

**2009 IFA TRAVELLING LECTURESHIP ON ROYALTIES BY NATHAN BOIDMAN
APPENDICES TO LECTURE OUTLINE**

APPENDIX 81 (CRA STUDIES OF E-COMMERCE)

Material:

Revenue Minister Announces Release of Advisory Committee Report on Electronic Commerce, April 30, 1998, p. v-ix

Electronic Commerce and Canada's Tax Administration, A Report to the Minister of National Revenue from the Minister's Advisory Committee on Electronic Commerce, April 1998, p. 1-6

4.2.3 Characterization and Withholding Tax Issues, p. 62-64

4.2.5 Foreign Activities of Canadian Residents, p. 67-70

Electronic Commerce and Canada's Tax Administration, A Response by the Minister of National Revenue to his Advisory Committee's Report on Electronic Commerce, September 1998

Note "To the Reader"

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6.3.3-6.3.3.2 Characterization and Withholding Tax Issues

6.3.5-6.3.5.3 Foreign Activities of Canadian Residents

Revenue Minister announces membership of advisory groups on electronic commerce, May 31, 1999, modified 2002-11-04

E-Commerce & Computer Software, Window on Canadian Tax Commentary, May 16, 2002
Document number: 2002-0135765, Income Tax Act: 212(1)(d)

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E-Commerce & Computer Software

May 16, 2002

Window On Canadian Tax Commentary

Document number: 2002-0135765

Income Tax Act: 212(1)(d)

Please note that the following document, although believed to be correct at the time of issue, may not represent the current position of the CCRA.

Prenez note que ce document, bien qu'exact au moment émis, peut ne pas représenter la position actuelle de l'ADRC.

PRINCIPAL ISSUES: request for IFA conference to provide status of e commerce papers (Position Paper Internet Commerce and Characterization Issues Arising From Electronic Commerce) and announcements regarding related issues

POSITION: e commerce paper at Department of Finance for their consultation and CCRA no longer views payment for computer software as payment for secret formula

REASONS: Department of Finance removed Canada's observation in OECD Model Convention that Canada viewed a payment for "computer software" as a payment for a "secret formula"

2002-013576
Memo to Close File

DATE: May 16, 2002

SUBJECT: May 2002 Ifa Conference Question Regarding Status of E Commerce Papers and Change in Ccra View Regarding Payments For Computer Software

For the May 2002 IFA Conference in Toronto, we were asked whether we had any internal papers regarding the taxation of E commerce and whether we had any significant related announcements to make. Our response is as follows:

Question 3. Electronic Commerce

There have been various electronic commerce initiatives at the CCRA and OECD recently. Has the Income Tax Rulings Directorate prepared any publications or

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papers regarding the taxation of electronic commerce as a result? If yes, will the publications be made available to the public? Are there any significant announcements that the Income Tax Rulings Directorate can make now with respect to this study?

CCRA's Response

The Income Tax Rulings Directorate is currently working on two papers with respect to electronic commerce.

1. Position Paper Internet Commerce, which evolved from 2 sources:
 - a 1998 CCRA Technical Advisory Group (TAG) on Interpretation & International Cooperation; and
 - The "Taxation Framework Conditions", agreed upon in Ottawa in 1998 by member countries of the OECD.
2. Characterization Issues Arising From Electronic Commerce, which evolved from the OECD TAG on Treaty Characterization of Electronic Commerce Payments.

The above two papers have not been completed, but preliminary drafts have been forwarded to the Department of Finance for consultation purposes. Once the consultation process is completed with the Department of Finance, and once the OECD has finalized its positions on electronic commerce, the CCRA will make a decision as to how to communicate to the public the content of these two papers or, at least, how to communicate any significant discrepancies between the views of the OECD and the CCRA on this subject.

Computer Software

An issue that did come to the forefront as a consequence of the work done so far on the above two papers dealt with computer software. In the Commentary on Article 12 of the OECD Model Tax Convention on Income and Capital (April 29, 2000 condensed version) concerning the taxation of royalties, at paragraph 27, Canada has an observation that states:

Canada does not adhere to paragraphs 14 through 14.3. In Canada, payments by a user of computer software pursuant to a contract that requires that the source code or program be kept confidential, are payments for the use of a secret formula or process and thus are royalties within the meaning of paragraph 2 of the article.

After consultations with the Department of Finance, the Department of Finance wrote to the OECD on March 28, 2002 to inform them that Canada is removing its observation on Article 12 of the Commentary. Accordingly, as of March 28, 2002, for the purposes of Canada's Income Tax Conventions, subject to the

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exceptional cases described in paragraph 14.3 of the commentary on Article 12, the CCRA will no longer view such a payment as a payment for a "secret formula" and the CCRA will apply this interpretation for the Conventions in force as of March 28, 2002 and subsequent Conventions that come into force after that date.

However, for the purposes of Canada's Income Tax Conventions, the CCRA does view such a payment as a payment for "other intangible property", where the definition of a "royalty" in the royalty article in the particular Convention refers to "other intangible property". Also, the CCRA continues to view that Part XIII tax applies to such a payment pursuant to paragraph 212(1)(d) of Canada's Income Tax Act, unless the payment is in respect of what the CCRA refers to as "shrinkwrap" or the exception in subparagraph 212(1)(d)(vi) applies, because the payment is a "rent, royalty or similar payment, including, . . . , any payment (i) for the use of or for the right to use in Canada any property . . . or other thing whatever".

The CCRA intends to make an announcement regarding computer software payments in our next Technical News publication.

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The file is being closed since there are no other issues to address.

Gilles Gosselin
May 15, 2002