Tax Notes

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Wolters Kluwer

COVID-19 UPDATE

Given the rapidly changing information related to COVID-19 we are providing continuously updated information at https://wolterskluwer.ca/learning/covid-19/.

Canada

OAS Recovery Return for Non-Residents (June 19, 2020)

Non-resident seniors who receive Canadian old age security ("OAS") payments may have to pay recovery tax on those payments. A non-resident senior who receives OAS payments must submit an Old Age Security Return of Income ("OASRI") so that the CRA can determine if they have to pay recovery tax and also to ensure that OAS payments are not suspended.

In response to the COVID-19 pandemic, OAS payments to non-resident seniors have been temporarily extended if their 2019 OASRI has not been assessed. To avoid an interruption in benefits, non-resident OAS recipients are encouraged to submit their 2019 OASRI as soon as possible and no later than October 1, 2020.

No Change to SR&ED Filing Deadline (June 25, 2020)

The CRA website was updated with a confirmation that reporting deadlines for the scientific research and experimental development ("SR&ED") tax incentive program have not changed. Corporations still have 18 months after their tax year-end to file their SR&ED claim. However, businesses are strongly encouraged to file their SR&ED claim with their income tax return.

Upcoming Economic and Fiscal Snapshot (June 17, 2020)

Finance Minister Bill Morneau will present an Economic and Fiscal Snapshot on Wednesday July 8, 2020. The snapshot will provide information on the current state of the economy and the Government of Canada's response to support Canadians during the COVID-19 pandemic.

New COVID-19 Measures Bill Introduced (June 10, 2020)

Bill C-17, *An Act respecting additional COVID-19 measures*, received First Reading in the House of Commons on June 10, 2020. Part 1 amends the *Income Tax Act* to revise the eligibility criteria for the Canada Emergency Wage Subsidy. Part 2 enacts the *Time Limits and Other Periods Act (COVID-19)*, which addresses the need for flexibility in relation to certain time limits and other periods that are established by or under Acts of Parliament and that are difficult or impossible to meet as a result of the exceptional circumstances produced by COVID-19. In particular, the enactment

(a) suspends, for a maximum of six months, certain time limits in relation to proceedings before courts;

(b) temporarily enables ministers to suspend or extend time limits and to extend other periods in relation to specified Acts and regulations for a maximum of six months; and

(c) provides for the transparent exercise of the powers it confers and for Parliamentary oversight over the exercise of those powers.

Part 3 amends the *Income Tax Act* to authorize the use by officials, or disclosure to Government of Canada officials, of taxpayer information solely for the purpose of a one-time payment to persons with disabilities for reasons related to COVID-19. It also amends the *Children's Special Allowances Act* to authorize the disclosure of information for the purpose of that one-time payment. Part 4 amends the *Canada Emergency Response Benefit Act* to, among other things, enhance the administration and enforcement of the Act and allow a review of decisions made under the Act. It also provides that a worker is not eligible for an income support payment if they do not return to work when it is reasonable to do so or decline a reasonable job offer.

Extended Deadlines for Filing Partnership Return (June 1, 2020)

The CRA has extended some deadlines for filing a T5013 partnership information return for 2019. The deadline was previously extended to May 1, 2020. The CRA has updated its website with the following deadlines:

- May 1, 2020, for partnerships that would normally have a March 31, 2020, filing deadline;
- June 1, 2020, for partnerships that would normally have a filing deadline after March 31 and before May 31, 2020; and
- September 1, 2020, for partnerships that normally have a filing deadline on May 31, or in June, July, or August 2020.

CRA Resumes Some Audit Activities (May 28, 2020)

The CRA is resuming a full range of audit work, but is prioritizing actions that are beneficial to the taxpayer or where taxpayers have indicated there is an urgency to advancing their audit. The CRA is also focusing on higher dollar audits first, audits close to completion, and those with a strategic importance to the Government of Canada, provinces and territories, or tax treaty partners. In addition, efforts to combat suspected fraud and other criminal activity are advancing.

New methods of taxpayer and registrant interaction will be required, and the CRA is working to develop procedures and protocols to adapt these to the current reality. For example, taxpayers are provided with the option to send information via e-mail. Some key changes will relate to offering additional time and upfront consultation on requests to provide the CRA with information and access. Public Health directives will be respected, and additional reasonable measures will be extended both in terms of timing or another aspect of a CRA request.

In addition, Requirements for Information ("RFIs") issued prior to March 16 and due after that date will be reviewed, and taxpayers and third parties, including financial institutions, will be contacted where the CRA continues to require the information in the RFI.

Obtaining International Waivers and Notifications for Certificates of Compliance (May 27, 2020)

The CRA provided an update on its website with regard to its process for reviewing international waivers and requests for a certificate of compliance under section 116. The CRA has created a temporary procedure allowing taxpayers and their representatives to electronically submit urgent requests. Processing times might be longer than usual. For further information, see https://www.canada.ca/en/revenue-agency/campaigns/covid-19-update/international-waiver-compliance-certificate.html.

Clearance Certificate Update (May 26, 2020)

The CRA recently provided an update regarding its processing of requests for clearance certificates. The CRA continues to process clearance certificates, but its employees have limited access to their offices due to COVID-19. They are receiving minimal submissions sent by mail or fax, and therefore any documentation or new clearance request applications sent to the CRA after March 12, 2020, may not have been included in the inventory for processing. Legal representatives who submitted a clearance request after March 12, 2020, are encouraged to resubmit the request and supporting documents electronically, either through Represent a Client or by email.

As part of the response to COVID-19, the CRA has created a temporary procedure allowing taxpayers and their representatives to submit clearance certificate requests and supporting information via email. To submit the request via email, the legal representative must contact the CRA by sending an email, without confidential information, to CCTX19G@cra-arc.gc.ca and including in the subject line the province where the executor lives. A CRA officer will reply by email, outlining the potential security risks of using email to transmit confidential information. If you reply by email accepting the risks, the CRA will allow you to submit the clearance application and supporting information.

Provincial

Alberta

Corporate Tax Return Deadline Extended (May 25, 2020)

The filing deadline for an Alberta Corporate Income Tax Return ("AT1") has been extended to September 1, 2020, for an AT1 that would otherwise have a filing deadline in June, July, or August 2020. The deadline is June 1, 2020, for an AT1 that would otherwise have a filing deadline after March 18 and before June 1, 2020. Alberta will not assess a late-filing penalty with respect to an AT1 otherwise due during these deferral periods if the AT1 is filed on or before the respective extended deadline noted above.

Furthermore, the filing deadline for a Notice of Objection (Form AT97) that would otherwise have a filing deadline after March 18 and before June 30, 2020, is extended to June 30, 2020.

British Columbia

New Legislation Proposes Tax Amendments (June 24, 2020)

The provincial government has introduced the *Economic Stabilization Act*, which proposes to enact the many tax measures that have been introduced in response to COVID-19.

Logging Tax Return Extension (May 28, 2020)

Where a BC logging tax return is otherwise due between the periods of March 18, 2020, and August 31, 2020, the logging tax return is now due by September 1, 2020. Penalties and interest will not be charged if the payment requirements are met by the extended filing deadline.

Manitoba

Extension for RST Remittances (June 24, 2020)

Retail sales tax ("RST") returns for small and medium-sized businesses with monthly RST remittances of no more than $10,000 per month that would normally be due on April 20, May 20, June 22, July 20, August 20, and September 21 will now be due on October 20, 2020.

Businesses that file on a quarterly basis that have a due date of April 20 and July 20 will now have the due date extended to October 20, 2020.

Businesses that qualify for the above filing extension that were not able to file and remit their February sales tax return by the March 20 due date will not be assessed a late filing penalty, and interest will not be applied until after October 20, 2020.

Interest will continue to apply on all outstanding tax debts established prior to the March remittance deadlines. Businesses will still receive paper returns in the mail or web notice reminders by email for return periods March, April, May, June, July, and August.

Extension for HE Levy Remittances (June 24, 2020)

Health and Post Secondary Education Tax Levy (also known as "HE Levy") returns for small and medium-sized businesses with monthly HE Levy remittances of no more than $10,000 per month that would normally be due on April 15, May 15, June 15, July 15, August 17, and September 15 will now be due on October 15, 2020.

Businesses that qualify for the above filing extension that were not able to file and remit their February HE Levy tax return by the March 16 due date will not be assessed a late filing penalty, and interest will not be applied until after October 15, 2020.

Interest will continue to apply on all outstanding tax debts established prior to the March remittance deadlines.

Businesses will still receive paper returns in the mail or web notice reminders by email for return periods March, April, May, June, July, and August.

Tax Appeals Commission Update (May 26, 2020)

If a taxpayer wants to appeal to the Tax Appeals Commission ("TAC") a Notice of Assessment issued after the state of emergency was declared on March 20, 2020, the 90-day period does not start until the earlier of September 21, 2020, or the end of the state of emergency. If the taxpayer or the Taxation Division want to appeal to the Court of Queen's Bench a decision rendered by the TAC after the state of emergency was declared on March 20, 2020, the 90-day period does not start until the earlier of September 21, 2020, or the end of the state of emergency.

New Brunswick

Property Tax Reduction Cancelled (May 27, 2020)

In light of the financial impact of the COVID-19 pandemic, the provincial government will not proceed with the proposed property tax reductions contained in the 2020–2021 Budget. In its Budget, the government had announced phased-in reductions to the provincial property tax on non-owner-occupied residential properties, often referred to as the double tax, and to non-residential properties.

Newfoundland and Labrador

Filing Deadlines

To provide continued support to businesses dealing with the COVID-19 pandemic, tax return filing deadlines have been further extended by two months until August 20, 2020. All tax returns, with the exception of tax returns required from interjurisdictional carriers, falling under the purview of the *Revenue Administration Act* and *Regulations*, which would otherwise be due March 20, 2020, to July 31, 2020, are now due August 20, 2020. The tax returns applicable to this extension include:

- Gasoline Tax
- Carbon Tax
- Health and Post-Secondary Education Tax
- Insurance Companies Tax
- Mining and Mineral Rights Tax
- Tax on Insurance Premiums
- Tobacco Tax

Monthly filers have the option to extend the filing and remittance of tax amounts for the February to June 2020 reporting periods to August 20, 2020.

To continue to file during the extension period, tax returns should be submitted via email to taxreturn@gov.nl.ca or faxed to 709-729-2856. Please email taxadmin@gov.nl.ca or call 709-729-6297 (toll free 1-877-729-6376) to set up electronic funds transfer, wire payment, or e-file payment options.

If online options are not possible, returns can be submitted via mail or by utilizing the drop-off box. The drop-off box is located in the East Block, Confederation Building in St. John's, and can be accessed via the Employee Entrance at the back of the building nearest to the daycare.

Anyone who avails themself of the extension and files each of the required returns on or before August 20, 2020, is advised that they must file each of the monthly returns as a separate filing at that time.

Ontario

Non-Resident Speculation Tax Update (May 20, 2020)

The Ministry of Finance understands that the effect of COVID-19 and the state of emergency could make it difficult for individuals who seek a Non-Resident Speculation Tax ("NRST") rebate to fulfil the condition that they occupy a property as their principal residence within 60 days after the date of purchase. Therefore, the Ministry will apply an administrative concession to extend the period of time within which a person must occupy a property as their principal residence for the purposes of an NRST rebate to 60 days after the final day of the state of emergency. The administrative concession will be applied only to purchases that have occurred from January 17, 2020, to the final day of the state of emergency. The administrative concession will not apply with respect to purchases that occurred on or before January 16, 2020, or purchases that occur after the state of emergency is no longer in effect. Rebates must be applied for within four years after the day on which the NRST became payable, except for the rebate for a foreign national who becomes a permanent resident of Canada. The rebate for a foreign national who becomes a permanent resident of Canada must be applied for within 90 days of the foreign national becoming a permanent resident, and no application may be made more than four years and 90 days from the date the NRST became payable. All rebate applications must be made using the Ontario Land Transfer Tax Refund/Rebate form for NRST.

Quebec

School Tax Rate To Decrease (June 10, 2020)

The government confirmed that it is moving ahead with the reduction of the single school tax rate, effective July 1, 2020. As a result, the school tax rate applicable to Quebec for the period from July 2020 to June 2021 will be set at $0.1054 per $100 of standardized property assessment.

Extended Health Services Fund Credit (May 29, 2020)

On May 29, 2020, the government announced that the credit on employers' contribution to the Health Services Fund in respect of employees on paid leave is extended until August 29, 2020. This change was made in response to the Canada Emergency Wage Subsidy ("CEWS") being extended to August 29, 2020.

Minister Granted Discretion To Extend Certain Time Limits (May 29, 2020)

On May 29, 2020, the government announced amendments to tax legislation to provide, in certain cases, a discretionary power to the Minister of Revenue to extend the time limit for applying for tax incentives intended for businesses.

Extension of Administrative Deadlines (June 1, 2020)

Revenu Québec has extended to September 1, 2020, most administrative deadlines that would normally fall in the period from June 1, 2020, to August 31, 2020. This extension does not apply to mandatory or preventive disclosures of aggressive tax planning or returns for which the deadline has already been extended to another specific date.

Partnership Return Deadline (June 1, 2020)

A partnership (including a SIFT partnership) that would normally have to file from May 31 to August 31, 2020, now has until September 1, 2020, to file.

Deadline for Corporate Tax Returns Extended (May 25, 2020)

Revenu Québec is extending the income tax return filing deadline for certain corporations to September 1, 2020. This new relief measure is for corporations that would have otherwise been required to file their income tax return between June 1 and August 31, 2020 (corporations whose taxation year ended between December 1, 2019, and February 29,

2020). In March 2020, Revenu Québec announced that corporations normally required to file their income tax return between March 17 and May 31, 2020, would have until June 1, 2020, to do so. The payment deadline for instalment payments and any income tax balance owing that would otherwise be due between March 17 and August 31, 2020, was extended to September 1, 2020, for both individuals and corporations.

Deadline for Trust Tax Returns Extended (May 25, 2020)

Revenu Québec is extending the information return and income tax return filing deadlines for certain trusts to September 1, 2020. This new relief measure is for trusts that would have otherwise been required to file their information return or income tax return between June 1 and August 31, 2020 (trusts whose taxation year ended between March 2 and May 31, 2020). In March 2020, Revenu Québec announced that trusts normally required to file their information return or income tax return between March 31 and May 31, 2020, would have until June 1, 2020, to do so.

CURRENT ITEMS OF INTEREST

Prescribed Interest Rates for Q3 (June 22, 2020)

The CRA announced the prescribed annual interest rates that will apply to any amounts owed to the CRA and to any amounts owed by the CRA to individuals and corporations. These rates will be in effect from July 1, 2020, to September 30, 2020. Many of the rates have decreased since the previous calendar quarter.

The income tax rates are as follows:

- The interest rate charged on overdue taxes, Canada Pension Plan contributions, and employment insurance premiums will be 5% (down from 6%).
- The interest rate to be paid on corporate taxpayer overpayments will be 1% (down from 2%).
- The interest rate to be paid on non-corporate taxpayer overpayments will be 3% (down from 4%).
- The interest rate used to calculate taxable benefits for employees and shareholders from interest-free and low-interest loans will be 1% (down from 2%).
- The interest rate for corporate taxpayers' pertinent loans or indebtedness will be 4.27% (down from 5.65%).

FOCUS ON CURRENT CASES

This is a regular monthly feature examining recent cases of special interest. This month's case reviews were provided by Joseph Frankovic of Toronto.

Director's Liability Arose When Corporation Failed To Remit Source Deductions; Spouse Jointly and Severally Liable

***The Queen v. Caroline Colitto*, 2020 DTC 5039 (Federal Court of Appeal)**

In *Colitto*, the taxpayer's spouse, Mr. Colitto, was a director of a corporation when the corporation failed to remit source deductions in 2008. The Canada Revenue Agency (the "CRA") took various actions under the *Income Tax Act* (the "Act") to collect these amounts from the corporation between 2008 and 2011. Ultimately, in 2011, a certificate for the amount of the corporation's liability was registered under section 223 of the Act, but execution for the amount was returned unsatisfied.

After the corporation's tax liability was executed and not satisfied, the CRA assessed Mr. Colitto under the directors' liability provisions of subsection 227.1(1). Generally speaking, under subsection 227.1(1), a director of a corporation is liable for the corporation's unremitted source deductions, subject to a due diligence provision and other conditions. Mr. Colitto did not fall within the due diligence provision, did not file a notice of objection, and apparently did not pay the tax assessed to him.

Subsequently, in 2016, the CRA assessed the taxpayer under the joint liability rules of subsection 160(1). That provision can apply where a person ("transferor") transfers property to the transferor's spouse for inadequate consideration. Mr. Colitto had transferred properties to the taxpayer in 2008 for inadequate consideration. Under subsection 160(1), the transferee spouse is jointly and severally liable with the transferor for the transferor's tax liability "in or in respect

of the taxation year in which the property was transferred or any preceding taxation year". The transferee's liability is limited to the amount by which the fair market value of the transferred property exceeds the consideration given for the property.

It was agreed that Mr. Colitto was liable to pay the corporation's unremitted source deductions by virtue of subsection 227.1(1). The only issue before the Federal Court of Appeal was whether his liability was in respect of 2008, when the corporation failed to remit the source deductions, or 2011, when the execution of the corporation's tax debt was returned unsatisfied. If his liability was in respect of 2008, the taxpayer was liable under subsection 160(1) because Mr. Colitto transferred the properties to her in that year. If his tax liability was in respect of 2011, the taxpayer was not liable because the transfer of properties took place in a prior year.

In the Tax Court of Canada decision (2019 DTC 1064), the trial judge held that the tax liability of Mr. Colitto was in respect of 2011. As such, the taxpayer was not liable under subsection 160(1). The trial judge based his decision largely on subsection 227.1(2), which provides that "a director is not liable under subsection 227.1(1) unless . . . a certificate for the amount of the corporation's liability referred to in that subsection has been registered . . . under section 223 and execution for that amount has been returned unsatisfied in whole or in part". According to the trial judge, subsection 227.1(1) is silent as to the timing of a director's liability. However, the clear and unambiguous language of subsection 227.1(2) suggests that a director's liability does not arise until the conditions in that provision are met. Since those conditions were met in 2011, Mr. Colitto's tax liability did not arise until 2011.

The Federal Court of Appeal (the "Federal Court") disagreed. The Federal Court held that subsection 227.1(1) is, at the least, ambiguous about timing. Moreover, subsection 227.1(2) is not a timing provision, but rather a relieving provision that sets out specified circumstances when the liability otherwise imposed by subsection 227.1(1) may be avoided. In particular, subsection 227.1(2) "does not state that a director is not liable for the corporation's default 'unless and until' the specified actions take place. This is the language that would be required to effect the result found by the Tax Court. The Tax Court impermissibly read the words 'and until' into subsection 227.1(2)."

More generally, the Federal Court held that the purpose of subsection 227.1(2) is to avoid double taxation, by prohibiting the CRA from recovering a corporation's unremitted source deductions from a director unless the corporation has failed to pay those amounts (e.g., unless the execution for the amounts has been returned unsatisfied). Furthermore, subsection 227.1(1) was "based on the presumption that a decision by a corporation to default on its remittance obligations would originate with the directors". The trial judge's interpretation of the provision would render that purpose "nugatory and pointless", as it would allow directors to re-arrange their affairs to avoid liability after the failed remittance.

Lastly, the Federal Court effectively overturned (or perhaps fine-tuned) a finding in the previous *McKinnon* case (2000 DTC 6593 (FCA)). In that case, the Court held that ". . . the liability of a director for unremitted source deductions and GST does not crystallize until the conditions prescribed in subsection 227.1(2) have been satisfied." The Federal Court in *Colitto* held that this comment was made *in obiter*, and therefore not binding as a matter of law. Additionally, the fact that a director may be required to pay a debt under subsection 227.1(1) only after collection efforts have been exhausted against the corporation is not inconsistent with the director's liability arising in or in respect of an earlier taxation year.

The Federal Court concluded that Mr. Colitto's liability arose in 2008. As a result, the taxpayer was jointly and severally liable for the amount assessed under subsection 160(1).

The *Colitto* decision is interesting mainly from a statutory interpretation perspective. The so-called plain meaning of subsections 227.1(1) and (2) might lead one to agree with the Tax Court decision. But considering the scheme of those provisions in particular and the Act in general, it is hard to quarrel with the Federal Court decision.

Receipt of Equity and Debt Capital by Foreign Affiliate Not "Investment Business"

***Loblaw Financial Holdings Inc. v. The Queen*, 2020 DTC 5040 (Federal Court of Appeal)**

In *Loblaw*, the Federal Court of Appeal allowed the taxpayer's appeal and overturned the previous Tax Court of Canada decision (2018 DTC 1128), which had held that the business income of the taxpayer's controlled foreign affiliate was foreign accrual property income ("FAPI") and therefore included in the taxpayer's income.

Under the *Income Tax Act* (the "Act"), the FAPI rules can apply where a controlled foreign affiliate of a Canadian resident taxpayer earns income from a business other than an "active business". An "investment business" is not an active business. However, a business is not an investment business if it is carried on by the foreign affiliate as a foreign

bank ("foreign bank exception") and certain other conditions are met (paragraphs (*a*), (*b*), and (*c*) of the definition of "investment business" in subsection 95(1) of the Act).

However, the foreign bank exception does not apply if the foreign affiliate's business is conducted principally with persons with whom the affiliate does not deal at arm's length (the "non-arms length exclusion"). In other words, where the non-arm's length exclusion applies to the foreign affiliate's business that is otherwise an investment business, the foreign bank exception does not apply, and the income from the business is FAPI.

The taxpayer, Loblaw Financial Holdings Inc., is resident in Canada and is an indirect wholly-owned subsidiary of Loblaw Companies Limited ("Loblaws"). In the taxation years in question, the taxpayer was the parent corporation of the Barbados subsidiary corporation Glenhuron Bank Limited ("GBL"). For purposes of the Act, both the taxpayer and GBL were related to, and therefore did not deal at arm's length with, Loblaws and various members of the Loblaws group of corporations (the "Loblaws Group"). Under Barbados law, GBL was a bank subject to Barbados international banking legislation.

In the taxation years in question, GBL engaged in various investment activities, including investments in short-term securities and interest-rate and currency swap contracts. It was accepted that the investment activities formed part of GBL's business. GBL earned significant income from these activities.

GBL was financed or "capitalized" prior to the taxation years with funds received from non-arm's length members of the Loblaws Group on the issuance of GBL shares and debt ("capitalized" is used tentatively here, since whether these receipts were capital or formed part of GBL's business was one of the main issues in the case). However, GBL's investments in the taxation years were made largely from GBL's retained earnings.

The only issue before the Federal Court of Appeal (the "Federal Court") was whether GBL's business was conducted principally with members of the Loblaws Group, and therefore with non-arm's length persons, so as to fall within the non-arm's length exclusion and outside of the foreign bank exception. If the non-arm's length exclusion applied, GBL's income from its business was FAPI. If it did not apply, GBL's income from its business was not FAPI.

The Federal Court (Woods, JA, speaking for the Court) overturned the Tax Court judge's decision that the non-arm's length exclusion applied. The Federal Court held that the Tax Court judge erred in at least two aspects.

First, the Federal Court disagreed with the trial judge's finding that GBL's receipts of equity and debt capital, being the "receipt of funds side" of its activities (the trial judge's term), formed part of GBL's business. The trial judge's finding in this regard was significant to his decision that the non-arm's length exclusion applied, since the receipts came entirely from non-arm's length members of the Loblaws Group. The Federal Court felt otherwise. The "capital invested by the Loblaw group" was not part of GBL's business, simply because GBL was not in the business of receiving such investments. As such, the receipts from the Loblaws Group were not relevant in determining whether GBL's business was conducted principally with non-arm's length persons. In making this determination, the Federal Court held that the meaning of "business" for the purposes of the Act was applicable, rather than the meaning of "business" under Barbados law.

The trial judge's decision on the "receipt side" of GBL's activities is difficult to rationalize. It appears that the judge relied largely on the definition of "international banking business" in the Barbados legislation that governed the activities of GBL at the time. Under that definition, an international banking business included, among other things, "the business of receiving foreign funds" through various means. Apparently, the trial judge felt that since GBL received foreign funds from the Loblaws group, those receipts formed part of GBL's business. However, the Barbados legislative definition referred to the "business" of receiving foreign funds; it did not define or deem the receiving of foreign funds to be a business. In other words, the trial judge put the cart before the horse, so to speak. In any event, as noted above, the Federal Court held that Barbados law was not relevant in determining whether GBL was conducting business.

At this point, the Federal Court was on solid ground in dismissing the trial judge's finding on the "receipt side" issue. It is unfortunate that the Federal Court took a tangential turn regarding the meaning of "banking" in order to (apparently) bolster its finding on the issue. The Federal Court referred to the Supreme Court of Canada decision in *Canadian Pioneer Management Ltd. v. Labour Relations Board of Saskatchewan* ([1980] 1 S.C.R. 433) in concluding that the meaning of banking "should be based on a formal, institutional approach rather than a substantive approach, in the sense of the functions of banking. It follows that the use of the term 'bank' in the name of the entity, and whether it is regulated, are factors to be considered, *rather than the actual activities that are conducted*." (Emphasis added.) Based on the formal, institutional approach of *Canadian Pioneer*, the Federal Court felt that "there is no reasonable basis to conclude that the arm's length test requires both business receipts and uses."

There are at least a couple of problems with the Federal Court's conclusion as to "banking". First, the "actual activities

that are conducted" by a foreign affiliate are surely relevant in determining whether it is conducting an investment business or whether its business is conducted with non-arm's length persons. (Not to mention that "banking" involves the receipts of funds?) Second, in *Canadian Pioneer*, a constitutional law case, the issue was whether a trust company was engaged in banking so as to come within federal jurisdiction over banks and "banking" under subsection 91(15) of the *British North America Act*. Essentially, the Supreme Court in *Canadian Pioneer* held that "banking" for these purposes applied to banks and their activities, and not to trust companies that carried on similar activities. It is difficult to see how the "formal, institutional" reasoning that was applied in *Canadian Pioneer* for constitutional law purposes has anything to do with the rationale underlying the non-arm's length exclusion. The Federal Court engaged in a classic exercise of conflating the purposes and objectives of one area of law with another, and an unnecessary one at that.

On the "receipt side", the trial judge's decision in *Loblaw* also focused on an element of competitiveness. The trial judge felt that ". . . in looking at both aspects of a foreign bank's business, the receipt of funds and use of funds, there should be emphasis on the receipt side as that is where one would expect to find the competition element . . . It remains to determine whether GBL, in all aspects of the conduct of business, though with an emphasis on its competitiveness . . . dealt primarily with non-arm's length persons." The judge went on to hold that the receipt side of GBL's business involved no competition.

The competition argument is difficult to comprehend. The trial judge felt that the receipt side is where one would expect most of the competition, so that emphasis should be placed on the receipt side. But the judge concluded there was no competition on the receipt side, and went on to emphasize it anyway. Regardless, the Federal Court dismissed the trial judge's analysis on this point, holding that Parliament has not explicitly required competition as an element of the foreign bank exception.

Turning to the "use of funds side" of GBL's activities (again, the trial judge's term), namely its investment activities, the trial judge was not satisfied "that even the use of funds side of the conduct of banking business was not principally conducting business with non-arm's length persons." The Federal Court also overturned this aspect of the trial decision. The Federal Court held that GBL's investments in short-term securities and interest-rate and currency swaps were conducted entirely with arm's length parties. The fact that the non-arm's length taxpayer may have "provided direction, support and oversight" to GBL with respect to these investments was not particularly relevant: "Parliament could not have intended that the foreign bank exclusion should be denied as a result of support and oversight provided by a parent corporation."

Lastly, although GBL engaged in other investment activities, the Federal Court held that its main business consisted of the investments in short-term securities and interest-rate and currency swaps, such that the other investments did not affect the application of the foreign bank exception.

In summary, the Federal Court concluded that GBL's business of investing was not conducted principally with non-arm's length parties. As such, the foreign bank exception applied and GBL's income from the business was not FAPI.

RECENT CASES

Corporate taxpayer not under audit, but still required to furnish Minister with identity of its customers and details of its transactions with those customers

Roofmart was a large supplier of roofing and building materials. The Minister obtained from the Federal Court an unnamed persons requirement order (the "UPR") under subsection 231.2(3) of the *Income Tax Act* (the "ITA") and its equivalent subsection 289(3) of the *Excise Tax Act* (the "ETA"). This order required Roofmart to supply to the Minister particulars concerning, among other things, the identity of its customers and the details of its transactions with those customers. Roofmart itself was not under tax audit at the time. On its appeal to the Federal Court of Appeal, Roofmart argued that: (a) the Minister's application for the UPR was *ultra vires* because it was not brought by a person authorized by statute to do so; (b) the Federal Court judge erred in applying the relevant statutory criteria, and in particular in finding that the unnamed persons mentioned in the UPR were "ascertainable" within the meaning of subsections 231.2(3) of the ITA and 289(3) of the ETA; and (c) the Federal Court judge applied the incorrect burden of proof to his assessment of the Minister's application.

Roofmart's appeal was dismissed. There was no merit in Roofmart's arguments. The application in this case was brought by the Minister, and not by the CRA official who swore the affidavit in support of the UPR application, as the taxpayer had contended. Also, there was ample evidence to justify the Federal Court's conclusion that the unnamed persons mentioned in the Court's order were ascertainable, and, finally, the Minister did meet the high standard of proof required in this case. The jurisprudence on which the taxpayer had applied was from a different era when UPR applications were made *ex parte*, which is no longer the case. Accordingly, the taxpayer's contention that the *ex parte* standard of disclosure should still apply in this case because UPR orders are intrusive was untenable. Finally, when a court of appeal is faced with the exercise of discretion by a lower court judge it must be cautious in intervening, only doing so where it is established that the discretion was exercised in an abusive, unreasonable, or non-judicial manner (see *Minister of National Revenue v. Rona Inc.*, 2017 DTC 5069 (FCA)). In the present proceedings, the Federal Court judge made no error in the exercise of his discretion.

Roofmart Ontario Inc. v. Canada (MNR)

2020 DTC 5046

Foreign exchange transactions did not give rise to tax benefit for corporate taxpayer; Minister's GAAR assessment set aside accordingly

The corporate taxpayer BMO undertook certain transactions to reduce its foreign exchange risk in financing its US subsidiaries. As part of these transactions, BMO was a limited partner in a Nevada limited partnership (the "limited partnership"), which acquired the shares of a Nova Scotia unlimited liability company ("NSULC"). Because of the increase in value of the Canadian dollar in relation to the American dollar, BMO suffered a loss on the limited partnership's ultimate disposition in 2010 of its shares of NSULC. To avoid the possible application of subsection 112(3.1) of the *Income Tax Act* (the "Act") (which, if it had applied, would have reduced the limited partnership's capital loss on the disposition of its NSULC shares by the amount of the dividends that were paid to it by NSULC), the limited partnership acquired a separate class of shares on which dividends were paid. The Minister reassessed BMO on the basis that the GAAR applied to the transactions undertaken to avoid the reduction in the capital loss contemplated by subsection 112(3.1). In allowing BMO's appeal (2018 DTC 1131), the Tax Court of Canada concluded that: (a) the loss realized by BMO on the limited partnership's disposition of its shares of NSULC was deemed under subsection 39(2) of the Act to be a loss from the disposition of a foreign currency, and not a loss from the disposition of shares; (b) as a result the provisions of subsection 112(3.1) would not have applied to reduce the loss by the amount of the dividends paid even if only one class of shares had been issued; and (c) no tax benefit was realized by BMO in completing the transactions to avoid the possible application of subsection 112(3.1). The Crown appealed to the Federal Court of Appeal.

The Crown's appeal was dismissed. A textual, contextual, and purposive analysis confirmed that the Tax Court judge was correct in his interpretation of subsection 39(2) of the Act as it read in 2010. Accordingly, the loss realized by BMO as a result of the limited partnership's disposition of its shares of NSULC was deemed to be a loss from the disposition of a foreign currency. This loss would not have been reduced under subsection 112(3.1) even if only one class of shares had been issued by NSULC. Hence, no tax benefit was realized in this case.

BMO v. The Queen

2020 DTC 5043

Appellant Foundation entitled to additional disclosure from Minister

The appellant Foundation appealed to the Federal Court of Appeal from the Minister's refusal to register it as a Canadian amateur athletic association. In response to the Foundation's request, the Minister sent it a Tribunal Record, with certain redactions made on the bases of solicitor-client privilege, and of confidential personal or third-party information. When the parties reached an impasse concerning the redactions, the Minister brought a motion for a confidentiality order in relation to the redacted information.

The Minister's motion was granted in part. Rules 317 and 318 of the *Federal Courts Rules* provide that, absent a recognized exception, a party is entitled to receive everything that the decision maker had before it when it made its decision (see *Canadian National Railway Company v. Canada (Transportation Agency*), 2019 FCA 257). In the present proceedings, the issues were: (1) whether the redactions should continue to be treated confidentially; and (2) whether the Court should order further disclosure by the Minister. The Foundation conceded that the test for *res judicata* or issue estoppel was met for the Minister's redactions based on solicitor-client privilege, so that those redactions should be maintained. However, the Minister should be required to produce any material apart from that already disclosed that was before her when her decision was made, with the exception of properly redacted information.

Athletes 4 Athletes Foundation v. Canada (MNR)

2020 DTC 5041

Crown's statutory trust for GST owing by corporate taxpayer took precedence over appellant bank's interest as a secured creditor of the taxpayer

In 2007 and 2008, before he became a customer of the appellant bank (the "Bank"), the taxpayer collected but failed to remit GST in relation to his landscaping business. In 2010, the Bank granted the taxpayer a line of credit secured by a charge in the Bank's favour against a property owned by him (the "Property"). At that time, the Bank was not aware of any GST owing by the taxpayer. In 2011, the taxpayer sold the Property and paid out the line of credit with the Bank. The CRA subsequently asserted a deemed trust claim under section 222 of the *Excise Tax Act* against the Bank. Upon the Bank's refusal to pay that claim, the Crown commenced an action against the Bank in the Federal Court to recover the portion of proceeds of the taxpayer's sale of the Property caught by the Crown's section 222 deemed trust GST claim. This action was allowed (2018 GTC 1020 (FC)) and the Bank appealed to the Federal Court of Appeal.

The Bank's appeal was dismissed. The Court of Appeal defined the issues to be whether the Federal Court erred: (a) in finding that the deemed trust did not a require a triggering event causing the trust to crystallize; (b) in finding that secured creditors cannot avail themselves of the *bona fide* purchaser for value defence in cases such as this one; and (c) in failing to consider that the security interests of the Bank were not created and granted in a transaction providing financing to the debtor's business. The Court of Appeal decided all of these issues against the Bank, noting that: (a) when the Bank lent money to the taxpayer and took its security interests, the taxpayer's property to the extent of the tax debt was already deemed to be beneficially owned by the Crown (see subsection 222(3) of the *Excise Tax Act*); (b) secured lenders, however, are not without some ability to manage the risk posed by statutory deemed trusts; and (c) these lenders can require borrowers either to give evidence of tax compliance, or to authorize the CRA to provide such evidence concerning the borrower. In the FCA's view, Parliament made a considered policy choice to prioritize protection of the fisc over the interests of secured creditors. Parliament tempered the potential harshness of this choice by providing for prescribed security interests by waiving the Crown's deemed trust rights in cases of bankruptcy and arrangements under the *Companies' Creditors Arrangement Act*. The foregoing analysis led to the conclusion that the Federal Court made no error in this case warranting appellate intervention.

TD Bank v. The Queen

2020 DTC 5042

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