TAX FOR THE Owner-Manager

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Bresse Syndics Inc.: De Jure Versus De Facto Control

The recent case of *Bresse Syndics Inc. v. Canada* (2021 FCA 115) dealt with the issue of whether CO2 Solutions Technologies Inc. ("New CO2") was a CCPC in its 2009 taxation year. The case was decided prior to the 2017 amendment of the Act, which added subsection 256(5.11). This provision expanded the circumstances that can be considered in determining whether de facto control exists.

The facts are reasonably straightforward. In March 2004, CO2 Solutions Inc. became a public corporation ("Public CO2"). In 2005, a reorganization was carried out under which a trust governed by the laws of Quebec was created with a deed of trust. Public CO2 transferred its SR & ED activities to New CO2 (the appellant), and they entered into a research agreement.

As part of the reorganization, the trust became New CO2's sole shareholder, and it had the power to choose New CO2's directors. The deed of trust required the trustees to be sitting directors of Public CO2 and to accept the office of trustee in writing. With respect to its 2009 taxation year, the appellant claimed refundable tax credits related to its SR & ED expenses on the basis that it was a CCPC. The minister disallowed the credits, saying that New CO2 was not a CCPC because it was directly or indirectly controlled by Public CO2, a public corporation.

The TCC (2019 TCC 286) found that in determining whether Public CO2 had de jure control, the court was entitled to examine the deed of trust. Because that document provided that only members of Public CO2's board of directors could be trustees of the trust, the TCC concluded that this mechanism was sufficient to establish that Public CO2 exercised de jure control over New CO2. However, the case was not decided on this basis because the minister did not explicitly raise this argument but instead relied on the existence of de facto control.

The TCC also found that Public CO2 had de facto control on the basis that the deed of trust was a legally enforceable arrangement giving Public CO2 the "clear right and ability to . . . influence in a very direct way" its sole shareholder following the criteria developed by the jurisprudence.

The TCC concluded that appendix C of New CO2's certificate of incorporation—which provided that only Public CO2 or its subsidiaries, or a trust whose beneficiaries were Public CO2 or those subsidiaries, could own New CO2's capital stock—and the research agreement were also legally enforceable arrangements within the meaning of the case law. Therefore, the TCC concluded that these documents gave Public CO2 de facto control of New CO2.

On appeal, the FCA first noted that the TCC heard the case prior to the enactment of subsection 256(5.11) and that the governing law was the decision in *McGillivray Restaurant Ltd. v. Canada* (2016 FCA 99). *McGillivray* held that the influence required to ground a finding of de facto control must come from "legally binding or enforceable arrangements."

The FCA stated that on the basis of *Duha Printers (Western) Ltd. v. Canada* (1998 CanLII 827 (SCC)), a de jure control analysis must be limited to the internal (that is, constating) documents of the corporation, which prima facie excluded the deed of trust. The FCA also noted that *Duha Printers* held that it can be relevant to examine a deed of trust to see whether the deed restricted the trustees' ability to exercise their voting rights on shares held by the trust. However, the FCA declined to undertake this analysis of de jure control: it was of the view that the deed of trust gave Public CO2 de facto control of New CO2 under the test set out in *McGillivray*, which was sufficient to dispose of the appeal.

The FCA held that the deed of trust conferred "a legally enforceable right and ability to effect a change to the board of directors or its powers, or to exercise influence over the shareholder" who has that right or ability. The FCA reasoned that by electing Public CO2's board of directors, Public CO2's shareholders also elected the trust's trustees, because the trustees had to be directors of Public CO2. Consequently, Public CO2 had the ability to terminate a trustee either by removing that person as a director or by not renewing the term of a director. The FCA held that the fact that the directors of Public CO2 were not required to accept a trusteeship was immaterial. In the court's view, the requirement that the trustees be directors of Public CO2 gave Public CO2 the ability to change the appellant's board of directors or to influence in a very direct manner those who had the ability. The FCA concluded that Public CO2 had de facto control of New CO2 and dismissed the appeal. Given its finding regarding the deed of trust, the court decided that it did not need to consider the research agreement or appendix C of the certificate of incorporation.

Although this decision sheds little light on how the amended de facto control test in subsection 256(5.11) will apply in future, it is a valuable reminder of the complexities of applying the de jure control test and determining de facto control.

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