Dockets: 2007-2033(IT)G
2007-3490(IT)G

BETWEEN:

KNIGHTS OF COLUMBUS,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeals heard on January 14, 15, 16, 17 and 18, 2008,
at Toronto, Ontario,

By: The Honourable Justice Campbell J. Miller

Appearances:

Counsel for the Appellant:	William I. Innes, Chia-yi Chua and Brendan Bissell
Counsel for the Respondent:	Marie-Thérèse Boris and Justin Kutyan

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JUDGMENT

The appeals from assessments made under Parts I, I.3 and XII.3 of the *Income Tax Act* for the 2000 and 2002 taxation years are allowed, and the assessments are vacated in respect of the tax assessed, the penalties assessed and the interest assessed on the basis that the Knights of Columbus did not carry on business in Canada through a permanent establishment in those years.

Costs are awarded to the Appellant.

Signed at Ottawa, Canada, this 16th day of May 2008.

"Campbell J. Miller"

C. Miller J.

Citation: 2008TCC307
Date: 20080516
Dockets: 2007-2033(IT)G
2007-3490(IT)G

BETWEEN:

KNIGHTS OF COLUMBUS,

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REASONS FOR JUDGMENT

Miller J.

[1] The Knights of Columbus, a resident United States corporation, provides life insurance to its Canadian members. It relies upon Canadian agents to do so. The issue before me is whether the Knights of Columbus is liable for tax in Canada on business profits from its insurance business. This hinges on the application of the Convention between the United States of America and Canada with respect to Taxes on Income and Capital (the *Canada-U.S. Treaty*), specifically a determination of whether the Knights of Columbus has a permanent establishment in Canada as a result of either:

(1) carrying on its business through a fixed place of business in Canada (Article V(1) of the *Canada-U.S. Treaty*).

(2) using agents, other than independent agents acting in the ordinary course of their business, who habitually exercise in Canada authority to conclude contracts in the name of the Knights of Columbus (Article V(5) and (7) of the *Canada-U.S. Treaty*).

[2] Counsel for the Knights of Columbus stressed at the outset the complexity of the *Treaty* provisions, and consequently called three experts to explain them. With the greatest respect, my initial reaction to counsel equating the Organisation for

Economic Co-operation and Development Model Convention ("OECD Model Convention") to the special theory of relativity in its complexity was that it was just legal hyperbole, though having heard the experts, I have some greater appreciation of what counsel was getting at in his opening remarks.

Background

[3] The Knights of Columbus is a Roman Catholic fraternal organization established in New Haven, Connecticut in 1882. It came to Canada in 1897. The organization has four levels of councils: local, district, state (or province) and supreme. One purpose of the organization, through its insurance program, was to help widows and orphans of deceased members. This evolved into a formal insurance program.

[4] The Knights of Columbus in 2006 raised approximately 25% of its funds from its insurance activities. The Knights of Columbus is not subject to income tax on its insurance activities in the United States.

[5] The Knights of Columbus' insurance business is handled through agents. In Canada, there are approximately 220 Field Agents, 22 General Agents, one Field Director, and a Chief Agent. I will describe the role of each, and then describe the business activities that take place in the United States, notably the underwriting process.

Chief Agent

[6] The description of the duties and responsibilities of the Chief Agent came from Mr. Tom Brockett, the Deputy Chief Accountant for the Knights of Columbus in New Haven. The Chief Agent for the Knights of Columbus in Canada during the relevant period, Mr. Soden, passed away in 2001.

[7] The Office of the Superintendent of Financial Institutions ("OSFI") stipulates that organizations such as the Knights of Columbus must have a Chief Agent in Canada. It also requires that the Chief Agent keep certain records with respect to the Canadian insurance activity. It was Mr. Brockett who oversaw the preparation of the Canadian Annual Return, test of adequacy form and monthly and quarterly reports. Reports would be submitted to OSFI through the Chief Agent's office, and his signature would be required on such reports. Documents would be kept at the Chief Agent's office. So for example, if OSFI conducted a compliance review, it would have access in Canada to the records.

[8] Mr. Soden was a Chartered Accountant. He was paid an hourly fee for acting as Chief Agent. He would submit claims to the Knights of Columbus for his expenses. His office bore no indication of any connection to the Knights of Columbus, and no one from the Knights of Columbus had access to his office. Mr. Soden was not on the Board of the Knights of Columbus, nor on any management committee. He played no role in the sale of insurance and no role with any of the agents nor the insureds. He would have to attend OSFI examinations, but this would be with the Knights of Columbus' Chief Accountant or Mr. Brockett.

[9] The Chief Agent was a signatory on the Knights of Columbus' cash receipt bank account with the Bank of Montreal, but not on the disbursements account. Funds would move from the receipts to the disbursements account on the initiation of the Treasurer's Department in New Haven. Mr. Brockett explained that the Chief Agent's involvement with the banking arrangements was an OSFI requirement. OSFI also required a Canadian Trust to maintain investments in Canada to ensure the adequacy of the assets or the liabilities. The Knights of Columbus retained CIBC Mellon as its Canadian Trustee.

Field Director

[10] No arguments centered on the role of the Field Director, so I simply mention that the Field Director was a Knights of Columbus' employee, whose role was to serve as something of a mentor to the General Agents in Canada.

General Agents

[11] The description of the General Agents' work came from Mr. Brockett and a General Agent, Mr. Darrell Gall, who worked in Nova Scotia and Newfoundland and Labrador.

[12] The General Agent must be a member of the Knights of Columbus. He oversees eight to 10 Field Agents. The General Agent is not actively involved in making sales to members, though was not precluded from doing so. The General Agent makes his income from a commission override from the Field Agents in his jurisdiction at a rate determined by the Knights of Columbus. The Knights of Columbus also provides the following benefits to the General Agent: term insurance, pension plan, group medical plan, training in New Haven and certain incentives. The General Agent is responsible for recruiting, training, managing and motivating the Field Agents.

[13] The General Agent works primarily from home. The Knights of Columbus does not have access to the General Agent's premises. There are no signs to indicate the General Agent's house has any connection to the Knights of Columbus. The Knights of Columbus does not reimburse the General Agent for his expenses, although there is an expense allowance calculated as a percentage of sales commission. The General Agent does not account for any expenses in order to receive the expense allowance, which Mr. Gall indicated does not approximate expenses. He viewed it as an additional commission.

[14] The General Agent's responsibility to recruit is ongoing. Mr. Gall described his activities in this regard as asking his Field Agents to keep their eyes open, advertising in parish bulletins, attending the Knights of Columbus' meetings and communicating with local priests. Mr. Gall would meet several times with potential agents. If acceptable to him, the agent goes through a security check and is also screened by the Knights of Columbus in New Haven, though Mr. Gall indicated the Knights of Columbus never denied one of his applicants for an agency. Mr. Tom Smith, a Knights of Columbus' Executive Vice-President testified that the Knights of Columbus reviews approximately 350 applications each year from a General Agent for consideration of a Field Agent. Mr. Smith himself reviews the most difficult applications and approves all but ten or twelve. A contract is then signed by the Field Agent, the General Agent and someone from the Knights of Columbus' head office in New Haven.

[15] The General Agent determines the councils the Field Agent will serve. The new Field Agent will submit a budget to the General Agent who determines what funding the Field Agent will require, and makes a draw or advance request to the Knights of Columbus. The Field Agent is expected to repay this funding as he earns commissions. However, if the Field Agent does not earn enough and is terminated, the General Agent becomes liable for the debt that remains owing to the Knights of Columbus.

[16] The General Agent is primarily responsible for training the Field Agents. Indeed, Mr. Gall developed his own three-week program for his Field Agents. The Field Agent also receives training from the Knights of Columbus in New Haven. The General Agent is responsible for the cost of the Field Agent's accommodation, while the Knights of Columbus picks up the balance of the expenses. The Knights of Columbus also offers a training program called Pro Start which involves reading a manual and doing regular tests, which are marked by the General Agent.

[17] It is the General Agent who regularly supervises and monitors the Field Agent. He is familiar with how all his Field Agents are handling their operations, and the General Agent will follow up if he is not seeing sufficient applications from the Field Agents. A General Agent may provide incentive programs beyond what the Knights of Columbus may offer. Similarly, the General Agent may set requirements beyond the Knights of Columbus' expectations. Mr. Gall requires his General Agents to have a private space with a door, telephone, desk, fax and highspeed internet access.

[18] Mr. Gall considered his role similar to that of a franchisee. While he operates within the Knights of Columbus' guidelines he runs his business his way for himself but not by himself. He is required to provide monthly reports to a Vice-President at the Knights of Columbus.

Field Agents

[19] The Field Agents are the frontline workers. They are required to be Knights of Columbus' members and can only solicit applications for sales of the Knights of Columbus' insurance products, and then only from the Knights of Columbus' members. The Field Agent is paid on a commission basis as well as receiving the expense allowance as described earlier. The Field Agent can also get bonuses if certain quotas are met.

[20] The contract entered into by the Field Agent with the General Agent and with the Knights of Columbus stipulates in part:

> 3. The Field Agent is authorized to solicit and procure applications for insurance from members of councils assigned to him. The insurance may be on the life of the member, his spouse or his minor children; provided, however, that no member may apply for insurance on a son age 18 or older; even if the son is still a minor under applicable state or provincial law. The Field Agent is also authorized to collect initial premium payments for such insurance and to perform such other tasks as may be incumbent upon them as the Order's insurance sales representative.
>
> The Field Agent shall have no authority to bind the Order to issue any insurance policy. He shall also have no authority: to waive, modify or amend provisions of any insurance policy or rider issued by the Order; to extend the time for paying any premium; to bind the Order by making any promise, or by accepting any representation or information not contained in an application for insurance; or to collect or receive any premium or partial premium, other than the initial premium, unless specifically authorized to do so by the Order.

> **4. Nothing contained in this Agreement shall be construed to create the relationship of employer and employee between the Order and the Field Agent, between the Order and the General Agent, or between the General Agent and Field Agent. The Field Agent shall be free to exercise independent judgment as to the eligible persons from whom applications for insurance will be solicited, and as to the time and place of such solicitation. The Field Agent shall abide by rules and procedures established by the Order, but such rules and procedures shall not be construed as interfering with the freedom of action of the Field Agent as described in this Agreement.**

[21] Apart from the General Agent's expectations with respect to the Field Agents' home offices, there are no requirements regarding an office from the Knights of Columbus. The Knights of Columbus' representatives do not have access to the Field Agents' premises. The Field Agents' home offices are not marked with any Knights of Columbus' signage. The Field Agents who testified, Mr. Raymond Bechard and Mr. Mark John Lewans, both stated that they had a separate business phone line in their names, not in the name of the Knights of Columbus. They rarely met clients at their home offices. The offices were used mainly for administrative purposes. There was some indication that one Field Agent may have seen clients more often in the home office. The Field Agents conduct their business from their home office, their car and the homes of the Knights of Columbus' members whose business they are soliciting.

[22] As well as the commissions (basic, expense and quota-based), the Knights of Columbus provides the following to Field Agents:

> - some training, a rate book and kit for oral fluid tests, benefits such as pension, medical and term insurance, payment of their initial license and cards and letterhead, unless their production slips below quotas

[23] The Field Agent visits the Knights of Columbus' member at home to discuss the Knights of Columbus' insurance products and to conduct a needs analysis. This is intended to lead to a determination of the appropriate insurance coverage. The Field Agent is trained on the impact of certain medical conditions to assist in this determination. The Field Agent is equipped with a Knights of Columbus' rate book, from which he can determine the approximate premium for the suggested insurance. The Field Agent completes the application, has it signed and collects the initial premium. This package is then sent to New Haven. The Field Agent cannot change any terms of the insurance application. The Field Agent leaves the applicant with a receipt and the Temporary Insurance Agreement Certificate.

[24] The Temporary Insurance Agreement is part of the application: indeed, an application cannot be submitted without it. Its terms are contained on one page of the application which also includes the receipt. Some of the relevant terms are:

> **Payment of Temporary Insurance**
>
> The Temporary Insurance will be paid to the beneficiary named in the application, if any person who is to be covered by the insurance contract applied for dies while the Temporary Insurance is in force.
>
> **Amount of Temporary Insurance**
>
> This Agreement provides Temporary Insurance, for any person who is to be covered by the insurance contract applied for, in the amount applied for on that person or $100,000, whichever is less.
>
> **Commencement of Temporary Insurance**
>
> The Temporary Insurance will start on the later of these dates: (a) the date of the above receipt; (b) the date of completion of any medical or paramedical examinations required at time of application.
>
> **Duration of Temporary Insurance**
>
> Unless this Temporary Insurance ends sooner for one of the three reasons listed in the Termination of Temporary Insurance section below, it will end 90 days after it starts.
>
> **Termination of Temporary Insurance**
>
> 1. The Temporary Insurance will end when the Knights of Columbus issues the insurance contract as applied for.
>
> 2. The Temporary Insurance will end when the Knights of Columbus issues an insurance contract other than as applied for, and the contract is accepted by the contract owner.
>
> 3. The Temporary Insurance will end when the Knights of Columbus refunds the initial premium or restores the existing values used to pay the initial premium.

[25] The Temporary Insurance Agreement provides insurance to an applicant while the application is processed, having effect for 90 days or until the Knights of Columbus, through its underwriting process, either turns down the application or the insurance becomes permanent, if sooner. Mr. Smith testified that the Temporary Insurance Agreement is offered to be competitive in the industry. Mr. Brockett stated

that the Temporary Insurance Agreement plays a very small role in the Knights of Columbus' insurance business. The claims paid out under the Temporary Insurance Agreements are well below 1% of total claims. Premiums for the Temporary Insurance Agreements as a percentage of total premiums are even less, at a small fraction of 1%. Dr. Michael Conforti, the Knights of Columbus' Medical Director, indicated that the claims' process or payments under the Temporary Insurance Agreements are not factored into pricing the Knights of Columbus' insurance products.

Underwriting Process

[26] The underwriting process takes place entirely in the United States. The New Business Department in New Haven reviews each application, checks information from the Medical Information Bureau and considers existing medical information. The Medical Information Bureau is a clearing house of information about medical status and prior dealings with individuals' insurance. The application is then forwarded to the Underwriting Department for consideration.

[27] Dr. Conforti testified that it was he, along with the Chief of Underwriting who determined the medical criteria necessary to order certain medical requirements. He also relied on a Swiss Re manual to rate medical impairments. Dr. Conforti also plays a role in reviewing contestable claims.

[28] The Underwriting Department can approve an application, rate it substandard, postpone or decline an application. Approximately 90 to 92% of applications are approved, although as Dr. Conforti stated:

> Yet you have to understand the majority of that 90 to 92 percent are for age and amounts that require medical requirements, and even of those that are standard, very often – you could still be standard but still have medical history that requires further investigation by the underwriter.

Approximately 2% are postponed or declined. If the underwriter determines more information is required they can order an attending physician statement or additional tests. The Underwriting Department supplies the agents with questionnaires for the more common ailments. Results of any additional tests go directly to the Underwriting Department. If an applicant dies while the underwriting is ongoing, the underwriting process will continue and, if the application is approved, the Temporary Insurance Agreement will operate to provide coverage.

[29] Dr. Conforti explained that the rate book which the agent has with him to assist in making the appropriate assessment of the applicant goes into a variety of factors, both medical and non-medical, that would impact on risk, even to the point of identifying when the agent might refuse to take an application. The Agent is also equipped with sufficient information to determine if a medical exam is required.

Expert Evidence

[30] The Appellant called three expert witnesses: Brian Arnold, David Rosenbloom and Richard Vann: all three were eminently qualified to comment upon the interpretation of "permanent establishment" as used in the OECD Model Convention, the UN Model Convention and corresponding commentaries. Mr. Rosenbloom, a former Director of the Office of International Tax Affairs of the United States Treasury Department, and the lead negotiator of the *Canada-U.S. Treaty*, also provided the American perspective on the relevant provisions of that *Treaty*.

[31] The Respondent brought a motion for an order declaring that the expert evidence of all the expert witnesses was inadmissible. The grounds the Respondent relied upon were that the expert evidence:

(i) was not necessary;
(ii) was not relevant;
(iii) opines on matters of domestic law; and
(iv) engages in advocacy.

[32] The Appellant countered that the experts provided evidence on what the OECD Model provisions were intended to mean, and with respect to Mr. Rosenbloom's evidence, what the *Canada-U.S. Treaty* provisions were intended to achieve from an American perspective. In that light, the Appellant contends the evidence does not run afoul of any of the rules for admissibility as laid out in the *R. v. Mohan*[1] case from the Supreme Court of Canada.

[33] Rather than matching the detailed argument of both sides in analyzing the admissibility of the expert evidence globally, I shall outline only those aspects of the expert evidence upon which I intend to rely, and indicate why I find such evidence admissible. There are only two areas of expert evidence which will factor into my analysis:

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1 [1994] 2 S.C.R. 9.

(i) the significance of the requirement for a power of disposal by the Knights of Columbus over Canadian premises to find there is a fixed place of business of the Knights of Columbus in Canada; and

(ii) the inference to be drawn that substantial insurance activity could be carried out by an American organization such as the Knights of Columbus in Canada without subjecting itself to Canadian tax, due to the absence in the *Canada-U.S. Treaty* of an insurance clause similar to subparagraph 5(6) of the *UN Model Tax Treaty*.

[34] On both these matters it is the intent of the drafters of the *Treaty* that is the fact I am attempting to ascertain. I have no difficulty in finding such evidence relevant. As indicated by Justice La Forest in the decision *Thomson v. Thomson*[2]:

> It would be odd if in construing an international treaty to which the legislature has attempted to give effect, the treaty were not interpreted in the manner in which the state parties to the treaty must have intended.

Also, as Justice Iacobucci opened his analysis in *Crown Forest Industries Ltd. v. Canada*[3]:

> In interpreting a Treaty, the paramount goal is to find the meaning of the words in question. This process involves looking to the language used and the intentions of the parties.

Clearly, intention is relevant.

[35] With respect to necessity, where do I turn for guidance as to the drafters' intention. In *Crown Forest Industries Ltd.*, the Supreme Court of Canada accepted that it was entirely in order to rely on extrinsic materials to assist in the interpretation of a *Treaty*. Is it necessary for me to go beyond those materials (UN Model, OECD Model, commentaries, academic writings, international jurisprudence)? I believe it is. The experts brought a wealth of knowledge and background to the development of the term "permanent establishment" in the OECD Model and the UN Model. Indeed, they were involved in that very development. This was summarized and subjected to cross-examination and, consequently, provided me with evidence necessary to

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2 [1994] 3 S.C.R. 551.

3 [1995] 2 S.C.R. 802.

appreciate as fully as possible the intended meaning of "permanent establishment", both in the OECD Model and, from an American perspective, in the *Canada-U.S. Treaty*.

[36] The Respondent argued that even if I got by the hurdles of relevance and necessity, I should find the expert evidence inadmissible as:

(i) it goes to domestic law; or
(ii) it engages in advocacy.

[37] With respect to the drafters' intention in connection with the definition of the fixed place of business permanent establishment, and especially the requirement for some power of disposal, I do not conclude this is a matter of domestic law, certainly as it pertains to the OECD Model. Further, Mr. Rosenbloom's opinion in that regard pertained to the American perspective only and not the Canadian perspective.

[38] With respect to the inference to be drawn from there being no insurance clause, which I will describe in more detail shortly, I also do not view this as a matter of interpreting domestic law. I recognize it is up to me to determine the meaning of permanent establishment as it pertains to the Knights of Columbus' potential Canadian tax liability pursuant to the *Canada-U.S. Treaty*. Evidence leading to drawing an inference by the exclusion of an insurance clause that is found in another model, and indeed found in other Canadian tax Treaties is not evidence of domestic law: it is simply evidence of what was intended by the drafters by not including such a clause.

[39] I conclude these two areas of expert evidence do not run afoul of the criteria set out in *Mohan*, nor do they engage in advocacy. So, what was the expert evidence?

Fixed Place of Business

[40] Although the Commentary to the OECD Model refers to a place of business being "at the disposal" of the enterprise, the experts provided valuable insight as to what was intended by this aspect of the fixed place of business. It does not mean simply that the Knights of Columbus must have a key to the agent's premises, as this would too easily circumvent the objective of this requirement, though, according to Mr. Vann, it is necessary to show an independent right of disposition in the principal, in this case the Knights of Columbus. Mr. Vann did not, in any detailed way, clarify the independent right, other than to stress the importance of distinguishing between the agent's fixed place of business and the enterprise's fixed place of business. This

begs the question -- whose business is the agent carrying on at his place of business, or as Mr. Rosenbloom put it:

> A place of business that is simply useful or used by an agent to carry on its function as an agent must be distinguished from a place of business that is used by the Knights to carry on its business, and the tool that we have to make that distinction is the words "at the disposal".

Mr. Rosenbloom assisted in this regard suggesting that an agent carries on an agency business for the most part, but when actually meeting a prospective Knights of Columbus' member to solicit an application, that could be viewed as the Knights of Columbus' business. If those customer meetings regularly took place at the agent's place of business, Mr. Rosenbloom conceded in such circumstances, the place of business could be viewed as being at the disposal of the non-resident enterprise. What struck me from the experts is how they struggled with the question of what business the agent carries on. Again, Mr. Rosenbloom:

> The distinction is the fixed place of business used for the agent's own activities, even though they help the Knights, and a fixed place of business used for the business of the Knights. That is the distinction I am trying to make. … I would draw your attention to paragraph 23 of the commentary on Article 5. I refer to this at page 16 of my report. I had been looking for it fruitlessly until now. The OECD commentaries say that the decisive criterion is whether the activity of a fixed place of business forms an essential and significant part of the activity of the enterprise as a whole. That's essentially what I'm trying to say.

[41] All to say, the experts did not answer the very issue facing me, but this certainly illuminated the trickiness of nailing down precisely what was intended by a fixed place of business.

Inference from Lack of Insurance Clause

[42] Some background is in order. Paragraph 39 of the OECD Commentary on Article 5 of the OECD Model reads:

> According to the definition of the term "permanent establishment" an insurance company of one State may be taxed in the other State on its insurance business, if it has a fixed place of business within the meaning of paragraph 1 or if it carries on business through a person within the meaning of paragraph 5. Since agencies of foreign insurance companies sometimes do not meet either of the above requirements, it is conceivable that these companies do large-scale business in a State without being taxed in that State on their profits arising from such business. In order to obviate this possibility, various conventions concluded by OECD Member

> countries include a provision which stipulates that insurance companies of a State are deemed to have a permanent establishment in the other State if they collect premiums in that other State through an agent established there – other than an agent who already constitutes a permanent establishment by virtue of paragraph 5 – or insure risks situated in that territory through such an agent. The decisions as to whether or not a provision along these lines should be included in a convention will depend on the factual and legal situation prevailing in the Contracting States concerned. Frequently, therefore, such a provision will not be contemplated. In view of this fact, it did not seem advisable to insert a provision along these lines in the Model Convention.

[43] The provision this Commentary refers to I have called the "insurance clause". The insurance clause is embodied in Article 5(6) of the UN Model which reads:

> Notwithstanding the preceding provisions of this article, an insurance enterprise of a Contracting State shall, except in regard to re-insurance, be deemed to have a permanent establishment in the other Contracting State if it collects premiums in the territory of that other State or insures risks situated therein through a person other than an agent of an independent status to whom paragraph 7 applies.

[44] Paragraph 26 of the Commentary on this Article states:

> This paragraph does not correspond to any provision of the OECD Model Convention. It was included because it was the common feeling of the Group that the OECD definition of permanent establishment was not adequate to deal with certain aspects of the insurance business. Members from developing countries pointed out that if an insurance agent was independent, the profits would not be taxable in accordance with the provisions suggested in article 5, paragraph 7, of the United Nations Model Convention (based on Article 5, paragraph 6, of the OECD Model Convention); and if the agent was dependent, no tax could be imposed because insurance agents normally had no authority to conclude contracts as would be required under the provisions suggested in subparagraph 5(a) (based on Article 5, paragraph 5, of the OECD Model Convention). Those members expressed the view that taxation of insurance profits in the country where the premiums were being paid was desirable and should take place independently of the status of the agent. However, such taxation is based on the assumption that the person (employee or representative) through whom premiums are collected and risk insured is present in the country where the risk was located.

[45] Professor Arnold then draws the following inferences:

> 4.6.14 Some inferences may be drawn from Paragraph 39 of the Commentary on Article 5 of the OECD Model, Article 5(6) of the UN Model, and Paragraph 26 of the Commentary on that Article as set out in the preceding paragraphs. First, if the Canada-United States Tax Convention as amended contained a provision corresponding to Article 5(6) of the UN Model, then the Knights of Columbus would be deemed to have a PE in Canada because it collects premiums and insures risks in Canada through its agents. Second, as members of the OECD, both Canada and United States and their treaty negotiators must be considered to have been aware of the possibility, expressly stated in Paragraph 39 of the Commentary on Article 5 of the OECD Model, that insurance companies resident in one country could engage in large-scale business activities in the other country without having a PE there. Further, they must be considered to have been aware of the possibility, alluded to in Paragraph 39 of the Commentary on Article 5 of the OECD Model and evidenced by Article 5(6) of the UN Model, of including a specific provision with respect to insurance companies along the lines of Article 5(6) of the UN Model. The fact that they did not include such a provision indicates that they accepted the possibility that insurance companies resident in one state would organize their affairs so as to be taxable only in their country of residence despite carrying on substantial business activities in the other state. Third, given the widespread and clear recognition that the provisions of Article 5 of the OECD Model might not allow a country to tax insurance companies resident in their treaty partners, and given that both Canada and the United States are members of the OECD, it is fair and reasonable to assume that each country accept the nontaxation of insurance companies resident in the other country on profits derived from insurance business conducted in the country because that nontaxation would operate on a reciprocal basis. In other words, the United States accepted that Canadian-resident insurance companies could conduct extensive business activities in the United States without the imposition of any US tax because US-resident insurance companies could conduct similar activities in Canada without any Canadian tax. This reciprocity is a fundamental principle of tax treaties and should not be undermined by one party to the treaty bargain adopting a strained and unnatural interpretation of Article 5(5) concerning dependent agents in order to subject an insurance company resident in the other country to tax.

Professor Arnold goes on to conclude:

> The inclusion of specific provisions dealing with insurance in several Canadian and a few US tax treaties reinforces the conclusion arrived at in the preceding paragraphs on the basis of the Commentary on Article 5 of the OECD Model and Article 5(6) of the UN Model, namely, that the intention of the parties to the Canada-United States Tax Convention was not to tax insurance companies resident in one country doing substantial business in the other country in certain circumstances.

[46] Professor Vann confirmed the OECD specifically decided against the insurance clause,

> "even though this meant that a substantial insurance business could be conducted in a country without producing a permanent establishment and taxing rights there".

He explained the insurance provision is more favoured in Treaties with developing countries, though is by no means exclusive to them. Both Canada and Australia have inserted this provision in many of their Treaties.

Analysis

[47] The Government of Canada assessed the Knights of Columbus principally on the basis that it had a deemed permanent establishment in Canada arising from the application of Articles V(5) and (7) (the "dependent agent permanent establishment"), and secondly, on the basis it had a fixed place of business permanent establishment in accordance with Article V(1) (the "fixed place of business permanent establishment").

[48] The *Treaty* provisions are attached as Schedule "A". Before addressing the specific issues of a dependent agent permanent establishment and fixed place of business permanent establishment I will provide a brief roadmap as to the application of the *Canada-U.S. Treaty*. Pursuant to paragraph 2(3)*(b)* of the *Income Tax Act*, a non-resident is taxed on business profits earned in Canada, if the non-resident carries on business in Canada. However, Article VII of the *Canada-U.S. Treaty* stipulates the business profits are only taxable in Canada if the non-resident carries on business through a permanent establishment. Thus we get to Article V with its two types of permanent establishment. It is important to note that the *Canada-U.S. Treaty* is modelled after the OECD Model, and commentary with respect to that model is useful in interpreting the *Canada-U.S. Treaty*. As mentioned earlier, the Supreme Court of Canada was clear in the case of *Crown Forest* that it is appropriate for the Courts to interpret Treaties liberally, relying upon extrinsic materials such as commentaries to do so.

Dependent Agent Permanent Establishment

[49] As the dependent agent permanent establishment is the Respondent's major assessing position I will address it first. Paragraphs 5, 6 and 7 of Article V of the *Canada-U.S. Treaty* operate together as follows:

(i) There must be a person who habitually exercises an authority to conclude contracts in the name of the Knights of Columbus.

(ii) That person cannot be an agent of an independent status acting in the ordinary course of his business.

(iii) There will be no dependent agent permanent establishment if the person in Canada engaged solely in certain activities including "advertising, the supply of information, scientific research or similar activities which have a preparatory or auxiliary character".

The OECD Commentary adds some clarification to these provisions by suggesting that:

(4) The authority to conclude contracts must cover contracts relating to operations which constitute the business proper of the Knights of Columbus. (see paragraph 33 of the OECD Commentary)

[50] I am not going to delve into the considerable arguments concerning the dependence or independence of the Field Agents. I have concluded that neither the Chief Agent nor the General Agents are legally or economically dependent on the Knights of Columbus, and are indeed agents of an independent status acting in the ordinary course of their own business. The Field Agents are another matter. They are not, I find, as independent as the agents in American Income Life Insurance Company. However, for purposes of determining whether the Knights of Columbus has a dependent agent permanent establishment, I need not reach a final conclusion of their status. The issue of dependent agent permanent establishment is determined by an examination of the habitual exercise of an authority to conclude contracts. I find none of the Chief Agent, General Agents or Field Agents, even if any of them were dependent, exercise such authority.

[51] There are three contracts which the Respondent suggests might meet the *Treaty* criteria of being habitually exercised by Agents:

(i) the permanent insurance contract itself;
(ii) the Temporary Insurance Agreement; and
(iii) the contracts whereby the General Agents retain the Field Agents.

Retention of Field Agents

[52] I will deal with the last contract first, as it can be readily discounted. The contract pursuant to which Field Agents are hired are not contracts constituting the business proper of the Knights of Columbus. The contracts constituting the

business proper are contracts for the sale of insurance. In paragraph 33 of the OECD Commentary, this type of authority to contract is specifically mentioned:

> It will be irrelevant, for instance, if the person had authority to engage employees for the enterprise to assist that person's activity for the enterprise…

[53] Further, I find the hiring of the Field Agents is not concluded by the General Agents in any event. The evidence was that every Field Agent had to be screened by the Knights of Columbus, and, notwithstanding Mr. Gall's 100% track record of having all his prospective agents approved, there remained a procedure that specifically deprived the General Agents of concluding these contracts: the contracts were concluded in New Haven.

Permanent Insurance Contracts

[54] The Respondent's position is that the permanent insurance contracts are concluded in Canada by the Field Agents, on the basis that the agents solicited and received applications which were routinely approved. The Respondent draws support for this proposition from the OECD Commentary paragraph 32.1:

> For example, an agent may be considered to possess actual authority to conclude contracts where he solicits and receives (but does not formally finalise) orders which are sent directly to a warehouse from which goods are delivered and where the foreign enterprise routinely approves the transactions.

[55] With respect, I do not agree with the Respondent. The Commentary refers to a delivery of goods. The underwriting process involved in approving insurance applications is a far cry from filling in orders at a warehouse for the delivery of goods. Further, I find it is inaccurate to describe a 90% approval rating for applications as routine approval. There is nothing routine about the complex, detailed medical inquiries that form part of the application process, which were developed in New Haven, not by the Field Agents. Even with respect to the 90% of applications that were approved, as Dr. Conforti pointed out, many of these still required further investigation: that investigation is initiated from New Haven.

[56] The Respondent conceded that approximately 8% of the applications are not routinely approved. Yet all applications are subjected to the same screening. That screening, whatever the result, cannot be considered routine approval.

[57] The Respondent further argues that "concludes contract" involves more than legalistic formality. It can mean negotiation, not negotiation of each and every clause, but when dealing with a standardized contract, the act of persuasion and discussion. This, goes the Respondent's argument, is what the Field Agent does. Article 33 of the OECD Commentary says this about concluding contracts:

> A person who is authorized to negotiate all elements and details of a contract in a way binding on the enterprise can be said to exercise this authority "in that State", even if the contract is signed by another person in the State in which the enterprise is situated or if the first person has not formally been given a power of representation. The mere fact, however, that a person has attended or even participated in negotiations in a State between an enterprise and a client will not be sufficient, by itself, to conclude that the person has exercised in that State an authority to conclude contracts in the name of the enterprise.

[58] I have not been satisfied that what the Field Agents do is the extent of negotiation contemplated by this Commentary, when referring to all elements and details of a contract, even when dealing with what the Respondent calls a standardized contract. It is head office in New Haven that determines both the form and substance of the permanent insurance contract. Some of these details are predetermined, and some are determined as a result of the underwriting process. The involvement of the Field Agents in presenting the Knights of Columbus' products does not go to the negotiation of the details of those products. Frankly, I see their role more in line with that of a technician than a contract negotiator. Even if I viewed the Field Agents' activities as some form of negotiation, the Commentary is clear that participation in negotiation may not be sufficient. In these circumstances, I find the Field Agents' activities are not in fact sufficient to constitute concluding contracts. They simply have no control over the details of the contract.

[59] There is no question that the permanent insurance contracts only become legally binding once the Knights of Columbus in New Haven have completed the underwriting process: the contract is concluded in the United States. The Agent solicits applications, the applications are reviewed in New Haven and it is in New Haven that the contract is finalized.

<u>Temporary Insurance Agreements</u>

[60] This leaves the Temporary Insurance Agreement. If I find, as I did in *American Income Life Insurance Company v. Her Majesty the Queen*[4], that the Temporary Insurance Agreement and permanent insurance are all one contract, then the Respondent's argument cannot be successful for reasons just given in the previous section. It is only if I conclude that the Temporary Insurance Agreement is a separate contract that I must then consider if the Field Agents have indeed habitually exercised authority to conclude the Temporary Insurance Agreement. Interestingly, Respondent's counsel took the position that the Temporary Insurance Agreement and permanent insurance are indeed one, but argued in the alternative if I found the Temporary Insurance Agreement to be a separate contract.

[61] Is the Temporary Insurance Agreement part and parcel of the permanent insurance contract? Neither party addressed this in any detail, unlike in *American Income Life Insurance* case where the issue was explored at length. In *American Income Life* I concluded the conditional receipt (equivalent to the Knights of Columbus' Temporary Insurance Agreement) was not a separate contract, but was part of the one contract for permanent insurance. Although the wording of the Temporary Insurance Agreement is different from the conditional receipt in *American Income Life,* coverage is still dependent on the successful completion of the underwriting process. The Temporary Insurance Agreement contains no wording as was found in the American Income Life conditional receipt which expressly stipulated "the entire contract consists of the application and policy". However, it was clear from the Knights of Columbus' representatives that a claim pursuant to the Temporary Insurance Agreement could only be successfully made if the applicant is approved for permanent insurance by the underwriting process: in effect, if no permanent insurance would have been provided, no temporary insurance could be claimed. The Temporary Insurance Agreement cannot stand alone. The applicant is paying the premiums for permanent coverage, not for temporary coverage; temporary coverage results from a successful underwriting, though effective to the date of application. In this respect it is part and parcel of the permanent insurance, and it is only a matter of the timing of the effective date of coverage at issue, not a question of some separate insurance contract. I further adopt my reasons from *American Insurance Life* on this point to conclude that the Temporary Insurance Agreement is not a separate contract. However, as both parties addressed the issue as if the temporary insurance was a separate contract, I will do likewise.

[62] The Appellant first argues that the Temporary Insurance Agreement is not a contract at all, but more in the form of a promotional gift. While I agree it is a

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promotional tool, I disagree that it is not a contract. A promotional gift suggests no consideration, yet the applicant does have to provide something to obtain the temporary insurance coverage. The applicant must provide the application, including the initial premium. Clearly, the Knights of Columbus feels bound and it keeps some consideration to cover costs of meeting its obligation. The initial premium itself is consideration for the permanent insurance, but the fully completed application is the consideration for the temporary insurance. All the elements of a contract are in place to constitute the Temporary Insurance Agreement a contract. It may be part of the application as a form of motivation to the applicant, or, as Mr. Smith put it, to simply be competitive in the industry, but that does not make it something other than a contract.

[63] Did the Field Agents conclude the Temporary Insurance Agreement? The Respondent's position is that because the Knights of Columbus was bound to provide the temporary insurance, upon the agents accepting the application from the applicant along with the initial premium, the agents have effectively "concluded" the contract. The Appellant argues that because the Field Agents had no authority or ability to alter, add or remove any term of the Temporary Insurance Agreement – a take it or leave it proposition from the Knights of Columbus to the Applicant – it cannot be said that the Field Agents "concluded" the contract.

[64] What did the Field Agents do in relation to the Temporary Insurance Agreement? They basically presented it to applicants as an incentive to apply for permanent insurance. If you apply for permanent insurance with the Knights of Columbus, it will provide this temporary coverage pending approval of the permanent insurance. Yes, the Knights of Columbus was bound at the point the Field Agent took the application and initial premiums (or somewhat later depending on medical tests), but it was not the Field Agent who bound them. The Knights of Columbus was bound by the very term of the contract presented to the applicant, terms developed by the Knights of Columbus and not alterable by the Field Agent. Vis-à-vis the temporary insurance, the Field Agent was simply the messenger. Unlike the permanent insurance coverage, which is what the applicant is applying for, and which is not finalized until completion of the underwriting process, the temporary insurance is effective immediately. It is effectively an offer which binds the Knights of Columbus once the applicant accepts by completing an application and depositing the initial premium with the Field Agent. But what is the Knights of Columbus bound to do? It is bound to continue the underwriting process, even after the applicant dies, and to pay out a claim for temporary coverage. The Field Agent's role in the process

surrounding the Temporary Insurance Agreement is minimal. I find the Field Agent is not, in these circumstances, concluding the contract.

[65] Had I found that the Field Agents were concluding the contracts, two further questions need to be addressed. First, was the contract for the temporary insurance part of the business proper of the Knights of Columbus? This is an additional qualification raised by the OECD Commentary and to which neither party took exception. Certainly, the Knights of Columbus was in the business of selling life insurance, and the temporary insurance was life insurance. But that temporary coverage must be put in context: it was something that the Knights of Columbus offered to be competitive. It was an incentive to get that application for permanent insurance. While I have concluded it was not legally a gift, as there was some consideration, it was, for business purposes, something of a throw-away for the Knights of Columbus. The initial premium was for the permanent insurance; only if the applicant died before final approval, and the Knights of Columbus had to pay out under the Temporary Insurance Agreement, and consequently kept some of the premium, could the premium be seen as relating to the Temporary Insurance Agreement. Dr. Conforti was clear though, the price of insurance was not impacted by the temporary insurance coverage. I draw from this that the Knights of Columbus was not selling temporary insurance. It was simply recouping some cost of administering a claim from the initial premium. The Appellant described this coverage as a "loss leader". I do not believe that is exactly accurate. That presumes the temporary insurance is part of what the Knights of Columbus sells, a part that is simply not profitable. I find a truer picture is that the Knights of Columbus is not in the business of selling temporary insurance: it provides temporary insurance solely as an incentive. That incentive could just as readily have been a five-day cruise. I find temporary insurance coverage, as a form of incentive, is no more the Knights of Columbus' business proper than would the cruise be, if that had been the incentive. I conclude there is no dependent agent permanent establishment, even if the agents were found to have authority to conclude the Temporary Insurance Agreements, and even presuming they were separate contracts.

[66] I would, however, like to address the second question that would arise had I found the Field Agents concluded the temporary insurance contract, and if that temporary insurance is viewed as part of the business proper of the Knights of Columbus. The question is whether the Field Agents' activities are simply of a preparatory or auxiliary character, and thus pursuant to Article V(6)*(e)*, insufficient to constitute a dependent agent permanent establishment. This is a broader inquiry than just looking at the Field Agent's activities in connection with the Temporary Insurance Agreement. For Article V(6) to deem the Field Agents not to be a deemed

permanent establishment requires a finding that the Field Agent is engaged "solely in one or more" of the activities listed. From a different perspective, did the Field Agent engage in any activity other than those enumerated in Article V(6)? If so, then it follows that the agent was not engaged solely in the listed activities. The wording of the *Canada-U.S. Treaty* and the OECD Model is different in this respect. The provision in the *Canada-U.S. Treaty* applies to both the fixed place of business permanent establishment and the dependent agent permanent establishment. The OECD provision applies to a fixed place of business permanent establishment, but only to a dependent agent permanent establishment if the activities are exercised through a fixed place of business permanent establishment. The contorted nature of the interplay between paragraphs in these Treaties is at times tortuous.

[67] The wording in the *Canada-U.S. Treaty* does not appear to allow for limiting the analysis of the Field Agents' activities to their activity in connection with the Temporary Insurance Agreement only. The Temporary Insurance Agreement, in and of itself, could well be considered as a promotional tool, to fall into the category of "advertising….or similar activities which have a preparatory or auxiliary character". But that finding alone is not sufficient to deem the Field Agents not to be a permanent establishment. The wording of Article V(6) requires a broader inquiry into all of the Field Agents' activities to determine if all of their activities are of the nature set forth in the Article V(6) list. Bear in mind, at this stage I am still exploring the application of Article V(6) to the dependent agent permanent establishment, not the fixed place of business permanent establishment. In applying Article V(6) to a dependent agent permanent establishment, one is left to consider an agent with authority to conclude a contract that goes to the business proper of the non-resident may yet be engaged in only preparatory or auxiliary activities. How can an agent's activities be preparatory or auxiliary if the agent can ultimately conclude the very contracts of the business proper of the principal? The OECD Commentary is of little assistance as the OECD Model only applies to activities of the dependent agent if exercised through a fixed place of business, which brings in entirely different considerations. It is at this stage, one of many, where I have a greater appreciation for Mr. Innes' theory of relativity.

[68] Do the Field Agents do something more than the activities listed in Article V(6)? They contact the Knights of Columbus' members, arrange to meet them, discuss the Knights of Columbus' insurance products with the members and determine if there is a product that fits the member's needs and profile, obtains an application and the initial premium and forwards that to the Knights of Columbus in New Haven. Fortunately, given my findings that no contract is concluded, and even if one had been, it does not go to the business proper of the Knights of Columbus, I do

not have to resolve the issue of the auxiliary or preparatory nature of these activities. I do have some concerns, however, that if the Field Agent is considered to have concluded the contract for the business proper of the Knights of Columbus, that it would be difficult to find all of these activities as simply of a preparatory or auxiliary character. I had been referred to comments in *Western Union Financial Service Inc. v. Additional Director of Income Tax*[5], but it dealt with the preparatory or auxiliary nature of activities in the context of a fixed place of business permanent establishment, and were not helpful in the context before me.

[69] My conclusions thus far make it unnecessary to address the question of whether any agents in Canada were of an independent status acting in the ordinary course of their business (Article V(7)). I would, however, like to comment on the interplay between Article V(5) and V(7). I interpret this somewhat awkward language as follows. If the agent is found to be both legally and economically dependent, then Article V(7) simply does not come into play, as it addresses only agents of independent status. If the agents are of independent status, then one must ask whether they are acting in the ordinary course of their own business. As I have previously indicated, I find the General Agents and Chief Agent to both be of independent status, and also to be acting in the ordinary course of their business. I have found the Field Agents, regardless of whether they are dependent, do not have authority to conclude contracts. The question of whose business is being carried on by the Field Agents is significant in determining the fixed place of business permanent establishment, which I now turn to.

Fixed Place of Business Permanent Establishment – Article V(1)

[70] It was the Respondent's fall-back position that the Knights of Columbus had a fixed place of business permanent establishment. The Respondent relied to a large extent on the decision of President Thorson in the case of *Panther Oil & Grease Manufacturing Co. of Canada Ltd.*[6] As I indicated in my Reasons in *American Income Life*, the *Panther Oil* case is clearly distinguishable from the situation of the application of the *Canada-U.S. Treaty* to insurance companies such as American Income Life, or the Knights of Columbus, carrying on business in Canada. Further, the Supreme Court of Canada in a subsequent decision, *Sunbeam Corporation (Canada) Ltd. v. Minister of National Revenue*[7], faced the very same regulations at

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5 (2006) 8 ITLR 1067 (Income Tax Appellate Tribunal of India).

6 61 D.T.C. 1222.

7 62 D.T.C. 1390 (S.C.C.).

issue in *Panther Oil*, and reached a different conclusion than *Panther Oil* as to what constituted a fixed place of business permanent establishment. A well-established selling organization is not sufficient to constitute a branch, and consequently, a permanent establishment. I take from *Sunbeam* that you do need a physical place, not the mere nebulous agency network. I put little reliance on the decision of *Panther Oil*.

[71] The Respondent argues that if a physical place is necessary, then the Field Agents' offices serve as that physical place as they effectively carry on the selling activity, which constitutes the Knights of Columbus' business, out of their offices, notwithstanding the actual solicitations take place almost entirely at the applicant's premises, not at the agents'. According to the Respondent, you cannot divide up what the Field Agent does between the agent's business (only carried out from their home office) and the Knights of Columbus' business, carried on through the agent outside the agent's home office.

[72] To constitute the Field Agent's office a fixed place of business permanent establishment of the Knights of Columbus requires:

(i) a place of some permanence;
(ii) that is a place of business; and
(iii) through which the Knights of Columbus' business is carried on.

[73] I am only raising the Field Agents' offices, as neither the Chief Agent nor General Agents' offices were vigorously argued by the Respondent, as being the fixed place of business of the Knights of Columbus, and for good reason. I find both the Chief Agent and the General Agents were not carrying on the Knights of Columbus' business from their offices, but were carrying on their own businesses. In the case of the Chief Agent, his work for the Knights of Columbus was part of his independent accounting practice. With respect to the General Agents, their business was the development of an agency network: it was not selling the Knights of Columbus' insurance.

[74] The Field Agents' home offices are a place of permanence, but are they places of business? The Appellant argues that they are not, as a place of business requires some minimum level and type of business activity to be conducted at the fixed place. I agree that one's home would not normally be considered a place of business if only a minor amount of business activities occur in the home. But what did the Knights of Columbus' Field Agents do from their home office? They organized their business activities, arranged for their solicitation meetings with potential applicants, kept

records, completed reports and did what commission salespeople do, other than the actual face-to-face solicitation. I disagree with the Appellant that this is such a minor amount of activity as to not constitute the home office a place of business. I find the Field Agents' home offices were permanent and were places of business.

[75] The issue of a fixed place of business permanent establishment is to be determined by considering the third condition. Was the Knights of Columbus' business being carried on through the Field Agents' home offices. This is where I found the experts' evidence of most assistance. Mr. Rosenbloom relies on OECD Commentary to conclude that the key concept on this issue was whether a place is "at the disposal" of the enterprise, the Knights of Columbus. Mr. Rosenbloom went on to state in his testimony:

> Now, I can see -- I think this is a question that is undecided. I don't think there's any jurisprudence on this. I can see someone saying that "at the disposal" means that the Knights actually, a representative of the Knights, must have access, but I am telling you that I would be troubled by a situation where even if the Knights didn't have access, the place was regularly being used to carry on the core business of the Knights of Columbus.

[76] Mr. Vann confirms this reliance on the concept of premises being at the disposal of the enterprise. In his opinion he states:

> The clear separation between the two types of permanent establishments that now exists in the OECD and UN Models requires the drawing of a distinction between a fixed place of business of the enterprise and a fixed place of business of a dependent agent of the enterprise. When the separation occurred, this distinction was drawn in terms of whether the place of business was "at the disposal" of the enterprise…What is clear is that the fixed place of business has to be that of the enterprise, not that of an agent or an associated enterprise.

[77] Further, in his opinion, after quoting the OECD Commentary, Mr. Vann clarifies the position as follows:

> From these extracts it is clear that a place of business of a representative of an enterprise cannot be a place of business of the enterprise unless the enterprise itself or through other representatives has access to the fixed place of business in its own right and not simply because it is the place of business of the representative.

[78] For the Field Agents' residences to be considered fixed places of business of the Knights of Columbus, the Knights of Columbus must have a right of disposition over these premises. A right of disposition is not a right of the Knights of Columbus

to sell an agents' house out from under him. The Knights of Columbus might be viewed as having the agents' premises at its disposal, for example, if the Knights of Columbus paid for all expenses in connection with the premises, required that the agents have that home office and stipulate what it must contain, and further required that clients were to be met at the home office and in fact the Knights of Columbus' members were met there. In such circumstances, although the Knights of Columbus may not have a key to the premises, the premises might be viewed as being at the disposal of the Knights of Columbus. This would be consistent with Mr. Rosenbloom's comments.

[79] What it comes down to is distinguishing the agents' business activities from the Knights of Columbus' business activities. If sufficient Knights of Columbus' business activities are carried on at the agents' home offices, then the condition of the premises being at the Knights of Columbus' disposal would be met. The Respondent argues that the agents' activities cannot be segregated – everything they do goes towards obtaining an application, and that is the Knights of Columbus' business. I disagree with the Respondent.

[80] Once it has been determined that the Field Agents are independent contractors, which has been agreed, that is, that they are in business on their own account, then it is illogical to find that all the organizing and recordkeeping that they conduct at home is anything other than business activities of their own business. The Knights of Columbus do not have any right of disposition over these premises. The argument that payment of an expense commission creates some such right is not well founded. The expense commission is simply an added commission bearing no relation to actual expenses, which are totally borne by the agent. As well, the agents employ no Knights of Columbus' staff, have no Knights of Columbus' signage on the property, are not under the control of the Knights of Columbus for what is required at the home office, and simply provide no access to the Knights of Columbus. The agents do not meet applicants at the premises[8]. The Knights of Columbus make no operational decisions at the Field Agent's premises. The Knights of Columbus had no officers, directors or employees even visit the agents' home offices, let alone have any regular access. All risks connected with carrying on business at the home offices are borne by the agents themselves. The agents are not carrying on the Knights of Columbus'

[8] There was some evidence that one agent may have met applicants at the agent's home office. This is insignificant in the overall view of the *modus operandi* of the Knights of Columbus and the Field Agents generally. It is insufficient for concluding the Knights of Columbus has a fixed place of business permanent establishment.

core business from these premises. Their premises cannot therefore be found to be a fixed place of business permanent establishment.

[81] Although it is unnecessary to consider Article V(6) in the context of the fixed place of business permanent establishment analysis, given my conclusion, had I had to consider the application of Article V(6) to Article V(1), I would have found it did apply to deem the Field Agent's offices not to be permanent establishments. Unlike the dependent agent permanent establishment analysis where I consider Article V(6) in light of all the agents' activities, not just activities carried out at the home office, in applying Article V(6) to a fixed place, only the activities at the fixed place (the home office) are to be considered. The activities the Field Agent carries on from home consist, I find, solely of storage, collection of information, supply of information and similar auxiliary or preparatory activities.

[82] Relying on paragraph 7 of Article V of the *Canada-U.S. Treaty*, the Appellant argued that the offices of an independent agent cannot constitute a fixed place of business permanent establishment. Given my conclusions, I need not address this argument. I do however wish to comment that, notwithstanding Mr. Rosenbloom's opinion, I find Article V(7) does not appear to come into play with respect to the Article V(1) fixed place of business permanent establishment. As has been clear from the fixed place of business analysis, inherent in that analysis is a consideration of whose business the agent is carrying on from the home office. It strikes me as redundant to have to refer to Article V(7) in this context: the matter has already been addressed. I read the role of paragraph V(7) as relating to the deemed or dependent agent permanent establishment. Frankly, notwithstanding the experts' views that every word of these Treaties has been scrupulously negotiated, my impression is that the words are not beacons of clarity. Maybe this is the risk of dozens of negotiators of several languages negotiating the OECD Model, and then two countries trying to adopt that model to their circumstances – we end up with a camel rather than a horse.

Inferences from Lack of Insurance Clause

[83] Finally, I wish to address the second area where I found the experts' views valuable; that is, with respect to the significance of the lack of an insurance clause in the *Canada-U.S. Treaty*. The insurance clause found in the UN Model deems a foreign insurance enterprise to have a permanent establishment in the other state if the foreign insurer collects premiums or the foreign insurer insures risks in the other state through a person other than an agent of independent status. This clearly switches the emphasis onto the dependent versus independent status of the agent.

In effect, a dependent agent without authority to conclude contracts is not sufficient to escape liability in Canada. If premiums are collected or risks are insured through a dependent agent, the insurance clause would create a Canadian liability. The *Canada-U.S. Treaty* does not contain this provision, which the UN included as it felt the OECD Model was not adequate to deal with how the insurance industry operates. None of the experts suggested Canada omitted this clause because the Canadian Government believed the existing *Treaty* provisions were adequate to tax American insurance companies carrying on business in Canada through Canadian agents. Indeed, quite the opposite. As Professor Arnold explained (see paragraph 45), it can be assumed the United States Government and Canadian Government, in acknowledging the principle of reciprocity in tax Treaties, intended extensive insurance business activities could take place in the other country without tax liability.

[84] Canada has had many opportunities over several years to add the insurance clause to the *Canada-U.S. Treaty*, but it has chosen not to do so. It has included this clause in other Treaties. I find the inferences overwhelmingly support the conclusion I have reached on the interpretation of the existing *Treaty* provisions. The Knights of Columbus can indeed carry on significant business in Canada without establishing a permanent establishment, and thus not subjecting itself to tax in Canada.

[85] In summary, the Appellant's appeal is allowed and the assessments are vacated on the basis that the Knights of Columbus did not carry on business in Canada through a permanent establishment either on the basis of the fixed place of business permanent establishment, or a dependent agent permanent establishment. Neither form of permanent establishment has been proven. Costs to the Appellant.

Signed at Ottawa, Canada, this 16th day of May 2008.

"Campbell J. Miller"

C. Miller J.

Schedule "A"

Article V – Permanent Establishment

1. For the purposes of this Convention, the term **"permanent establishment"** means a fixed place of business through which the business of a resident of a Contracting State is wholly or partly carried on.

2. The term "permanent establishment" shall include especially:

(a) a place of management;

(b) a branch;

(c) an office;

(d) a factory;

(e) a workshop; and

(f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.

3. A building site or construction or installation project constitutes a permanent establishment if, but only if, it lasts more than 12 months.

4. The use of an installation or drilling rig or ship in a Contracting State to explore for or exploit natural resources constitutes a permanent establishment if, but only if, such use is for more than three months in any twelve-month period.

5. A person acting in a Contracting State on behalf of a resident of the other Contracting State – other than an agent of an independent status to whom paragraph 7 applies – shall be deemed to be a permanent establishment in the first-mentioned State if such person has, and habitually exercises in that State, an authority to conclude contracts in the name of the resident.

6. Notwithstanding the provisions of paragraphs 1, 2 and 5, the term "permanent establishment" shall be deemed not to include a fixed place of business used solely for, or a person referred to in paragraph 5 engaged solely in, one or more of the following activities:

(a) the use of facilities for the purpose of storage, display or delivery of goods or merchandise belonging to the resident;

(b) the maintenance of a stock of goods or merchandise belonging to the resident for the purpose of storage, display or delivery;

(c) the maintenance of a stock of goods or merchandise belonging to the resident for the purpose of processing by another person;

(d) the purchase of goods or merchandise, or the collection of information, for the resident; and

(e) advertising, the supply of information, scientific research or similar activities which have a preparatory or auxiliary character, for the resident.

7. A resident of a Contracting State shall not be deemed to have a permanent establishment in the other Contracting State merely because such resident carries on business in that other State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business**.**

8. The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not constitute either company a permanent establishment of the other.

9. For the purposes of the Convention, the provisions of this Article shall be applied in determining whether any person has a permanent establishment in any State.

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