (2) that the concept can be interpreted, as Justice Lamarre Proulx suggested in *Terexcavation*, "on the basis of the tax legislation" without resorting to private law.<sup>177</sup> To the extent that the concept of an acquisition of property has an ordinary meaning that does not depend on private law rules, principles, or concepts, it follows that it is not necessary

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<sup>175</sup> See e.g. Roderick A. Macdonald, "Provincial Law and Federal Commercial Law: Is '*Atomic Slipper*' a New Beginning?", Case Note, (1991-1992) 7 B.F.L.R. 437 [Macdonald, "A New Beginning?"] (provincial law in respect of property and civil rights should be displaced by federal law only "explicitly or by *absolutely necessary implication*" at 447 [emphasis in original]). See also *Markevich v. Canada*, 2001 FCA 144, [2001] 3 F.C. 449, 199 D.L.R. (4th) 225, aff'd 2003 SCC 9, [2003] 1 S.C.R. 94, 223 D.L.R. (4th) 17 (while the *ITA* "may exclude application of general legal principles, rules and remedies," this must be accomplished by "express language or necessary implication to that effect" at para. 25).

<sup>176</sup> Macdonald, "A New Beginning?", *ibid.* at 450.

<sup>177</sup> *Supra* note 7 at para. 35.



to refer to private law in order to interpret its meaning. Likewise, it is not necessary to refer to private law rules, principles, and concepts to interpret the meaning of an acquisition of property if the concept has an autonomous tax meaning that is inherently dissociated from these sources. Although the first of these arguments can, where applicable, provide a persuasive reason for ignoring provincial rules, principles, and concepts that might otherwise influence the interpretation of federal legislation,<sup>178</sup> it is not clear that it applies to the concept of an acquisition of property. On the contrary, as Justice Noël observed in his dissenting opinion in *Bérou*, in the context of a provision referring to the acquisition of property, the ordinary meaning of the word “acquired” means “the acquisition of *ownership* of property.”<sup>179</sup> *The Oxford English Dictionary*, for example, defines the word acquire as “[t]o gain, obtain, or get as one’s own, to gain the *ownership* of,”<sup>180</sup> while *Le Petit Robert* defines the word acquire as “[b]ecome *owner* of (property, right) by purchase, exchange or succession,” and *Le Dictionnaire du droit privé* defines the word acquisition as “[a]ct by individual of becoming *owner* of thing or holder of right.”<sup>181</sup> As a result, as Justice Noël explains in his dissenting opinion in *Bérou*, “in the absence of some indication to the contrary, ownership of property cannot be acquired otherwise than in accordance with the applicable private law.”<sup>182</sup>

For this reason as well, the second argument—that the concept of an acquisition of property can be interpreted “on the basis of the tax legislation”—should also be rejected. On the contrary, as the Supreme Court of Canada has held on several occasions, where the *ITA* employs a word or expression with an established private or commercial law meaning, the word or expression should be construed in accordance with this private or commercial law meaning in the absence of “express direction” that another interpretation is warranted.<sup>183</sup> In this circumstance, moreover, section 8.1 of the federal *Interpretation Act* stipulates that “reference must be made to the rules, principles or concepts in force in the province at the time the enactment is being applied.” Therefore, absent express direction to the contrary, the concept of an acquisition of property should be interpreted in accordance with the civil law in the Province of Quebec and the common law in the other provinces.

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<sup>178</sup> For example, for tax purposes, Canadian courts have interpreted the concept of “residence” according to its ordinary meaning without reference to private law. See *Thomson v. M.N.R.*, [1946] S.C.R. 209, 1 D.L.R. 689. For a brief discussion of this case in the context of Canadian bijuralism, see Duff, *supra* note 13 at 33-37.

<sup>179</sup> *Supra* note 7 at 221 [emphasis added].

<sup>180</sup> *The Oxford English Dictionary*, 2d ed., s.v. “acquire” [emphasis added].

<sup>181</sup> Cited in *Bérou*, *supra* note 7 at n. 34 [emphasis added, translated in *Bérou*].

<sup>182</sup> *Supra* note 7 at 221.

<sup>183</sup> *Will-Kare Paving & Contracting Ltd. v. Canada*, 2000 SCC 36, [2000] 1 S.C.R. 915 at para. 30, 188 D.L.R. (4th) 242, Major J. See also *Continental Bank Leasing Corp. v. Canada*, [1998] 2 S.C.R. 298, 163 D.L.R. (4th) 385.

## 2. Whether Otherwise Provided by Law

Turning to the second inquiry under section 8.1, the majority reasoning in *Bérou* suggests three arguments as to why a reference to the civil law of Quebec to interpret the concept of an acquisition of property might be “otherwise provided by law”: First, as Justice Létourneau declared, subsection 248(3) reflects a legislative intent “to harmonize” the civil law and the common law in order to provide “fair and equal treatment to all Canadian taxpayers,” as a consequence of which, courts must interpret the concept of an acquisition of property in accordance with this legislative intent.<sup>184</sup> Second, as Justices Desjardins and Létourneau both argued, because the concept of an acquisition is the counterpart of a disposition, and because the effect of the statutory definition of a disposition is to incorporate into the *ITA* the common law rule that there is a disposition of property whenever there is a transfer of beneficial ownership even though legal ownership remains unchanged, it follows that there is an acquisition of property whenever a party to an agreement obtains beneficial ownership even though the other party retains legal ownership.<sup>185</sup> Finally, as Justice Létourneau also argued, the judicial test in *Wardean Drilling* and the Canada Revenue Agency’s subsequent Interpretation Bulletin had endured for many years without legislative amendment, suggesting that they were consistent with the legislative intent expressed in subsection 248(3).<sup>186</sup> As with the arguments against any need to refer to private law rules, principles, or concepts in order to interpret the meaning of an acquisition of property for tax purposes, none of these arguments is persuasive in light of section 8.1 of the *Interpretation Act* and the goals of Canadian bijuralism.

Regarding what is now paragraph 248(3)(e), Justice Létourneau is correct to suggest that it reflects a legislative intent to harmonize various civil law and common law concepts for tax purposes. In order to accomplish this harmonization, however, the provision does not disregard the civil law altogether, but instead deems various civil law relationships to be trusts, beneficial interests, and beneficial ownership for the purposes of the application of the *ITA* in Quebec.<sup>187</sup> Most importantly, paragraph 248(3)(e) does not, for these purposes, deem property in relation to which a person has possession, use, and risk to be beneficially owned by that person, limiting this status to a situation where a person “has in relation to the property (i) the right of ownership, (ii) a right as a lessee under an emphyteusis, or (iii) a right as a beneficiary in a trust.”<sup>188</sup> Thus, while the provision assimilates various civil law relationships to the common law concept of beneficial ownership, it does not import the common law concept of beneficial ownership into the application of the *ITA* in

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<sup>184</sup> *Supra* note 7 at 186.

<sup>185</sup> *Ibid.* at 183, Desjardins J., 188, Létourneau J.

<sup>186</sup> *Ibid.* at 189.

<sup>187</sup> *Supra* note 1. This version, which differs from the version that was discussed in *Bérou*, applies to property the ownership of which was acquired after 1990.

<sup>188</sup> *Ibid.*

relation to the Province of Quebec. To conclude that legislative intent requires that the concept of beneficial ownership be harmonized in this manner therefore misconstrues the purpose and effect of subparagraph 248(3)(e)(i) and ignores the explicit legislative intent in section 8.1 of the *Interpretation Act* to respect both the common law and the civil law as “equally authoritative and recognized sources of the law of property and civil rights in Canada.”

The second argument—that the statutory definition of a disposition dictates that property is acquired for tax purposes when a taxpayer obtains beneficial ownership even though another person retains legal ownership—depends on two propositions: (1) that the concept of an acquisition is the counterpart of a disposition, and (2) that the effect of the statutory definition of a disposition is to incorporate into the *ITA* the common law rule that there is a disposition of property whenever there is a transfer of beneficial ownership even though legal ownership remains unchanged. While the first of these propositions reflects a plausible reading of the scheme of the *ITA*, it is not set out in any statutory provision, but rather depends entirely on judicial interpretation.<sup>189</sup> As such, it is not clear that such judicial interpretation should override the legislative intent expressed in section 8.1 of the *Interpretation Act* that courts should refer to the private law of the relevant province to complete federal legislation that employs undefined terms with established private law meanings. The second of these propositions is also doubtful, although apparently admitted by the parties in *Bérou*.<sup>190</sup> A provision that deems a disposition *not to include* a transfer of legal ownership without a change in beneficial ownership does not logically entail that a disposition *includes* a transfer of beneficial ownership without a transfer of legal ownership.<sup>191</sup> Subsequent amendments to the statutory definition of a disposition make this proposition even more doubtful by removing the reference to the common law concept of “legal ownership” that has no counterpart in the civil law.<sup>192</sup> As a result, although it seems reasonable to conclude (as Justice Addy did in *Olympia and York*)<sup>193</sup> that the statutory definition of a disposition is dissociated from provincial private law by specifically including “any transaction or event entitling a taxpayer to proceeds of disposition of the property,”<sup>194</sup> it does not clearly follow that a disposition includes a transaction in which there is a transfer of beneficial ownership without a transfer of legal ownership—particularly in Quebec, where these common law concepts have no meaning absent a deeming provision in the *ITA*. On the contrary, since paragraph 248(3)(e) deems property in respect of which a person has “*the right of ownership*”<sup>195</sup> to be beneficially owned by the person, this provision suggests that a transfer of

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<sup>189</sup> See e.g. *Olympia and York*, *supra* note 55.

<sup>190</sup> *Supra* note 8 at 183, Desjardins J.A., 223, Noël J.A.

<sup>191</sup> See Marie-Pierre Allard, “Conditional Obligations”, *supra* note 74 at 1796; Duff, *supra* note 13 at 57-58.

<sup>192</sup> *ITA*, *supra* note 1, ss. 248(1), s.v. “disposition” (e)-(f).

<sup>193</sup> *Supra* note 54.

<sup>194</sup> See *ITA*, *supra* note 1, s. 248(1), s.v. “disposition” (a).

<sup>195</sup> [Emphasis added].

possession, use, and risk in Quebec would not constitute a transfer of beneficial ownership under the *ITA* so long as the transferor retains “the right of ownership” in civil law.

The last of these arguments—that Parliament effectively endorsed Justice Cattanach’s twofold test in *Wardean Drilling* by allowing it and the Canada Revenue Agency’s subsequent Interpretation Bulletin to stand absent legislative reversal—is also unconvincing. Although Parliament’s inaction on the matter may signify legislative approval in one respect, it is important to note that it was not until the Federal Court of Appeal’s 1999 decision in *Bérou* that the twofold test in *Wardean Drilling* was conclusively applied within the Province of Quebec. More importantly, whatever legislative intent might be read into the absence of a statutory amendment is now subject to the express intent in section 8.1 of the federal *Interpretation Act* that “[b]oth the common law and the civil law are equally authoritative and recognized sources of the law of property and civil rights in Canada” and that “reference must be made to the rules, principles or concepts in force in the province at the time the enactment is being applied” whenever it is necessary in order to interpret a federal enactment. For this reason, it is difficult to conclude that legislative failure to assign a specific meaning to the acquisition of property implies legislative endorsement of a harmonized concept based on the twofold test in *Wardean Drilling*. On the contrary, as argued earlier, the goals of Canadian bijuralism suggest that courts should dissociate the interpretation of federal legislation from provincial private law only where a legislative intention to this effect is explicitly indicated or necessarily implied by the words of the statutory text.<sup>196</sup>

### 3. Conclusion

If it is both necessary to refer to “rules, principles or concepts forming part of the law of property and civil rights” in order to interpret the meaning of an acquisition of property and not “otherwise provided by law,” section 8.1 of the federal *Interpretation Act* provides that reference must be made to “the rules, principles or concepts in force in the province at the time [that the relevant provision] is being applied.” As explained in the second part of this paper, these rules, principles, and concepts are governed by the common law and provincial statutes like the *Sale of Goods Act* in the common law provinces, and by the C.C.Q. and other civilian authorities in the Province of Quebec. To the extent that the twofold test in *Wardean Drilling* reflects the common law distinction between legal and beneficial ownership, therefore, section 8.1 suggests that it should no longer apply within Quebec, thereby reversing the Federal Court of Appeal decision in *Bérou*. For the same reason, one might also question the Federal Court of Appeal decision in *Kowdrysh*, which ignored the rules, principles, and concepts governing the ownership and transfer of property in common law jurisdictions in order to conclude that the taxpayer had acquired

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<sup>196</sup> *Supra* notes 175-76 and accompanying text.

property for the purposes of a temporary investment tax credit when he entered into a binding and enforceable contract. Although this interpretation may have been justified on tax policy grounds,<sup>197</sup> dictionary definitions of the words “acquire” and “acquisition”, and section 8.1 of the federal *Interpretation Act*, suggest that the concept of an acquisition of property should, absent an express direction or necessary implication to the contrary, be governed by the common law test in *Wardean Drilling*.

#### IV. Codifying the Concept of an Acquisition of Property in the *Income Tax Act*

If section 8.1 of the federal *Interpretation Act* requires courts to interpret the concept of an acquisition of property in the *ITA* in accordance with the provincial private law to which the transaction is subject, differences between civil law and common law rules, principles, and concepts governing the ownership and transfer of property may produce different tax consequences depending on whether the transaction is subject to the civil law of Quebec or the common law of the other provinces. Where property is sold by means of a conditional sale or lease-option agreement, for example, the C.C.Q. suggests that the purchaser does not acquire the property until the condition is satisfied or the option is exercised because ownership remains with the vendor or lessor until that time,<sup>198</sup> while the common law suggests that the purchaser acquires the property as soon as possession, use, and risk are transferred, since this results in a transfer of beneficial ownership.<sup>199</sup>

Although these different outcomes may be compatible with the goal of Canadian bijuralism to recognize the civil law and the common law as “equally authoritative ... sources of the law of property and civil rights in Canada,” they contradict an important principle of Canadian income tax law—that the *ITA* should apply equally and uniformly throughout the country. Moreover, since the impact of section 8.1 on the interpretation of the *ITA* will ultimately depend on judicial decisions, the meaning of an acquisition of property for tax purposes may be subject to significant uncertainty for a considerable period of time—particularly in Quebec, where cases prior to the Federal Court of Appeal decision in *Bérou* took widely different views on the implications of lease-option agreements on the acquisition of property for tax purposes. For both of these reasons, it would be advisable to amend the *ITA* by enacting a statutory definition of an “acquisition of property” to ensure uniformity

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<sup>197</sup> The court explained that to require taxpayers to acquire beneficial ownership of the property in order to deduct the temporary investment tax credit would provide an unintended windfall to taxpayers who purchased farming equipment “before the program was even conceived and put into effect” and were “fortunate enough to have the equipment delivered after 2 December 1992 up to 31 December 1993,” while disqualifying taxpayers who the credit induced to purchase farming equipment after the program came into force but who did not receive the equipment until after 31 December 1993 (*Kowdrysh*, *supra* note 45 at para. 8).

<sup>198</sup> See the discussion in Part II.B, above.

<sup>199</sup> See the discussion in Part II.A, above.

and certainty in the application of *ITA* provisions that rely on this concept to determine the tax consequences of different transactions.

In order to devise such a definition, at least three issues must be addressed: As a preliminary matter, one must decide whether a single definition should apply throughout the *ITA* or whether different definitions should apply to specific provisions in which the concept is employed. However this preliminary question is addressed, a second issue concerns the language and content of the statutory definition or definitions, which should presumably accord both with the scheme of the *ITA* and with the goal of Canadian bijuralism to recognize the equal status of the common law and the civil law as “sources of the law of property and civil rights in Canada.” A final issue concerns the potential implications of this definition or definitions for related provisions such as the statutory definition of a disposition in subsection 248(1) and the interpretive rule for civil law relationships in subsection 248(3), or for other provisions such as the “available for use” rules for depreciable property,<sup>200</sup> the specified leasing property rules in the *Income Tax Regulations*,<sup>201</sup> the election for leasing properties,<sup>202</sup> or the rules in sections 79 and 79.1 governing the acquisition or reacquisition of property by a creditor as a consequence of a debtor’s failure to pay a debt.

Beginning with the first of these issues, it is certainly reasonable to suggest that a single definition of an acquisition of property for the purposes of the *ITA* as a whole might be inappropriate. Since the concept of an acquisition of property appears in

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<sup>200</sup> *ITA*, *supra* note 1, ss. 13(26)-(31). Under these rules, the capital cost of a property acquired by a taxpayer may not be added in computing the taxpayer’s undepreciated capital cost of property of the class until “the time the property is considered to have become available for use by the taxpayer.”

<sup>201</sup> C.R.C., c. 945, ss. 1100(1.1)-(1.3) [*Regulations*]. In general, these rules limit the amount that a taxpayer may deduct as capital cost allowance in respect of property that is used principally to earn rent or leasing revenue to an amount equal to the notional repayment of principal on a notional loan to the lessee of an amount equal to the purchase price of the property. As explained in the Supplementary Information accompanying the 1989 Federal Budget, the purpose of the rules is to reduce the tax advantages that would otherwise be available to tax-exempt or non-taxable taxpayers by leasing property with accelerated capital cost allowance rates from taxpaying lessors to whom they can effectively trade the capital cost allowance deductions in exchange for reduced rental payments. Although the economic effect of these rules from the lessor’s perspective is to treat a lease as a loan, the rules depend on the prior characterization of the transaction as a lease and do not actually recharacterize lease transactions as loans.

<sup>202</sup> *Ibid.*, s. 16.1. This provision complements the specified leasing property rules in ss. 1100(1.1)-(1.3) of the *Regulations*. It allows lessees to deduct capital cost allowance and notional interest in respect of leased property where they file a joint election with the lessor of the property. Unlike the specified leasing property rules, this provision deems the lease not to be a lease, the lessee to have acquired the property at a cost equal to its fair market value, the lessee to have borrowed an amount from the lessor equal to this fair market value for the purpose of acquiring the property, interest to accrue on this loan at a prescribed amount, and lease payments paid by the lessee to be blended payments of interest and principal on account of the loan. Like the specified leasing property rules, however, this provision also depends on the initial characterization of the transaction as a lease.

numerous *ITA* provisions with different tax implications, one might reasonably expect that the purpose of each provision in which the concept is used would be better served by a specific definition applicable to the provision itself rather than a general definition that applies for the purposes of the *ITA* as a whole. In *Kowdrysh*, for example, the Federal Court of Appeal held that the taxpayer had acquired property when it entered into a binding and enforceable contract, on the basis that this meaning of an acquisition of property was more suitable to the temporary investment tax credit at issue in the case than the judicial test in *Wardean Drilling*.<sup>203</sup> For the purposes of the capital cost allowance regime, on the other hand, a meaning akin to the second branch of the twofold test in *Wardean Drilling* might be more appropriate.<sup>204</sup>

Notwithstanding this argument for multiple statutory definitions of an acquisition of property, there are three reasons why a single definition for the *ITA* as a whole should be preferred: First, since the words “property acquired” appear in a consistent form in the various provisions in which the concept is used, established principles of statutory interpretation suggest that it should be given the same meaning on the basis that Parliament is presumed to have intended this result.<sup>205</sup> Second, to the extent that the concept of an acquisition is properly regarded as the counterpart to a disposition, the existence of a statute-wide definition of the latter in subsection 248(1) suggests that a statutory definition of an acquisition of property should also apply for the purposes of the *ITA* as a whole. Finally, as a practical matter, the urgency of enacting a statutory definition to prevent inequality and uncertainty in the application of the *ITA* favours the rapid enactment of a general definition, to which modifications could subsequently be made as necessary for the purpose of specific provisions.

Turning to the language and content of the definition, two considerations seem paramount. First, in order to prevent significant disruption to existing transactions and commercial practices, a statutory definition of an acquisition of property should conform as closely as possible to established judicial interpretations of the concept. Second, in order to recognize the equal status of the common law and the civil law as “sources of the law of property and civil rights in Canada,” the definition should be drafted in a manner that does not subsume one legal system to the other or disregard one of the two legal systems altogether by employing the rules, principles, or concepts of one legal system exclusively. While the first of these considerations

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<sup>203</sup> *Supra* notes 45-67 and accompanying text. See the discussion in Part III.B.3, above.

<sup>204</sup> To the extent that the subsequent disposition of depreciable property results in recaptured depreciation or a terminal loss, it seems reasonable to conclude that these tax consequences should fall upon the taxpayer who has the possession and use of the property and bears the risk of its loss. An emphasis on possession, use and risk is also consistent with the available for use rules in ss. 13(26)-(31) of the *ITA* (*supra* note 1), which in many cases defer the time when a taxpayer may add the capital cost of the property to the taxpayer’s undepreciated capital cost of property of the class until the property is delivered to the taxpayer.

<sup>205</sup> See Elmer A. Driedger, *Construction of Statutes*, 2nd ed. (Toronto: Butterworths, 1983) at 93-94; Ruth Sullivan, *Sullivan and Driedger on the Construction of Statutes*, 4th ed. (Markham, Ont.: Butterworths, 2002) at 162-68.

might favour a definition based on of the twofold test in *Wardean Drilling*, the second rejects this definition to the extent that it reflects the common law distinction between legal and beneficial ownership. Nonetheless, since the C.C.Q. employs the concepts of possession, use, and risk,<sup>206</sup> it would be possible to draft a statutory definition that could encompass both legal systems by stipulating that property is acquired for tax purposes either when a taxpayer acquires ownership of the property or where the taxpayer obtains possession and use of the property, and assumes all the risks of loss of the property.

In common law provinces, a definition along these lines would have the same effects as the twofold test in *Wardean Drilling*, and would presumably apply to purchasers under conditional sales agreements and lessees under security or financing leases. In Quebec, a definition along these lines would capture ordinary sales agreements, instalment sales, conditional sales with either a suspensive or a resolutive condition, as well as contracts of leasing, thereby achieving similar results as the twofold test in *Wardean Drilling* without relying on the common law concepts on which this test is based.

With respect to the implications of such a definition for other statutory provisions, this paper cannot offer definitive conclusions, since it has not examined these provisions in detail. To the extent that the concept of an acquisition is understood as the counterpart of a disposition, however, it seems reasonable to expect that the statutory definition of a disposition should mirror the definition of an acquisition. Indeed, since the current definition of a disposition refers to the concept of beneficial ownership, an amendment that would replace this language with a reference to possession, use, and risk would also advance the goal of Canadian bijuralism to recognize the equal status of the civil law and the common law. For the same reason, reconsideration should also be given to subsection 248(3), which subsumes the civil law of Quebec to the common law of the other provinces by deeming various civil law relationships to be trusts, beneficial interests, and beneficial ownership for the purposes of the application of the *ITA* in relation to the Province of Quebec. As well, since sections 79 and 79.1 also rely on the concept of beneficial ownership, they too should be reconsidered in light of any statutory definition of an acquisition of property. In contrast to these provisions, however, it does not appear as though any consequential amendment would be required to the “available for use” rules in subsections 13(26) to (31), the specified leasing property rules in subsections 1100(1.1) to (1.3) of the *Regulations*, or the election in section 16.1, since these provisions do not use common law concepts and do not affect the meaning of an acquisition of property, but instead determine specific tax consequences for property that is already acquired within the meaning of the *ITA*.

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<sup>206</sup> *Supra* notes 110-13 and accompanying text.



## Conclusion

Since the concept of an acquisition of property plays an important role in the *ITA*, it is somewhat curious that it remains undefined. Although courts have generally interpreted this concept in accordance with the twofold test in *Wardean Drilling*, this test is premised on common law concepts and is incompatible with the goals of Canadian bijuralism expressed in the *Federal Law—Civil Law Harmonization Act, No. 1* and section 8.1 of the federal *Interpretation Act*. As argued in the third part of this paper, since it is both necessary to refer to “rules, principles or concepts forming part of the law of property and civil rights” in order to interpret the meaning of an acquisition of property and it is not “otherwise provided by law,” section 8.1 of the *Interpretation Act* requires that the meaning of an acquisition of property be interpreted in accordance with the civil law in the Province of Quebec and the common law in the other provinces. For this reason, the continuing validity of the Federal Court of Appeal decisions in *Bérou* and *Kowdrysh* is uncertain. As a result, moreover, transactions may be subject to different tax consequences depending on whether they are subject to the civil law of Quebec or the common law of the other provinces. While this result may be compatible with the goals of Canadian bijuralism, it contradicts a fundamental principle of Canadian income tax law—that the *ITA* should apply equally and uniformly throughout the country.

In order to promote uniformity and certainty in the application of *ITA* provisions that rely on the concept of an acquisition of property, this paper recommends that the *ITA* be amended by introducing a statutory definition of the concept. More specifically, it suggests, this definition should apply for the purposes of the *ITA* as a whole and should encompass both legal systems by stipulating that property is acquired for tax purposes either when a taxpayer acquires ownership of the property or where the taxpayer obtains possession and use of the property, and assumes all the risk of loss of the property. Finally, the introduction of a statutory definition along these lines should be accompanied by consequential amendments to the statutory definition of a disposition of property in subsection 248(1), to the interpretive rules for civil law relationships in subsection 248(3), and to the rules in sections 79 and 79.1 governing the acquisition or reacquisition of property by a creditor as a consequence of a debtor’s failure to pay a debt.

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