Docket: 2002-479(IT)G
2002-4202(IT)G

BETWEEN:

UNIVAR CANADA LTD.,
(formerly Vopak Canada Ltd.
Van Waters & Rogers Ltd.)

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on May 9, 2005 at Vancouver, British Columbia

Before: The Honourable Justice R.D. Bell

Appearances:

Counsel for the Appellant:	Mr. E. Kroft Ms. E. Junkin **Ms. Stacey Sloan**
Counsel for the Respondent:	Mr. L. Chambers, Q.C. Mr. R. Carvalho

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AMENDED JUDGMENT

The appeal from the six August 9, 2002 reassessments made under Part I of the *Income Tax Act* with respect to the following taxation years is allowed and the reassessments are referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with the attached Reasons for Judgment:

(1) taxation year ended February 29, 1996;

(2) taxation year ended July 15, 1996;

(3) taxation year ended December 31, 1996;

(4) 1997 taxation year;

(5) 1998 taxation year;

(6) 1999 taxation year;

The appeal from the September 3, 2002 reassessment for a penalty under subsection 162(1) for failure to file a return of income as and when required for the taxation year ended July 15, 1996, is allowed and the penalty is deleted.

The appeal from the August 6, 2001 reassessment of Part XIII tax for the 1995 taxation year is allowed in accordance with the attached Reasons for Judgment.

This Amended Judgment is issued in substitution of the Amended Judgment dated November 4, 2005.

Signed at Ottawa, Canada, this **12th** day of **December** 2005.

"R.D. Bell"

Bell, J.

Citation:2005TCC723
Date: 20051103
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2002-4202(IT)G

BETWEEN:

UNIVAR CANADA LTD.,
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Appellant,

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Respondent.

REASONS FOR JUDGMENT

Bell, J.

General

The statutory provisions referred to herein are all in reference to the *Income Tax Act* ("Act") unless otherwise stated.

ISSUES

I. In respect of the six August 9, 2002 reassessments ("six reassessments") of the Appellant for the following taxation years, namely:

1. taxation year ended February 29, 1996

2. taxation year ended July 15, 1996

3. taxation year ended December 31, 1996

4. 1997 taxation year

5. 1998 taxation year

6. 1999 taxation year

could it be reasonably be considered that the principal purpose for the acquisition by the Appellant of shares of Van Waters & Rogers (Barbadosco) Ltd. ("Barbadosco") was to permit the Appellant to avoid, reduce or defer the payment of tax that would otherwise be payable under the *Act* within the meaning of paragraph 95(6)(*b*) with the result that:

(a) Barbadosco would not be a foreign affiliate of the Appellant, and, therefore

(b) dividends received by the Appellant from Barbadosco would not be deductible under subsection 113(1)?

II. Alternatively,

(a) respecting the six reassessments,

(i) was there an "avoidance transaction" (subsection 245(3)), and, if so

(ii) by virtue of subsection 245(4) does subsection 245(2) not apply in that it may reasonably be considered that the transaction did not result directly or indirectly in

(i) a misuse of clause 95(2)(*a*)(ii)(A), respecting Part I tax,

or

(ii) an abuse having regard to the provisions of the *Act* read as a whole?

(b) respecting the August 6, 2001 reassessment for non-resident tax under Part XIII for the 1995 taxation year,

(i) was there an "avoidance transaction" (subsection 245(3)), and, if so

(ii) by virtue of subsection 245(4) does subsection 245(2) not apply in that it may reasonably be considered that the transaction did not result in

(i) a misuse of subsection 15(2.2) respecting Part XIII tax, or

(ii) an abuse having regard to the provisions of the *Act* read as a whole?

III. Was the September 3, 2002 reassessment for the taxation year ended July 15, 1996 respecting a penalty under subsection 162(1) for failure to file a return of income as and when required and respecting the underlying tax, stature barred, having been made after the expiration of the normal reassessment period?

CONCLUSIONS

I have concluded that:

I. With respect to the six reassessments, it cannot, under paragraph 95(6)(*b*) reasonably be considered that the principal purpose for the acquisition of the shares of Barbadosco was to permit the Appellant to avoid, reduce or defer the payment of tax or any other amount that would otherwise be payable under the *Act*.

II. With respect to the six reassessments, there was no avoidance transaction within the meaning of subsection 245(3).

III. With respect to the August 6, 2001 reassessment there was no avoidance transaction within the subsection of 245(3).

IV. With respect to the September 3, 2002 reassessment for a penalty under subsection 162(1), the appeal will be allowed.

REASSESSMENTS

For ease of understanding the reassessments the attached Appendix A showing transactions should be consulted.

[1] The Minister of National Revenue ("Minister") issued original Notices of Assessment to the Appellant in respect of three 1996 taxation years (there having been three year-ends in that calendar year), and in respect of the 1997, 1998 and 1999 taxation years. For each of those taxation years, the Appellant included in its income dividends from Barbadosco and, pursuant to the provisions of subsection 113(1), deducted an equivalent amount.

[2] On September 7, 2001 the Minister reassessed the Appellant for those six taxation years by adding, in each such year, an amount described as:

> Interest Income from Univar Europe N.V.

No other adjustments to income having been made, it is apparent that the Minister simply added the aforesaid amounts characterized as interest, making no reference to the former dividend income inclusion and corresponding deduction. Each of the Notices of Reassessment bears the endorsement:

> Section 245 of the Income Tax Act is a position related to this assessment.

Unfortunately, as is mostly the case, the Minister neglects to include a statement of the basis of reassessment. Subsequent information confirmed that the Minister's basis for same was section 245.

[3] On August 9, 2002, the Minister again reassessed the Appellant for those six taxation years. Each Notice of Reassessment bears the following:

> Adjustments to Active Business Income
>
> Deduct:
> Interest income previously assessed.

A notation on each such Notice of Reassessment reads as follows:

> The section 113 dividend deduction previously allowed, is now denied pursuant to subsection 95(6) of the Act.
>
> In the alternative, section 245 applies to include in income of Univar Canada Ltd. interest received by Van Waters & Rogers (Barbados) Ltd. from loans made to various non-Canadian companies.

As set out later, Barbadosco did not make such loans. It simply purchased the debt owed by those companies to UC.

[4] On August 6, 2001 the Minister issued a Notice of Reassessment cancelling and replacing a Notice of Assessment dated July 25, 2001 for the Appellant's 1995 taxation year. The endorsement on the Notice of Reassessment reads as follows:

> This "Notice of Reassessment" cancels and replaces "Notice of Assessment" No. 6161436 dated July 25, 2001. You had to deduct and remit $232,201.00 of non-resident Part XIII tax on amounts paid or credited to non-resident(s) of Canada.
> As a result of this decrease, we have adjusted the arrears balance accordingly.
> We charge interest at the prescribed rate on the unpaid balance.

This reassessment appears to have arisen from the Minister's view of recharacterizing the within transactions to effect an assessment as a result of sections 15, 212, 214 and 215. Respondent's counsel stated that:

> The tax benefit was Univar Europe's avoidance of its liability to pay, and the Appellant's liability to deduct or withhold and remit to the Receiver General of Canada, the tax imposed on the indebtedness arising between Univar Europe and VWRB under Part XIII of the Income Tax Act, in particular, by a combination of subsections 15(2), 15(2.1), 15(2.2), 212(2), 214(3), 215(1) and 215(6) of the Act.

[5] On September 3, 2002, the Minister reassessed the Appellant for its taxation year ending July 15, 1996 consisting of, in the words of the SUMMARY OF REASSESSMENT:

Penalties:	Net balance
Subsection 162(1) late-filing penalty	$27,351.10

This was the third reassessment for this taxation year.

The second reassessment dated August 9, 2002 stated:

> We have cancelled the late-filing penalty previously assessed under subsection 162(1) of the Income Tax Act.

This penalty is computed as a percentage of tax payable.

The first reassessment dated September 7, 2001 reassessed a late-filing penalty under subsection 162(1).

GENERAL

[6] The parties submitted an AGREED STATEMENT OF FACTS with five charts showing companies in the international Univar group of corporations appended ("UC Group"). Those charts used several historical names of some companies[1] rendering the corporate structure difficult to comprehend. In addition, although I sought, at the beginning of the hearing, to gain agreement on the use only of the ultimate changed name and of a simple chart setting out readily identifiable names and the important facts, neither that chart nor those names were used at the hearing. To avoid reader confusion or early loss of interest I set forth a chart as Appendix A hereto and forming part of these Reasons virtually identical to that I presented in Court. It encapsules the corporate structure and the basic transaction facts in readily comprehensible fashion.

[7] The Court has no control over some aspects of the preparation and presentation of a case. However, some comments in respect of this appeal may be of assistance to counsel generally.

[8] The Minister of National Revenue ("Minister") followed unusual assessing procedures in this matter. As set forth under REASSESSMENTS the Minister's first reassessment of six of the Appellant's taxation years, adding interest to its income, was based on section 245. The second reassessment, disallowing the subsection 113(1) dividend deduction, was based upon subsection 95(6) and, in the alternative, on section 245. Two other Notices of Reassessment were issued. One assessed a non-resident Part XIII tax for the Appellant's 1995 taxation year. The other assessed a penalty for one of the Appellant's three 1996 taxation years.

[9] The Appellant filed a Notice of Appeal respecting the aforesaid first reassessments and the withholding tax assessment. Then it filed another Notice of Appeal in respect of a second reassessment of the six taxation years and the late filing penalty reassessment. Obviously, the second reassessments, disallowing the subsection 113(1) deduction for those six taxation years, replaced the first reassessments in respect of those years. However, the Part XIII tax reassessment for 1995 contained in the first Notice of Appeal survived and had to be addressed in Court.

[1] Univar is the third of the Appellant's three different names.

[10] The first Notice of Appeal contained 90 paragraphs, a substantial number of which were unnecessary. The form of Notice of Appeal prescribed by the General Procedure Rules requires that the Appellant relate the material facts relied on, specify the issues to be decided, refer to the statutory provisions relied on and set forth the reasons upon which the Appellant intends to rely. The Reply to that Notice of Appeal, although containing only 42 paragraphs, was not succinct and to the point.

[11] The second Notice of Appeal, containing 72 paragraphs, also lacked brevity and conciseness. The Reply containing 47 paragraphs suffered similarly.

[12] I raise these matters as a prelude to my statement that the content of the appeals and the reason for the continued existence of two Notices of Appeal was not clearly stated. In addition, the issues were not succinctly and clearly presented. Indeed, at the opening of the hearing, I sought agreement on the issues. I prepared a summary of what I perceived to be the issues and furnished counsel with same. It was not until the end of the ninth day of the hearing that an agreement on the issues was reached.

[13] A brief statement of what was in issue from each Notice of Appeal, a brief description of the reassessments and a brief description of the issues all could have been made by a co-operative act of counsel before the hearing, thus saving hours and hours of unnecessary search for comprehension of unfurnished detail. Further, the transcript of evidence consisting of nine thick volumes totalled 2,053 pages. The Appellant entered five thick volumes of documents and three volumes of "read-ins" of the manager of GAAR and Technical Support Section of the Canada Revenue Agency. The Appellant entered eleven volumes of documents as exhibits. The Appellant's written submission was a tome of 217 pages. Admittedly, there were a great number of references to the transcript respecting certain facts and statements. The Appellant's oral submission took the better part of one and one-half days. The Respondent's written submission consisted of 52 pages with 163 paragraphs.

[14] This case is complex. I understand counsel wanting to be certain that all facts which may be relevant be placed before the Court. However, better selection and precision in preparation would have made the presentation of evidence and submissions much shorter.

FACTS

[15] The details of the reassessments have already been presented. I now set forth a summary of the facts upon which my conclusions are based. Those facts, together with related facts, all in great detail, are set forth in Appendix B attached to and forming part of these Reasons for Judgment. They include the Agreed Statement of Facts filed by counsel and a presentation of the evidence of three of the Appellant's witnesses.

[16] The Appellant primarily carried on the business of industrial and agricultural chemical processing and distribution. Pruitt described Univar as a component that represented "maybe 15 to 20 percent of the entire UC conglomerate. This being a seasonal business, it regularly financed payments to suppliers of agricultural chemicals during the summer months and received payment after harvest.

[17] The UC Group policy was not to pay dividends. Only one dividend was paid by the Appellant to UC, that being the amount of approximately $6,000,000 in 1980.

[18] In the early 1990s the Appellant and the UC Group were facing a number of related and distinct problems.

<u>Excess Cash</u>

[19] The Appellant had excess cash from increasingly profitable operations and a strong balance sheet. It tried, to the fullest extent possible, to maximize monetary returns through various acquisitions or investments. It used some of its excess cash to fund acquisitions and the expansion of business operations. It expected the generation of excess cash to escalate, thereby resulting in serious treasury management issues. There were no further acquisition opportunities available after those made in the 1991 to 1993 period. The Appellant undertook to identify long-term investment opportunities that would produce a higher rate of return than the interest rate on Canadian Bankers' Acceptance Notes.

<u>Leverage</u>

[20] Pruitt, the Chief Executive Officer of UC at the time of the transactions herein, believed that a company's debt to equity ratio should be one to one in that if the business was under-leveraged (i.e., too little debt) it was not fully utilizing its capital. The Appellant's debt to equity ratio was significantly below the ideal ratio. Pruitt described it as "woefully" under-leveraged. Pruitt testified that one way of improving the ratio was for the company to borrow against its available capital to make

investments that had a rate of return in excess of the interest rate on the fund borrowed.

Guarantee Fee Issue

[21] In the 1989 through 1992 fiscal years UC and its wholly owned US subsidiary, the operating company, were borrowers under the 1989 Credit Agreement in respect of which the Appellant was the sole guarantor. As a result of the Appellant's guarantee the Minister reassessed the Appellant for its 1989 to 1992 taxation years to include in its income an amount for providing a guarantee of the obligations of UC. That issue was resolved, but not until September, 1996. In the 1992 to 1995 fiscal years UC and some members of the Group, including the Appellant, were borrowers under another credit arrangement, the Appellant being an authorized borrower and jointly and severally liable for the obligations of each. Pruitt and Lundberg testified that although this should have eliminated the Appellant's exposure to income inclusion, both the Appellant and UC continue to be concerned that the Minister would pursue this issue.

[22] As a result of the Appellant's status as a guarantor of the 1989 Credit Agreement and joint and several liability of the 1992 Credit Agreement, the law firm, Baker McKenzie, advised UC that it had a problem under Internal Revenue Code provision 956. The advice was that it would deem UC to have received, as a dividend, on most, if not all, of the Appellant's earnings and related deemed taxes.

Debt Within the Group

[23] In June 1991 UE borrowed funds from its shareholders and loaned the proceeds of those loans to the UK and Swedish operating companies. Some loans were interest bearing and others non-interest bearing. As a result, UC was holding a disproportionate amount of the Group's debt and was looking for strategies where it could equalize the debt to equity ratios throughout the Group as a whole.

Other Issues

[24] The aforesaid guarantee arrangements created American tax issues for UC involving the application of US foreign tax credit rules and limitations on their use. Those limitations created "excess foreign tax credits" subject to a two year carry-back and five year carry-forward life. They could be used only to the extent of "qualifying foreign source income", the ability to earn same being dependent on "overall foreign loss". The "overall foreign loss" was a significant deterrent to the use of foreign tax credits by UC. Lundberg was preoccupied with resolving UC's excess foreign tax credit issues.

[25] In addition, there were too many tiers of Group in Europe which created US tax problems, the result of which was that the operating companies had to be consolidated.

[26] In the early 1990s the Appellant and UC explored alternative investment strategies to address the foregoing problems. In early 1993, based on professional advice, Pruitt proposed and the Group decided to implement the following sequence of events as an integrated solution to the problems which, over a two-year period, evolved into the following:

(a) The number of tiers within the Group in Europe would be reduced.

(b) A greater amount of the European loans would be restructured into interest bearing obligations so the operating companies would bear their proportionate amount of the Group's debt and the notes receivable would become an attractive investment.

(c) The Appellant and UE would enter into a Multi-Currency Line of Credit.

(d) The Appellant would establish and capitalize an international financing subsidiary in a jurisdiction which had a corporate tax rate of less than 90 percent of the prevailing US corporate federal tax rate and would have no existed retained earnings or profits (“NEWCO”).

(e) NEWCO would purchase the notes receivable from UC, earn interest income thereon and pay dividends to the Appellant.

(f) The Appellant would use a combination of excess cash and borrowed funds to capitalize NEWCO and thereby improve its debt to equity ratio while still generating a good return on its investment, and

(g) These solutions would also address a number of American tax issues.

[27] The Appellant performed due diligence to ensure that the integrated solution was in its best interests. Canadian tax issues were reviewed as part of its due diligence. The Appellant determined that the investment in Barbadosco would be economically viable and generate a reasonable return. Tole characterized the integrated solution as an “elegant solution”.

[28] Barbados was suggested, and ultimately chosen, over a number of other countries, as the jurisdiction in which to incorporate NEWCO because of the low corporate tax rate and all the necessary corporate, legal and banking requirements already extant due to the presence of many international financing corporations.

[29] The integrated solution was implemented. UE would then pay interest to Barbadosco which, after tax and administrative costs, would pay the remainder, as a dividend, to the Appellant. The interest to Barbados would be active business income and the Appellant would, accordingly, be entitled to deduct the appropriate amount pursuant to paragraph 113(1)(*a*).

[30] I reiterate that the evidence of Pruitt, Lundberg and Tole was clear that no consideration was ever given to the Appellant acquiring the notes receivable itself because that would not have resolved any problem.

ANALYSIS

Applicable Statutory Provisions

[31] In issuing the six reassessments (other than the subsection 162(1) penalty reassessment) the Minister relied upon subsection 95(6)(*b*). It reads as follows:

> **95(6) Where rights or shares issued, acquired or disposed of to avoid tax** – For the purposes of this subdivision (other than section 90),
>
> (b) where a person or partnership acquires or disposes of shares of the capital stock of a corporation, either directly or indirectly, and it can reasonably be considered that the principal purpose for the acquisition or disposition of the shares is to permit a person to avoid, reduce or defer the payment of tax or any other amount that would otherwise be payable under this Act, those shares shall be deemed not to have been acquired or disposed of, as the case may be, and where the shares were unissued by the corporation immediately prior to the acquisition, those shares shall be deemed not to have been issued.

The Minister's alternative argument respected the application of section 245, reading as follows:

> **245.**(1) [Definitions] In this section,
>
> "tax benefit" means a reduction, avoidance or deferral of tax or other amount payable under this Act or an increase in a refund of tax or other amount under this Act;
>
> "transaction" includes an arrangement or event.
>
> (2) [General anti-avoidance provision] Where a transaction is an avoidance transaction, the tax consequences to a person shall be determined as is reasonable in the circumstances in order to deny a tax benefit that, but for this section, would result, directly or indirectly, from that transaction or from a series of transactions that includes that transaction.
>
> (3) [Avoidance transaction] An avoidance transaction means any transaction

(*a*) that, but for this section, would result, directly or indirectly, in a tax benefit, unless the transaction may reasonably be considered to have been undertaken or arranged primarily for bona fide purposes other than to obtain the tax benefit; or

(*b*) that is part of a series of transactions, which series, but for this section, would result, directly or indirectly, in a tax benefit, unless the transaction may reasonably be considered to have been undertaken or arranged primarily for bona fide purposes other than to obtain the tax benefit.

(4) [Where s. (2) does not apply] For greater certainty, subsection 245(2) does not apply to a transaction where it may reasonably be considered that the transaction would not result directly or indirectly in a misuse of the provisions of this Act or an abuse having regard to the provisions of this Act, other than this section, read as a whole.

(5) [Determination of tax consequences] Without restricting the generality of subsection 245(2),

(*a*) any deduction in computing income, taxable income, taxable income earned in Canada or tax payable or any part thereof may be allowed or disallowed in whole or in part,

(*b*) any such deduction, any income, loss or other amount or part thereof may be allocated to any person,

(*c*) the nature of any payment or other amount may be recharacterized, and

(*d*) the tax effects that would otherwise result from the application of other provisions of this Act may be ignored,

in determining the tax consequences to a person as is reasonable in the circumstances in order to deny a tax benefit that would, but for this section, result, directly or indirectly, from an avoidance transaction.

I now set forth in table form, the comparative steps for analysis of the two aforesaid sections in relation to the facts of this case:

Subsection 95(6)	Section 245
(a) acquisition of shares of Barbadosco.	(a) a "transaction" which includes an

	arrangement or event.
(b) did the acquisition permit a person to avoid, reduce or defer payment of that "that would otherwise be payable"?	(b) did the transaction result in a "tax benefit" which "means a reduction, avoidance or deferral of tax…"
(c) can it reasonably be considered that the *principal* purpose for the acquisition is to so avoid, reduce or defer tax otherwise payable?	(c) would the transaction be an "avoidance transaction" and can it reasonably be considered to have been undertaken or arranged *primarily* for *bona fide* purposes other than to so reduce, avoid or defer a tax benefit?
	(d) if there is an "avoidance transaction" can it reasonably be considered that it would result in a misuse of the provisions of the Act or an abuse having regard to the provisions of the Act, other than section 245, read as a whole?

Respecting the penalty reassessment, subsection 162(1) reads:

> Every person who fails to file a return of income for a taxation year as and when required by subsection 150(1) is liable to a penalty equal to the total of
>
> (a percentage formula follows)

Respecting the Minister's ability to reassess the penalty subparagraph 152(4)(*b*)(iii) reads:

> The Minister may at any time make an assessment, reassessment or additional assessment of tax for a taxation year, interest or penalties, if any, payable under this Part by a taxpayer or notify in writing any person by whom a return of income for a taxation year has been filed that no tax is payable for the year, except that an assessment, reassessment or additional assessment may be made after the taxpayer's normal reassessment period in respect of the year only if …
>
> (b) the assessment, reassessment or additional assessment is made before the day that is 3 years after the end of the normal reassessment period for the taxpayer in respect of the year and…
>
> (iii) is made as a consequence of a transaction involving the taxpayer and a non-resident person with whom the taxpayer was not dealing at arm's length.

Tax Benefit

[32] Essentially, the tax "that would otherwise be payable" referred to in paragraph 95(6)(*b*) is equivalent to the "tax benefit" under section 245.

[33] This is not a situation in which tax payable by Univar is reduced, avoided or deferred by any transaction that is part of a series of transactions.

[34] In *McNichol v. HMQ* 97 D.T.C. 111 this Court said at page 119:

> There is nothing mysterious about the subsection 245(1) concept of tax benefit. Clearly a reduction or avoidance of tax does require the identification in any given set of circumstances of a *norm* or *standard* against which reduction is to be measured.
>
> (Emphasis added.)

[35] In that case the termination of a corporation's affairs was desired. The relevant parties sought a distribution of its funds in a manner other than by way of dividend. That manner resulted in an arrangement producing capital gains taxed, because of capital gains exemptions, in an amount appreciably less than otherwise would have occurred. The above continued as follows:

> Difficulties may exist in other cases in identifying the standard but in this case there is no such difficulty. The benefit sought by the appellants is clearly identified in the March 16, 1989 letter of Mr. Dunnett. It is the difference between tax payable by the appellants upon receipt of taxable dividends and that payable upon realization of capital gains from the disposition of shares. It is beside the point that such benefit may also be described as the absence of a detriment. It cannot be said that the standard against which reduction is to be measured is nil on the basis that, absent a sale of shares, no tax would have been payable. For the appellants doing nothing was never in the realm of the possible, for their goal, present throughout, was the realization of the economic value of their shares…Their choice was between distribution of that accumulated surplus by way of liquidating dividend and sale of the shares and in choosing the latter they chose a transaction that resulted in a tax benefit within the subsection 245(1) definition.

[36] In *Canada Trustco*, 2005 SCC 54 the Supreme Court of Canada said:

> Whether a tax benefit exists is a factual determination, initially by the Minister and on review by the courts, usually the Tax Court.

The Court said further that in some instances:

> …it may be that the existence of a tax benefit can only be established by comparison with an alternative arrangement.

[37] Throughout the appeal, the Respondent's cross-examination of Pruitt, Lundberg and Tole and the Respondent's submissions clung to the hypothetical situation of the Appellant having acquired the debt owing by UE to UC as "an alternative arrangement". Each of Pruitt, Lundberg and Tole were, without doubt, credible. The evidence of Pruitt, Lundberg and Tole, including all comments with respect to all documents presented to them by counsel for both parties form the factual basis which I have considered in my analysis. The evidence of all three such witnesses was clear that there was never any intent for Univar to acquire that debt and, in fact, Univar did *not* acquire that debt. It was acquired by Barbadosco with the monies used by Univar to subscribe for shares of Barbadosco.

[38] An example of the foregoing appears in the Respondent's written submission which reads as follows:

> The Respondent submits that in some cases a reasonable measure of the taxes otherwise payable under the *Act* might be ascertained by determining the amount of tax that would have been paid by the shareholder on the income from the asset if it held the asset that the corporation acquired with the funds invested in the shares. It need not be contemplated that the shareholder would ever have contemplated acquiring that asset directly particularly if the sole reason that it would not be feasible to do so is the tax that would be payable under the Act on the income from the assets. …
>
> The focus of paragraph 95(6)(b) is the receipt of money by shareholders from their corporations. Such money can be received by dividends, loan or interest (if the shareholder is a creditor of the corporation). In the present case, the basic or core intent of the transactions in issue was that the interest payable on the Univar Europe notes be received by the Appellant tax-free. The only way this could be accomplished under the *Act* was to pay this interest income to VWRB and the Appellant becoming a shareholder of VWRB, so that that money could be paid to the Appellant by way of dividends, otherwise that interest could come to the Appellant only if the Appellant became Univar Europe's creditor. The tax that could

> otherwise have been payable under the Act would, had the shares not been acquired by the Appellant, have been the tax on that interest.

I underline what I have said above, namely that the Respondent's case, both with respect to paragraph 95(6)(*b*) and section 245 is built solely upon the hypothetical premise that the debt of UE to UC was purchased by Univar, not by Barbadosco.

[39] The Federal Court of Appeal in *Canadian Pacific Ltd. v. R.* 2002 D.T.C. 6742 said at page 6750, paragraph 33:

> A recharacterization of a transaction is expressly permitted under section 245, but only after it has been established that there has been an avoidance transaction and that there would otherwise be a misuse or abuse. A transaction cannot be portrayed as something which it is not, nor can it be recharacterized in order to make it an avoidance transaction.

[40] In *Canada Trustco* reference is made in paragraph 15 to the *Explanatory Notes to Legislation Relating to Income Tax* issued by the Honourable Michael H. Wilson, the Minister of Finance (June 1988) are an aid to interpretation. That paragraph says that the explanatory notes state at the outset that they

> are intended for information purposes only and should not be construed as an official interpretation of the provisions they describe.

[41] At paragraph 30 the Court continues as follows:

> It is useful to consider what will not suffice to establish an avoidance transaction under s. 245(3). The Explanatory Notes, at p. 464
>
>> Subsection 245(3) does not permit the "recharacterization" of a transaction for the purposes of determining whether or not it is an avoidance transaction. In other words, it does not permit a transaction to be considered to be an avoidance transaction because some alternative transaction that might have achieved an equivalent result would have resulted in higher taxes.

[42] The Respondent clearly cannot recharacterize what, in fact, happened in assuming that the Appellant purchased the aforesaid notes. That is simply not in accordance with the evidence of three credible witnesses for the Appellant. The

attempted recharacterization is not an appropriate alternative arrangement to establish tax otherwise payable.

[43] The only alternate arrangement that can be considered is the possibility of the alleged avoidance transaction not having occurred. Had the shares of Barbadosco not been acquired by the Appellant, there would be no tax otherwise payable which could be avoided, reduced or deferred. The acquisition of such shares by the Appellant does not change that.

[44] With respect to section 245 there was, as described in (a) above a "transaction" which includes an arrangement or event. However, that transaction did not, as set out above, result in a tax benefit in that there was no reduction, avoidance or deferral of tax payable under the *Act*.

Avoidance Transaction

I turn now to a consideration of the questions raised under (c) in the above chart, reproduced here.

Subsection 95(6)	Section 245
(c) can it reasonably be considered that the *principal* purpose for the acquisition is to so avoid, reduce or defer tax otherwise payable?	(c) would the transaction be an "avoidance transaction" and can it reasonably be considered to have been undertaken or arranged *primarily* for *bona fide* purposes other than to so reduce, avoid or defer a tax benefit?

[45] Paragraph 95(6)(b) requires the principal purpose of the share acquisition to be the avoidance, reduction or deferral of tax otherwise payable. As I have already decided that there was no tax otherwise payable to avoid, reduce or defer, subsection 96(5) cannot apply.

[46] If it were necessary for me to decide, under subsection 95(6), whether it could reasonably be considered that the principal purpose for the acquisition of shares of Barbadosco by the Appellant was to permit the Appellant

> …to avoid, reduce or defer the payment of tax…that would otherwise be payable.

I would have found on a factual basis that it could not be so considered.

[47] Likewise, with respect to Section 245 there was, as described, a "transaction" which includes an arrangement or event. However, that transaction did not result in a tax benefit in that there was no reduction, avoidance or deferral of tax payable under the *Act*. Therefore, the transaction cannot be an avoidance transaction because it would not result, directly or indirectly, in a tax benefit.

[48] If it were necessary for me to decide, under section 245, whether a transaction may reasonably be considered to have been undertaken or arranged primarily for *bona fide* purposes other than to obtain a tax benefit, I would have found on a factual basis that it could reasonably be considered to have been so undertaken or arranged.

[49] I now turn to the reassessment of the Appellant for tax payable under Part XIII respecting the August 6, 2001 reassessment for the 1995 taxation year. The Respondent's argument with respect to the imposition of such tax rests in its view that the Appellant's incorporation of Barbadosco and its use of Barbadosco to purchase the aforesaid notes formerly held by UC resulted in a misuse of subsection 15(2.2). Having made my conclusions above respecting section 245, the misuse argument is not open to the Respondent. Accordingly, the appeal respecting Part XIII tax will be allowed. No such tax will be payable under Part XIII.

[50] In respect of the September 3, 2002 reassessment of a subsection 162(1) late filing penalty, the reassessment was made after the expiry of the time limit for doing so, it not having been made, within the meaning of subparagraph 152(4)(*b*)(iii):

> ...as a consequence of a transaction involving the taxpayer and a non-resident person with whom the taxpayer was not dealing at arm's length.

It was made as a consequence of failing to file a tax return within the period prescribed for so doing. It is noted that this is an alternative argument. In respect of the taxation ending July 15, 1996 for which this penalty was assessed, no amount as reassessed will be includable in the Appellant's income and therefore no penalty will be payable.

RESPONDENT'S SUBMISSIONS

[51] I now turn to submissions made by Respondent's counsel.

[52] Respondent's counsel, in cross examination and in both the written and oral submission, dwelt upon the potential of how the debt purchase transaction could have been structured rather than of accepting the evidence as to how, in fact, it was structured. I have discussed the matter of recharacterization above, it not being available for the purpose of establishing an avoidance transaction but to be used only after determining the existence of an avoidance transaction under section 245. The same is true of paragraph 95(6)(*b*).

[53] Respondent's counsel, in discussing the *Principal or Primary Purpose of Setting Up Barbados* in a written submission said:

> The Respondent submits at the outset that the only purposes that are relevant under both paragraphs 95(6)(b) and section 245 of the *Act* are purposes that are relevant to the Appellant. In particular, the only purpose that is relevant under both paragraph 95(6)(b) and section 245, is the purpose of the share purchase transactions, i.e., whether they could reasonably be considered to have been entered into primarily for the purpose of avoiding, reducing or deferring the tax that would otherwise have been payable under the *Act*. Thus, even if it could be found that the principal or primary purpose of the transactions was to avoid, reduce or defer U.S. tax, this would be irrelevant.[2] In the Respondent's submissions, the same principle applies to any of the other alleged, non-tax, reasons, for the creation and operation of VWRB that are ex-traneous (sic) to the Appellant as a tax paying Canadian entity. They are also irrelevant to the issues under paragraph 95(c)(b) and section 245.[2]
>
> *RRM Canadian Enterprises Inc. and Equilease Corporation* 97 D.T.C. 302, at 312 (T.C.C.), per Bowman, T.C.C.J.

[54] Presumably, the Respondent's reasoning is derived from the statement by Bowman, J. that:

> Section 245 operates within the context of Canadian tax law and it is within that context that the primary purpose is to be determined.
> The Appellant's position appears to be that where an avoidance transaction in Canada results in greater inroads being made against the U.S. fisc than against the Canadian fisc the primary purpose cannot be the avoidance of Canadian tax. I do not accept that.

[55] Authorities for propositions must be carefully presented in the full context of the decision upon which those propositions are based. *RMM,* the Appellant, which was to be wound-up with a distribution dividend being subject to withholding tax, together with its U.S. parent company, arranged instead, a convenient purchase of the Appellant's shares. This transaction was designed to reduce both Canadian and U.S. income tax.

[56] The distinctions between the RMM decision and this case are:

(1) In this case there was no tax to be saved such as the Canadian withholding tax.

(2) The above quote acknowledges the existence in RMM of a "Canadian tax avoidance scheme". I have concluded that there was no avoidance transaction in this case.

(3) The latter part of the quote states that section 245 operates within the context of Canadian tax law and it is within that context that the primary purpose is to be determined. This cannot be interpreted to mean that one must not consider the *entire* fact situation in whatever geographical location, relating to and giving rise to the decisions made and the transactions implemented by a Canadian tax paying entity.

(4) There is no argument in this case that more tax was saved in any country or countries other than in Canada and that the primary purpose, was not, therefore, to obtain a Canadian tax benefit.

(5) The witnesses who testified in this case included the three gentlemen, Pruitt, Lundberg and Tole who were intimately familiar with the facts surrounding what took place, as stated herein.

[57] Bowman, J., in not accepting the Appellant's position was obviously influenced by the fact situation before him. The steps taken by that Appellant clearly related to and resulted in the avoidance of tax which would have been owing had the Appellant not sought to avoid the payment of tax that would inevitably have been owing on the distribution of assets in the normal corporate fashion.

[58] Also, Bowman, J.'s, comments in the above quote appear to be *obiter dicta*.

The English Oxford Dictionary, second edition, defines *obiter dictum* as follows:

> …in *Law*, An expression of opinion on a matter of law, given by a judge in court in the course of either argument or judgement, but not forming an essential part of the reasons determining the decision, and therefore not of binding authority;

[59] I do not believe that the RMM case stands for the proposition that an analysis of the purposes of transactions or events outside Canada should not be considered by this Court.

[60] In *Will-Kare Paving & Contracting Limited v. R.* 97 D.T.C. 506, this Court said at 510:

> The word 'primary' (and thus, primarily) means first in order of time, or development, or in intention. The word 'principal' (which is virtually interchangeable with the word 'primary') means chief; leading; most important or considerable; primary; original, highest in rank, authority, character, importance, or degree.

[61] In both written and oral submissions, Respondent's counsel stressed the importance of what was contained in multitudes of documents accepting little, if any, of the oral evidence given in Court. For example, undue reliance was placed on the oft used term "tax strategy" in those documents, being used by counsel to establish that the primary purpose of the transaction(s) was the reduction, avoidance or deferral of tax. Indeed, counsel, at one point stated in oral argument with respect to the guarantee fee issue, an absolute rejection of oral evidence as evidenced by the following exchange:

> Justice: So you don't believe that evidence.
>
> Counsel: No.

[62] Further, a number of counsel's submissions, such as those respecting the new section 17[2] had nothing to do with the *purpose* of the acquisition or any transactions involved in this appeal. They referred to events subsequent to the period that must be examined in order to determine that purpose. In this regard, Rothstein, J.A. in *OSFC Holdings Ltd. v. Canada* 2001 F.C.A. 260 at paragraph 46 said:

> The words 'may reasonably be considered to have been undertaken or arranged' in subsection 245(3) indicate that the primary purpose

---

2 Which became applicable only in 2000.

> test is an objective one. Therefore the focus will be on the relevant facts and circumstances and not on statements of intention. It is also apparent that the primary purpose is to be determined at the time the transactions in question were undertaken. It is not a hindsight assessment, taking into account facts and circumstances that took place after the transactions were undertaken.

[63] Counsel also, both in cross examination and in argument, placed great emphasis on the fact that the tax rate in Barbados was only 2.5 percent whereas it was some 45 percent in Canada. Counsel's written submission contains this statement:

> All that changed was that the return on the notes was taxed at 2.5%, versus 45% in Canada, and that there were other costs in Barbados. The only plausible explanation that therefore offers itself for the purpose of in effect investing in those interest-yielding securities offshore could only have been to avoid paying Canadian tax on that income.

[64] Respondent's counsel refused to accept evidence to the effect that the Appellant had approximately $12,000,000 cash on hand at the time it borrowed monies for the two-fold purpose of acquiring shares of Barbadosco and paying suppliers during the interim period preceding the harvest of crops raised by the Appellant's customers. The cross examination had posed numerous questions to the witnesses respecting whether the entire amount of some $37,600,000 used for the share acquisition had been borrowed. The answers given to those questions, that the company had cash on-hand and that it was used for this purpose was ignored. Finally, the last question asked by Respondent's counsel on cross examination of Tole was:

> Q. You will acknowledge, Mr. Tole, that the bulk of the $37,600,000 that was injected in to Barbados was borrowed money?
>
> A. I would, there was just under $12 million cash in the bank, so the bulk would have to be borrowed, I would agree.

I am satisfied by the evidence that, as always had been planned, the cash on hand was used as part of the Barbadosco share subscription. If any confusion existed respecting the analysis of the Appellant's bank statement entries on that date, one need only refer to the witnesses' testimony. In addition, money is fungible. In the words of the Oxford English Dictionary, Second Edition,

> One guinea…precisely supplies the place of another.

[65] Respecting the undue emphasis on "tax strategy", all business transactions, if properly analyzed, planned and implemented, must involve an acute awareness of the tax effect of every aspect thereof. The failure to exercise great care in dealing with that one aspect of a business transaction simply cannot exist in the complicated modern business world.

CONCLUSION

[66] In accordance with the conclusions set out above the appeal in respect of the following taxation years, namely:

(1) taxation year ended February 29, 1996;

(2) taxation year ended July 15, 1996;

(3) taxation year ended December 31, 1996;

(4) 1997 taxation year;

(5) 1998 taxation year;

(6) 1999 taxation year;

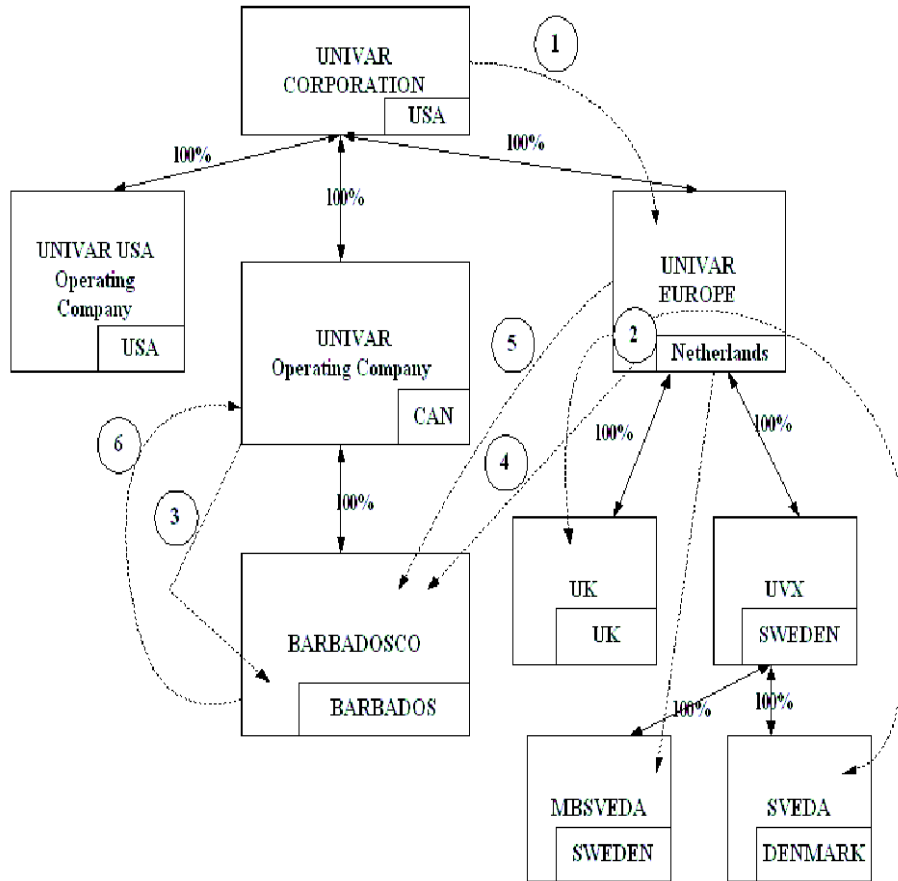
will be allowed.

[67] The appeal respecting a penalty under subsection 162(1) for failure to file a return of income as and when required for the taxation year ended July 15, 1996, will be allowed.

[68] The appeal respecting Part XIII for the 1995 taxation year will be allowed.

[69] Respecting costs, in accordance with the agreement of counsel, I will be available for a telephone conference for that purpose. Counsel can arrange this with the Trial Coordinator.

APPENDIX A



1. UC had loaned $27,036,660(US)to UE.
2. UE had, effectively, loaned monies to UK, MB SVEDA and SVEDA.
3. May 29, 1995 UNIVAR subscribed for 10,000 shares of BARBADOSCO for a total of $27,036,660(US) Canadian $37,360,000.
4. BARBADOSCO bought from UC the indebtedness of UE to UC for $37,352,574 (Canadian) so that UE then owed that amount to BARBADOSCO.
5. UE paid interest on dept owing to BARBADOSCO.
6. BARBADOSCO paid 2.5% tax in Barbados and paid after tax amount to UNIVAR which included those amounts in income and claimed deductions under section 113(1).

UC is Univar Corporation
UE is Univar Europe BV

APPENDIX B

AGREED STATEMENT OF FACTS

The parties hereto by their respective solicitors agree on the following facts, provided that this agreement is made for the purpose of these Appeals only and may not be used against either party on any other occasion, and provided that the parties may add further and other evidence relevant to the issues and not inconsistent with this agreement.

1. The Appellant is a "taxable Canadian corporation", within the meaning of subsection 89(1) of the *Income Tax Act* (Canada) (the "*Act*").

2. For the period up to April 2, 2001, the Appellant was named Van Waters & Rogers Ltd. ("VWRL"), then changed its name to Vopak Canada Ltd ("Vopak Canada"). Subsequently, on July 2, 2002, the Appellant's name again changed to Univar Canada Ltd. ("Univar Canada").

3. The Appellant is a corporation organized under the laws of British Columbia having its principal place of business at 9800 Van Horne Way Richmond, British Columbia.

4. During the relevant period, the Appellant was a wholly-owned subsidiary of Univar Corporation ("Univar"), a U.S.-resident corporation that changed its name to Univar North America Corporation on July 3, 2002.

5. On May 26, 1995, the Appellant incorporated a wholly-owned subsidiary, Van Waters & Rogers (Barbados) Ltd ("Barbadosco"). At all material times Barbadosco was a wholly-owned subsidiary of the Appellant.

6. On May 29, 1995 the Appellant subscribed for 10,000 shares of Barbadosco for U.S. $2,703.66 a share, for a total of US $27,036,660, whose Canadian dollar equivalent was CAD $37, 360,000.

7. On June 14, 1995 Barbadosco paid CAD $37, 352, 574 (equivalent to US $27,036,625) to Univar to acquire interest-bearing debts owed by the Univar Europe N.V., a Netherlands company, to Univar (the "Notes Receivable").

8. At all material times the Appellant and Univar Europe were wholly-owned subsidiaries of Univar.

9. Between 1995 and the end of 1999, Barbadosco earned and received interest income from the Notes Receivable and bank deposits.

10. Between 1995 and the end of 1999, Barbadosco paid the following amounts to the Appellant by way of dividends (the "Dividends"):

Taxation Year-End	**Dividends (CAD$)**
February 29, 1996	$1,810,855
July 15, 1996	$759,651
December 31, 1996	$1,313,172
December 31, 1997	$2,578,071
December 31, 1998	$2,090,000
December 31, 1999	$2,374,286
	$10,926,035

11. In computing its Part I tax payable for the 1996 to 1999 taxation years, the Appellant included the Dividends in its income and deducted the Dividends in computing its taxable income.

12. In December 1998, the Appellant paid a CAD $70,000,000 dividend to Univar and withheld and remitted non-resident withholding tax in the amount of CAD $3,500,000 under Part XIII of the *Act* and the Candada-U.S. Income Tax Convention.

13. On or about January 3, 2000, Barbadosco was dissolved. The Notes Receivable were distributed to the Appellant as a liquidating dividend, which the Appellant, in turn, distributed to Univar by way of dividend. The Appellant withheld and remitted non-resident withholding tax in the amount of CAD $1,790,228 under Part XIII of the *Act* and the Candada-U.S. Income Tax Convention.

14. The Appellant received Notices of Reassessment dated September 7, 2001 (collectively, the "Part I GAAR Reassessments"), in which the Minister of National Revenue (the "Minister") reassessed the Appellant in respect of its 1996 through 1999 taxation years for tax and interest under Part I of the *Act*.

15. The Appellant received a Notice of Reassessment dated August 6, 2001 (the "Part XIII Reassessment") which showed that the Minister reassessed the Appellant in respect of its 1995 taxation year for withholding tax and interest under Part XIII of the *Act.*

16. On October 12, 2001, the Appellant duly filed Notices of Objection to the Part I GAAR Reassessments and Part XIII Reassessment.

17. By Notice of Confirmation dated November 9, 2001, the Minister confirmed the Part I GAAR Reassessments and Part XIII Reassessment.

18. By Notice of Appeal filed on February 5, 2002, the Appellant appealed the Part I GAAR Reassessment and the Part XIII Reassessment to this Court (the "Vopak Appeal").

19. On April 12, 2002, the Respondent filed a Reply to the Appellant's Notice of Appeal in the Vopak Appeal in this Court.

20. The Appellant received Notices of Reassessment (the "2002 Reassessments") dated August 9, 2002 with respect to the Appellant's 1996-1999 taxation years. The Appellant was thereby reassessed for Part I tax and interest for those taxation years pursuant to paragraph 95(6)(b) of the *Act*, by reversing the previous interest inclusions in computing income and by denying the deduction of the Dividends in computing taxable income.

21. The Appellant received a Notice of Reassessment dated September 3, 2002 (the "September Reassessment") for the taxation year ending July 15, 1996 which reflected a penalty under subsection 162(1) of the *Act.*

22. On November 5, 2002, the Appellant filed a Notice of Appeal (the "Univar Appeal") in respect of the 2002 Reassessments and the September Reassessment.

23. On January 27, 2003, the Respondent filed a Reply to the Appellant's Notice of Appeal in the Univar Appeal.

24. On February 26, 2003, the Appellant filed an answer to the Reply in the Univar Appeal.

25. The attached charts accurately describe the corporate structure and ownership of the Univar group of corporations and are titled as follows:

    (a) Organization As of June 30, 1991 (Tab A);

    (b) Oraganization As of March 1, 1995 (at Tab B);

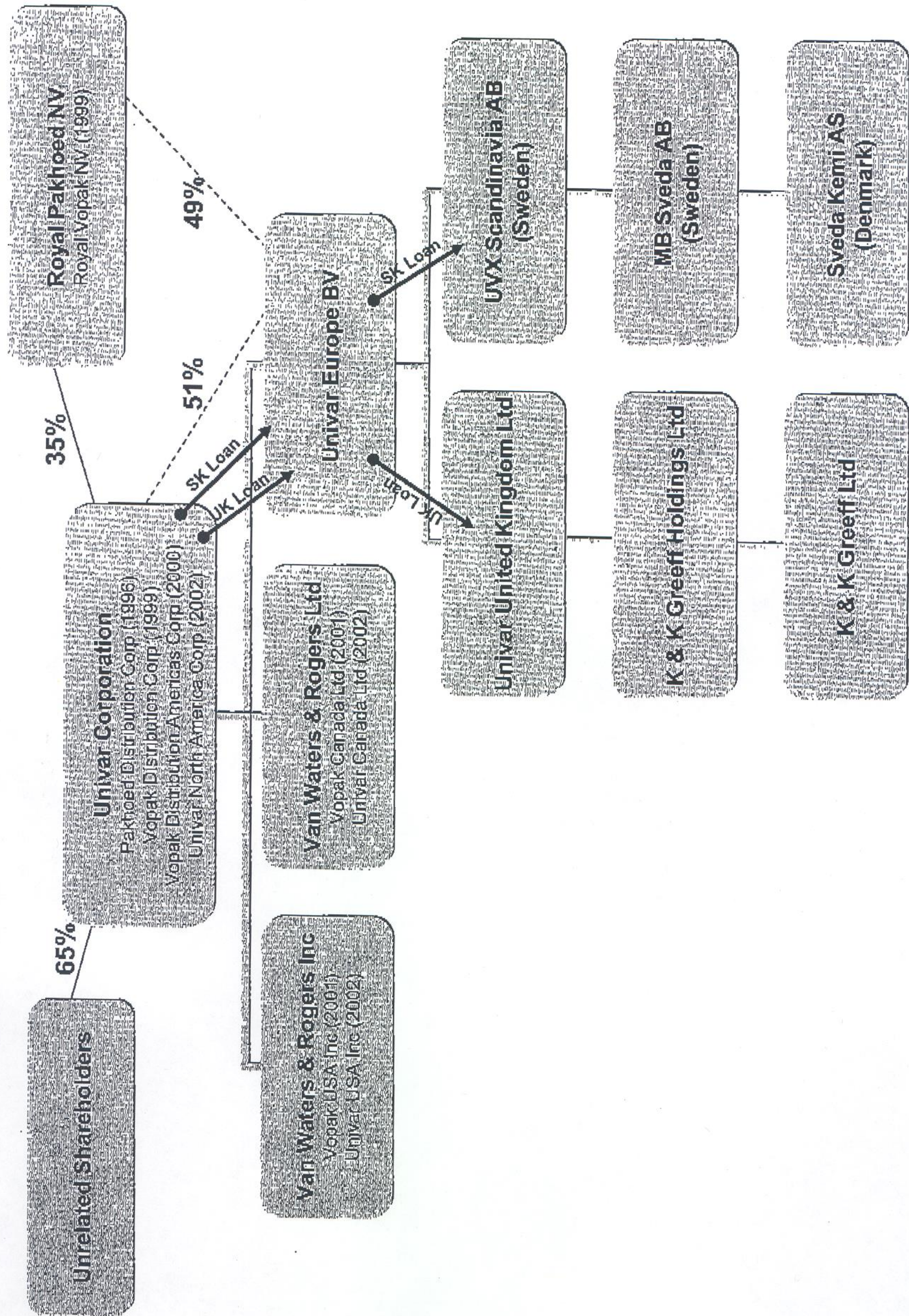
(c) Organization As of June 14, 1995 Following Formation of Van Waters & Rogers (Barbados) Ltd (at Tab C);

(d) Organization After Acquisition of Univar Corporation by Royal Pakhoed on July 16, 1996 (at Tab D); and

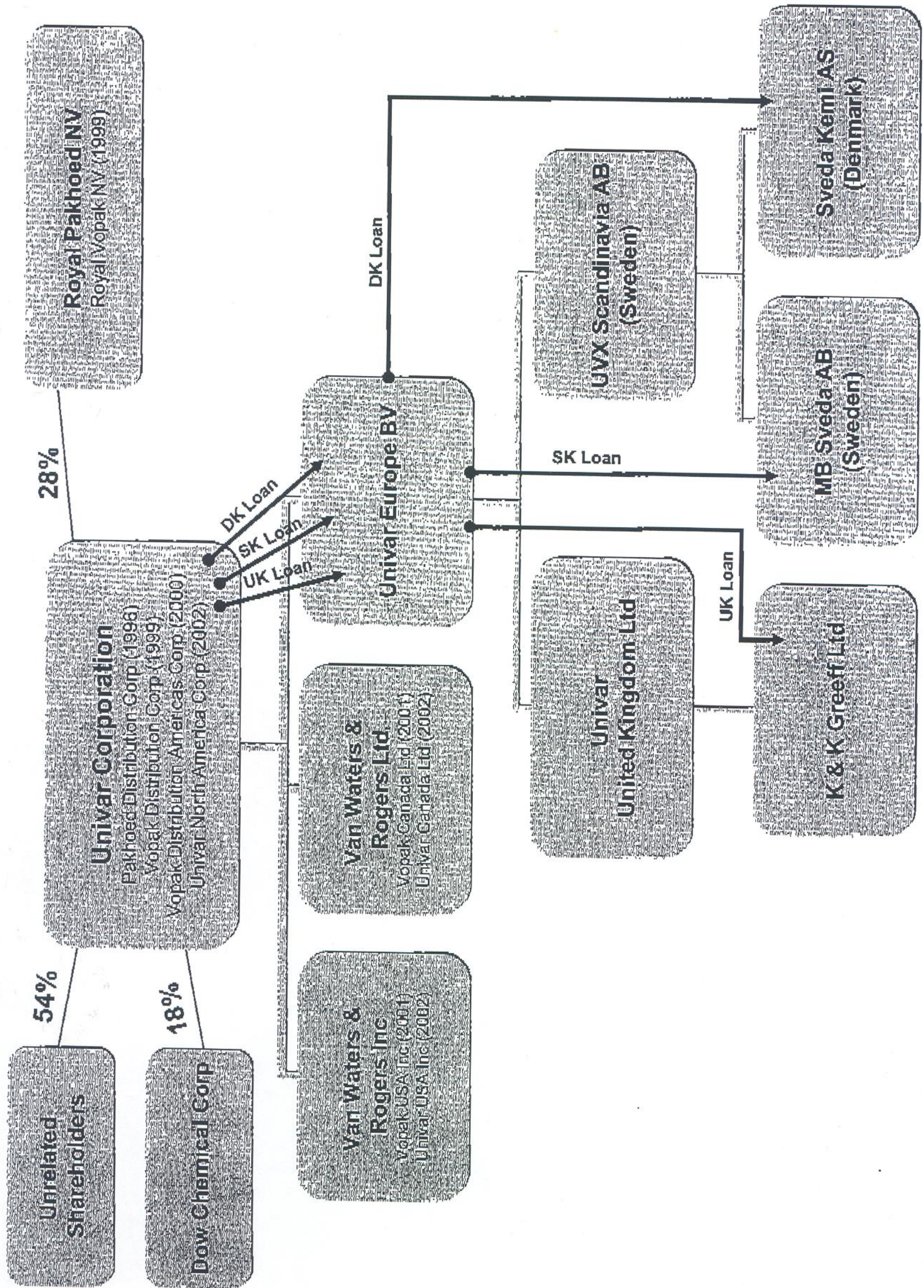
(e) Organization After Liquidation of Van Waters & Rogers (Barbados) Ltd on January 3, 2000 (at Tab E).

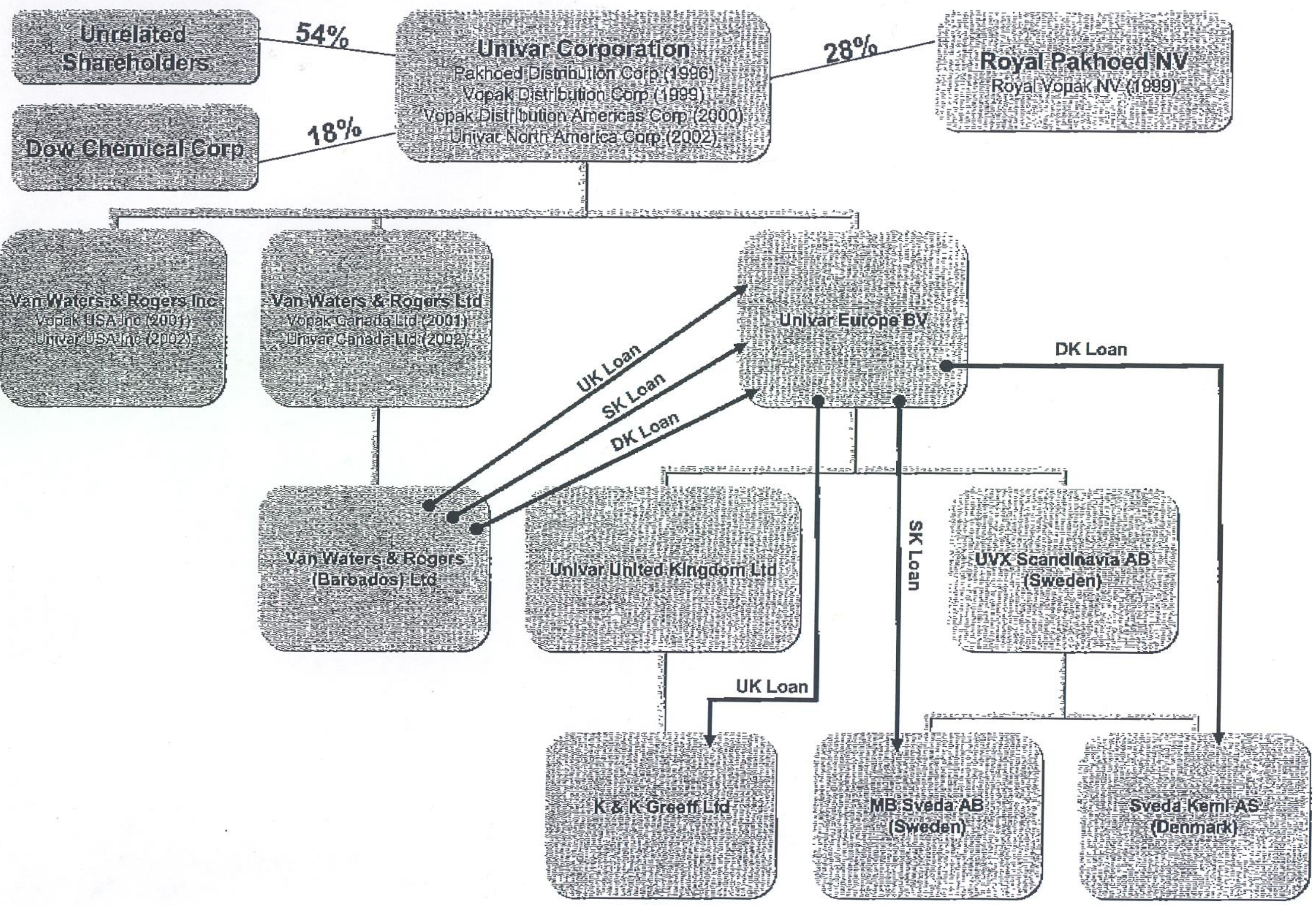
26. The original Notices of Assessment issued to the Appellant for its 1996 to 1999 taxation years were dated as follows:

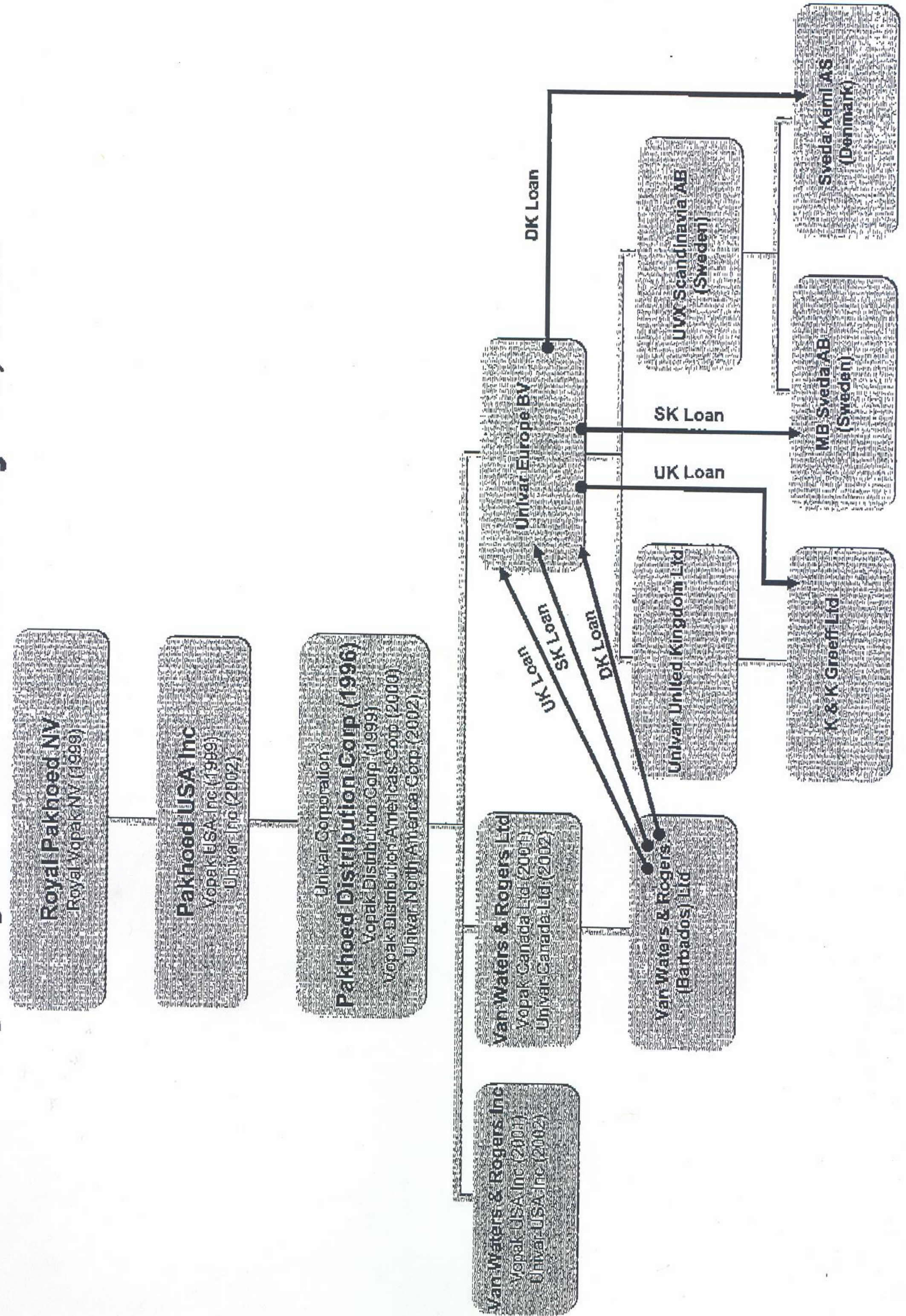
Taxation Year	**Date**
February 29, 1996	December 5, 1996
July 15, 1996	September 18, 1997
December 31, 1996	September 22, 1997
December 31, 1997	August 31, 1998
December 31, 1998	December 29, 1999
December 31, 1999	September 21, 2000


Organization As of June 30, 1991
Royal Pakhoed NV
Royal Vopak NV (1999)
Unrelated Shareholders
65%
35%
Univar Corporation
Pakhoed Distribution Corp (1996)
Vopak Distribution Corp (1999)
Vopak Distribution Americas Corp (2000)
Univar North America Corp (2002)
51%
49%
SK Loan
UK Loan
Univar Europe BV
Van Waters & Rogers Ltd
Vopak Canada Ltd (2001)
Univar Canada Ltd (2002)
Van Waters & Rogers Inc
Vopak USA Inc (2001)
Univar USA Inc (2002)
SK Loan
UK Loan
UVX Scandinavia AB
(Sweden)
MB Sveda AB
(Sweden)
Sveda Kemi AS
(Denmark)
Univar United Kingdom Ltd
K & K Greeff Holdings Ltd
K & K Greeff Ltd

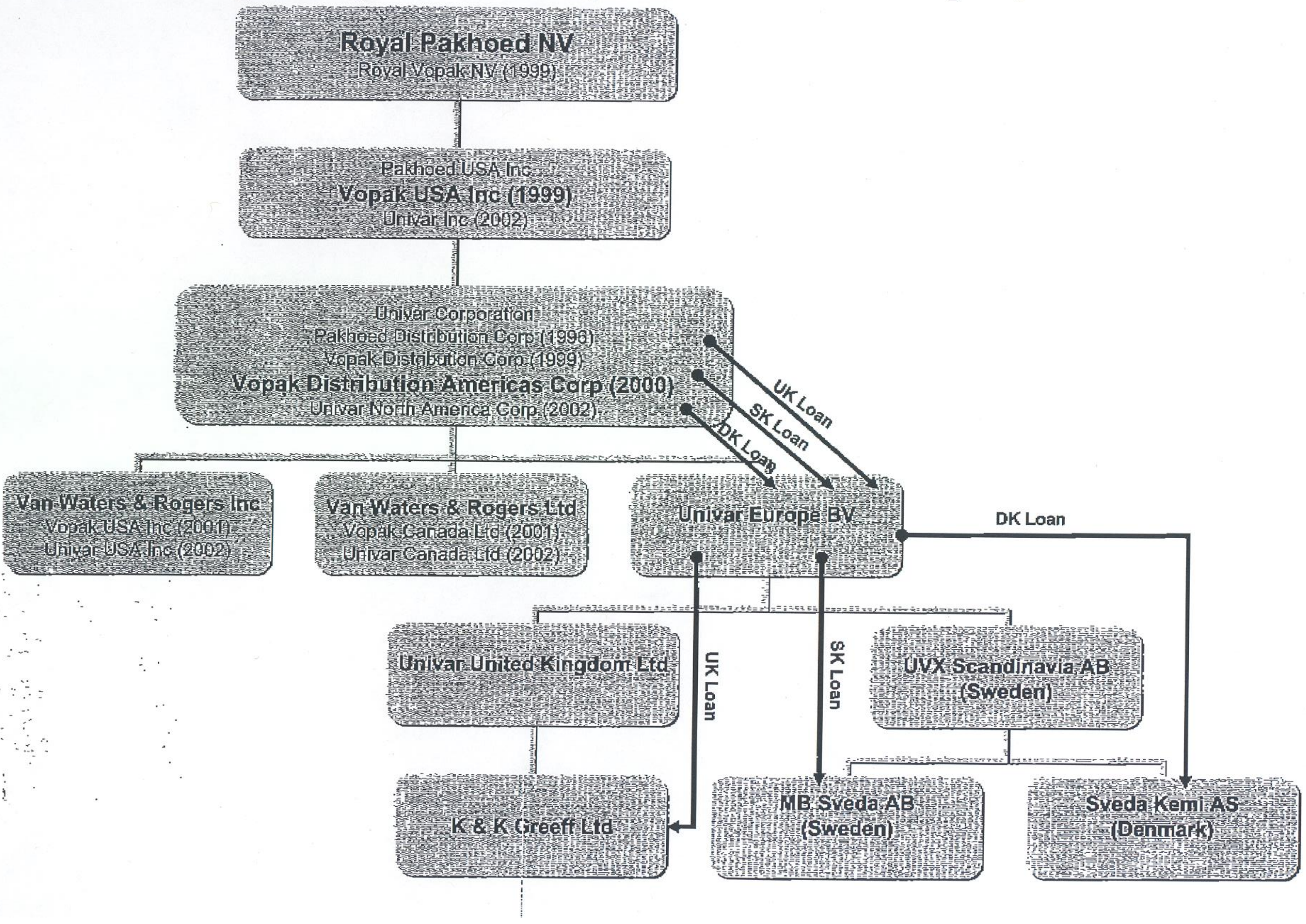
Organization As of March 1, 1995




Organization As of June 14, 1995 Following
Formation of Van Waters & Rogers (Barbados) Ltd
Unrelated Shareholders
54%
Dow Chemical Corp
18%
Univar Corporation
Pakhoed Distribution Corp (1996)
Vopak Distribution Corp (1999)
Vopak Distribution Americas Corp (2000)
Univar North America Corp (2002)
28%
Royal Pakhoed NV
Royal Vopak NV (1999)
Van Waters & Rogers Inc
Vopak USA Inc (2001)
Univar USA Inc (2002)
Van Waters & Rogers Ltd
Vopak Canada Ltd (2001)
Univar Canada Ltd (2002)
Univar Europe BV
UK Loan
SK Loan
DK Loan
DK Loan
Van Waters & Rogers (Barbados) Ltd
Univar United Kingdom Ltd
SK Loan
UVX Scandinavia AB (Sweden)
UK Loan
K & K Greeff Ltd
MB Sveda AB (Sweden)
Sveda Kemi AS (Denmark)



Organization After Acquisition of Univar Corporation
by Royal Pakhoed on July 16, 1996
Royal Pakhoed NV
Royal Vopak NV (1999)
Pakhoed USA Inc
Vopak USA Inc (1999)
Univar Inc (2002)
Univar Corporation
Pakhoed Distribution Corp (1996)
Vopak Distribution Corp (1999)
Vopak Distribution Americas Corp (2000)
Univar North America Corp (2002)
Van Waters & Rogers Inc
Vopak USA Inc (2001)
Univar USA Inc (2002)
Van Waters & Rogers Ltd
Vopak Canada Ltd (2001)
Univar Canada Ltd (2002)
Univar Europe BV
UK Loan
SK Loan
DK Loan
DK Loan
Van Waters & Rogers
(Barbados) Ltd
Univar United Kingdom Ltd
UK Loan
SK Loan
UVX Scandinavia AB
(Sweden)
K & K Greeff Ltd
MB Sveda AB
(Sweden)
Sveda Kemi AS
(Denmark)


Organization After Liquidation of Van Waters & Rogers (Barbados) Ltd on January 3, 2000
Royal Pakhoed NV
Royal Vopak NV (1999)
Pakhoed USA Inc
Vopak USA Inc (1999)
Univar Inc (2002)
Univar Corporation
Pakhoed Distribution Corp (1996)
Vopak Distribution Corp (1999)
Vopak Distribution Americas Corp (2000)
Univar North America Corp (2002)
UK Loan
SK Loan
DK Loan
Van Waters & Rogers Inc
Vopak USA Inc (2001)
Univar USA Inc (2002)
Van Waters & Rogers Ltd
Vopak Canada Ltd (2001)
Univar Canada Ltd (2002)
Univar Europe BV
DK Loan
Univar United Kingdom Ltd
UK Loan
SK Loan
UVX Scandinavia AB
(Sweden)
K & K Greeff Ltd
MB Sveda AB
(Sweden)
Sveda Kemi AS
(Denmark)

EVIDENCE OF GARY EMMETT PRUITT

[1] Gary Pruitt ("Pruitt") started working with the Appellant in October 1978. He is a certified public accountant (CPA) and has held a variety of positions in the UC empire. He commenced with internal audit, was Assistant Treasurer, Treasurer, Vice-President and Treasurer, Vice-President of Finance, Chief Financial Officer, and a member of the Executive Board and Chairman of the Executive Board and then Chief Executive Officer. Pruitt occupied these positions while UC was American controlled. In July 1996 UC became wholly owned by a Netherlands company, Royal Pakhoed NV. At the time of testifying, Pruitt was Chairman of the Executive Board and Chief Executive Officer of Univar NV, a Netherlands company which carried on the international business of product distribution, having, due to conflict, separated from another part of Royal Pakhoed's business.

[2] Pruitt said that:

> the primary business principle or purpose was to improve the overall value for shareholders through investing the full capital of the corporation for the best appropriate or reasonable return that the company could make.

this being corporate philosophy for many many years and "certainly since it was a public company in the mid-sixties." UC was a public company traded on the New York stock exchange.

[3] The witness testified that the four financial elements that needed to be carried out were, in his view and the view of management overall:

(1) profitable growth

(2) increased return on equity

(3) strong cash flow, and

(4) effective capital management.

[4] He described *profitable growth* as:

> the continual increase and growth of profitability that generates returns on total capital above our cost of capital.

[5] He described *increased return on equity* as referring to net profit as it relates to the total shareholder equity on the balance sheet. He said that he was:

> referring to the paid-in capital, the common share value and retained earnings typically for a total shareholder equity.

[6] He described *strong cash flow* as meaning:

> that the corporation in carrying out its efforts must generate positive and strong and growing positive cash flows for the company.

[7] He said further that, in order to obtain *effective capital management*, the company:

> must utilize all of its capital available to it, in the most efficient, or effective manner. That's shareholder capital as well as borrowing capacity.

He said that the companies must employ aggressive sales efforts and must also have, as a priority, the acquisition of businesses to improve the business conducted by them on a more profitable basis

> …so that they could fully utilize their capital in a profitable way.

[8] He said that when subsidiaries exhaust their opportunities to grow internally or to make acquisitions, they become under-leveraged, being a huge problem in that they are not able to utilize their leverage or debt capacity. Pruitt then stated that Univar fell short of meeting that goal. He described it as highly profitable and growing well but unable to grow at a pace that would keep up with the capital base it was accumulating. Accordingly, he said that it would fall short in terms of the level of new investments it was able to make. He said that if a company underutilizes its capital and is unable to grow its business fast enough:

> … then you end up with unutilized cash and unutilized debt capacity, which actually deteriorates shareholder value at the securities level, at the public company level. So you must do both. It must be profitable above your cost of capital and fully utilize your capital base.

[9] He said that Univar had made acquisitions by buying competitors but that there was an insufficient number of those available in order to keep up with using its capital base. He said that it had been a constant problem for the Canadian company, Univar, being a product of its highly successful business in the Canadian economy, stating that it had:

> been highly successful but was unable to grow as fast as it would need to grow to continue to generate ultimate increase in value.

[10] Pruitt said that the companies on Chart 1 in the Agreed Statement of Facts other than Royal Pakhoed and the unrelated shareholders would have been part of the consolidation at that time.

[11] Pruitt stated that the corporate philosophy was to have a debt-equity ratio of 1 to 1. He said:

> That was the basic premise upon which the public securities were valued in the marketplace in terms of return against that capital base, and so, if we were underutilizing our capital, it would deteriorate the securities value to our shareholders, and if we were overperforming relative to that, it would improve it … and so the objective would need to be, number one, that the corporation as a whole and each of its operations would have to fully employ all of its capital, both equity and available debt, and be able to utilize all of that capital in producing income at an appropriate return.

He then emphasized that Univar was not achieving those types of objectives. He said that the one to one debt equity ratio was not being met in either Europe or Canada. He added that restructuring was required in order to put Univar in a position where it could more effectively utilize its overall capital.

[12] With respect to capital management Pruitt said that capital is not only cash and other assets described on the balance sheet but also the capacity to

borrow money "at a reasonable gearing ratio." In response to a question from counsel as to why the European and Canadian companies didn't simply borrow money directly, Pruitt said that they needed to be able to put borrowed money to appropriate use in order to find effective business investments. He continued by saying that during this period Univar was struggling with trying to find investments that produced adequate returns, additional investments that produced adequate returns beyond what they had already made. The following exchange then took place:

> Q: Why don't we just have the Canadian company borrow the money and pay a huge dividend up to Univar Corporation? That will rebalance everybody.
>
> A: Well, that's never been our policy to do that. The reality is that … the worst thing about that from our perspective, the approach we took in operating our businesses is that we were very much a part of the companies and countries within which we operated. And if all we did was to drag money out of those companies that are continuing to be successful, we've always felt that it was de-motivating to the management that worked hard to develop those businesses. And so we've typically not done that, number one.
>
> Number two… if you leave it there and encourage them to fully utilize it, it puts pressure frankly on the management and on their incentive programs… to continue to grow the business faster and faster in those environments so that they are encouraged to grow the business for the benefit of the shareholders and… because of the incentive compensation designs.
>
> Third, is that if you were to do what you just suggested and were not able to do it in a tax efficient manner, it would deteriorate the ultimate shareholder value at the securities holder level of the public company. So we have never in our philosophy of approaching business taken that approach. There are companies out there that do, but that's never been Univar's philosophy."[3]

In support of this Pruitt said on a note to the financial statements of UC for 1993 Summary of Accounting Policies:

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[3] By Univar he was referring to UC

> No provision for foreign withholding or United States federal income taxes is necessary as it is management's intention that dividends will be paid only under circumstances which will not generate additional net tax cost.

Pruitt explained that that would hurt the overall share value at the consolidated level. His evidence re-emphasized this point on several different occasions.

Pruitt then referred to the acquisition of a company known as Harrison Crossfield, a competitor, which had been acquired by Univar. He said that steps like that helped but the rapid growth of business continued to produce cash flows to the point that those acquisitions did not solve the problem.

[13] He then testified that the business activities of the subsidiaries of Univar Europe were chemical distribution businesses similar to those of Univar. He expanded by saying that UC was, essentially, a holding company of a multi-national operation, not becoming directly involved in the carrying out of the distribution activities. He stated that it provided financing for the corporation in total, coordinated treasury activities, provided the appropriate checks and balances, corporate governance processes for the company, oversight management monitoring and services such as legal services and tax services that would be needed to have specialization to assist each of the operating units in those efforts. He also said that Univar would not be authorized to make investments outside its core business without going through the appropriate corporate governance process to obtain authorization. Pruitt said:

> That's typical of every multinational corporation I know that's well run that has good corporate governance process.

[14] Pruitt underlined what is said above when he stated:

> The performance of the Canadian company was good; there's no question about it. The challenge that you run into when companies' return on total capital, reach 20 percent and 25 percent and so forth are very, very high returns and can only really be achieved typically when you're underutilizing your capital base. So, the return on capital here is on the actual capital deployed, not the capital

> including its borrowing capacity, and what needed to happen was that the excess cash as well as the borrowing capacity needed to be utilized and employed in the business … typically the common view is that the less you owe the better it is but when you owe too little in a corporation you're underutilizing your capital base.

The witness then referred to Univar's acquisition of Wilber-Ellis, a business that expanded into agricultural chemical distribution which he described as another good step in the right direction but, again, facing the same problems of not being able more rapidly to make these kinds of investments. He said that management was doing everything that it could but these types of investments simply were not easily available.

[15] Pruitt, when he was referred to the minutes of the Board of Directors in the late summer of 1994 stated that Univar was still under leveraged while continuing to improve its operating performance. He then said:

> One of the challenges that was going on at the time is because of this leverage problem in Canada, the leverage problem being too little underutilization of cash and underutilization of debt capacity is that the returns were getting so high that the incentive compensation levels were inappropriately high and the Canadian employees were being overcompensated relative to competitors and relative to the value they were generating.

[16] Pruitt described Univar as a component that represented "maybe 15 to 20 percent of the entire UC conglomerate".

[17] He then referred to a 1988 general revolving credit agreement with several U.S. banks. He said that Univar was a guarantor for UC borrowings. The second credit agreement was the U.S. Revolving Credit Agreement, which replaced the 1988 credit agreement. Under this new credit agreement, Univar "was a borrower" but "wasn't a borrower at the first instance". He described Univar as just a guarantor in the first instance. The third credit agreement was described as the multi-currency line or credit agreement implemented in 1995. Under it, all non U.S. subsidiaries were allowed to borrow "under their own currencies".

[18] In answer to a query as to why it wouldn't have been appropriate to leverage Barbadosco, Pruitt said:

> Well, Barbados was set up as a subsidiary of the Canadian operation, an investment of the Canadian operation, for purposes of making - - investing in either loans or making loans to other enterprises. So it was an investment subsidiary and at least the initial capitalization that was provided in setting that up was sufficient to meet its needs at that time.

Pruitt described the difficulties and the occupation of many months of time necessary to implement a credit agreement of that nature. He said further:

> The idea was that the Canadian company would make this investment in this finance company and it would make the appropriate investments in acquiring loans or making loans to enterprises.

[19] Pruitt was referred to the Revenue Canada assessment with respect to deemed income associated with Univar's guarantee of the UC Revolving Credit Agreement. He said that he had been informed that the Canadian tax authorities had deemed that there was income associated with the guarantee of some of the credit agreements and wanted to assess tax on that assumed value. He said that he was referred to a document written for a UC finance committee meeting on April 22, 1993 in which he said that Revenue Canada had issued an assessment of $95,000 Canadian, and that a Notice of Objection had been filed. He testified that conversations with the Bank of America indicated that it attached no weight or value to the Canadian guarantee. He then relayed this information to Revenue Canada.

[20] He stated that the Canadian tax authorities were "still going after the Canadian company as of February 21, 1994." Pruitt also wanted to take whatever steps were necessary to ensure that the U.S. Internal Revenue Service ("IRS") did not impute a dividend if Univar borrowed under the line of credit. He said that he understood that in those circumstances "the IRS could claim there was really a dividend made when there wasn't one and no intention of making one, and thereby taxed accordingly". He said that this was a U.S. tax issue that concerned the corporation.

[21] The following exchange pertaining to the overall corporate plan reads:

> Q: Mr. Pruitt, you described these issues. What solution did the U.S. company think could be crafted for purposes of solving these various problems?
>
> A: Well, Univar Corporation, you know, is the parent company that oversaw the activities in Europe and Canada and U.S. We have multiple … a plethora of problems going on if I might say that. We had recapitalization issues that we needed to go through in Europe. We had U.S. deemed dividend exposures that didn't make any sense because of how we approached our businesses. We had ... under leverage situations in Canada, other capitalization issues in Europe as well and it was a perplexing problem, frankly, but our advisors came up with a process where we – and it seemed like a really rational solution, to have an international investment company that could allow appropriate investment by the Canadian company in an international financing subsidiary that could then be utilized to finance or loan money to or buy existing loans of, on the basis of business to go ahead and continue growing the business. It would give a good return to the Canadian company. It would give the opportunity to provide capital to grow in other areas, and it seemed like a logical, very logical solution to me that would solve a number of the finance and treasury problems that we had for our company and try to obtain a better leverage situation to allow our shareholders to have the increase in value overall for the shares, in that process.

Pruitt also described recapitalization work to be done in Europe. He said that there were interest-bearing and non-interest bearing loans that "needed to be sorted out." The companies that had greater than or less than target leverage needed to be dealt with as well. He said that the recapitalization effort, the whole kind of reorganization was designed to use more effectively the overall capital of the company:

> which is what we had committed to the shareholders we would do.

[22] Appellant's counsel presented Pruitt with Finance Committee meeting minutes of February 18, 1993 and read the following to Pruitt:

> Mr. Pruitt then presented the corporation's plan for consolidation of Univar Europe's subsidiaries. It was noted that this activity is designed to bring the structure of the

> European organization into compliance with United States tax laws. These laws require that no more than three tiers of corporate layers exist. Secondly, the consolidation will allow for review and evaluation of all existing subsidiaries with an eye towards understanding why they exist. Corporations working with local subsidiaries and personnel, as well as Cooper's & Lybrand's on this issue.

In response to this, Pruitt said that he was not a tax expert but that the issue was the deductibility of certain interest levels if there were four or five tiers of foreign subsidiaries owned ultimately by a U.S. parent. He then stated that too many corporate layers affected the deductibility of interest at the U.S. tax level. He said that they either allow or disallow interest expense or impute interest income in some fashion, depending on the number of layers. He then said that this was strictly an effort to reduce the number of tiers in the European network to clean up that U.S. tax issue that was really an accident on the mergers and consolidations that took place. Pruitt also said that all transactions have tax elements to them but that the key effort on each was outlined in terms of the finance, the returns and the other efforts. He said:

> Well, like most multi-national companies… we go through planning sessions to try to understand how to organize our affairs… including… ideas around tax planning and how to deal with foreign source income was really this issue here, and then URECO[4] was a real estate investment project that was not tax related… all things have tax elements to it but it is primarily how to more properly invest in our real estate efforts.

[23] The minutes of the Finance Committee of UC dated April 22, 1993 read, in part:

> Mr. Pruitt then presented a possible strategy regarding recapitalization of Van Waters & Rogers Ltd.[5] In essence, the strategy entails the Canadian organization purchasing receivables held by Univar Corporation and owed to it by Univar Europe Corporation. He reviewed the purpose of the recapitalization and the benefits to be obtained therefrom and reported that as a preliminary step and to

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4 This was a New York based potential real-estate transaction to which UC was referred but which it rejected on the basis that it was too tax oriented and not a good business deal.

5 This was the Appellant.

> allow the corporation the flexibility of executing this possible strategy $15 million in leverage and execute in Canada as at the most recent year end. He reported that preliminary research had uncovered a potential operational issue in Europe, and we would like to continue strategy development.
>
> On motion being obtained and seconded, the committee authorized Management to continue development of its possible Canadian recapitalization strategy.

With respect to the foregoing Mr. Pruitt said:

> What that paragraph is describing the creation of a foreign subsidiary that ultimately ended up being Barbados, that would be a foreign investment company that would be owned by the Canadian organization, and that investment company would make… in this case the initial transaction was contemplated to be the purchase of receivables that were currently owned by Univar by the European businesses. It was a low risk transaction for the new financing subsidiary because we knew the companies, obviously. They had very good market rates of interest and made a good and a relatively safe investment for this new subsidiary.

The following exchange then took place:

> Q: ... then you go on and you say: "Mr. Pruitt presented the corporation's plan for consolidation of Univar Europe's subsidiaries. It was noted there were several objectives of this process including compliance with U.S. tax laws in preparation for compliance with the Univar Europe shareholders agreement. In addition it was noted that in order to have a successful Canadian recapitalization plan, there needed to be a dovetailing of these two issues. Preliminary research indicates the contemplated recapitalization requires that European subsidiaries are consolidated such that interest payments on inter company loans held by Europe could be traced to an active corporation. We continue to work with local subsidiary personnel as well as Cooper's & Lybrand on successful resolution of these issues."
>
> …
>
> Q: What do you have to say about that?

> A: You know, all it's really saying is that this is an integrated solution. I mean as I described it earlier, the whole effort was to try to get all of these various elements accomplished through this process. So in order to have the receivables of such quality that the Barbados subsidiary could - - would, could and should acquire them, required us to reduce the number of tiers so we did not incur… unfavourable and inappropriate U.S. tax consequences. The other issue had to do with the fact that we needed to change some non-interest-bearing loans that were held, to interest-bearing loans because the Barbados subsidiary would not and should not and could not invest in receivables or buy loans that did not have very favourable interest rates, market level and favourable interest rates.
>
> So these elements, all of these things needed to happen in unison in order to make something that made sense at the end of the day.

David Olsen ("Olsen") was the assistant treasurer of UC at the time of this meeting. His report to that meeting read, in part:

> Included in the discussion is an overview of Univar Europe's consolidated balance sheet as of its 1992 fiscal year presented on a proforma basis for the long-term subordinating shareholder debt reclassified to shareholder's equity. These statements indicate that Univar Europe is in a very healthy leverage situation at an appropriate 0.5 to 1 debt to equity ratio. In addition, it was noted the corporation is pursuing alternatives to more effectively utilize excess cash. He then discussed the corporation's plan to implement a multi-currency borrowing line in Europe, the objectives of which would be to provide a vehicle to Univar Europe's liquidity management, establish banking relationships to facilitate corporate-wide requirements, and to fit into an international multi-tiered relationship strategy. It was reported that the corporation had held preliminary discussions with Univar Europe financial personnel and they were favourably disposed towards establishing such a line. In response to a question from Mr. Rogers, it was noted that the line would be very carefully monitored with tight controls such that it would not be utilized as a financing vehicle for speculative currency positions.

Pruitt's comments on the above read as follows:

> Well, it ties in in part. The total recapitalization effort that was going on was a necessary and integral part of this whole effort. The proforma balance sheets and long term subordinated shareholder debt reclassification was the - - when I described it earlier as non-interest bearing debt to interest bearing, that's describing that very act... And the statements indicated Univar is in a very healthy leverage position at approximately .5 to 1 debt to equity ratio indicates that they could afford and should take these subordinated non-interest bearing loans and put them into interest bearing loans as they should have been, and that's all that's saying.
>
> The pursuing alternatives to more effectively utilize cash, excess cash is still part of the overall effort that I described before. First effort is to utilize all excess cash. Second effort is to make sure that everybody is approximating this 1 to 1 leverage ratio that we had discussed earlier in the day, and of course the description indicated by the implement the multi-currency borrowing line in Europe was to - - was a summary comment regarding the multi-currency line that we had previously - – that I previously testified about in detail as to each of the borrowers being non-U.S. borrowers and so forth, and that would also fit into an international multi-tiered relationship, and that's getting the tiers to the proper number... And so, and he's just indicating here that there have been preliminary discussions with Univar Europe financial personnel and they're favourably disposed to this kind of multi-currency line and use it.
>
> One of the challenges that you always have in this effort is to get people from various cultures and countries to agree to have a common solution. Not everybody, and rightfully so, wants their independence, and so every time you take a move to add some sort of common solution, it's always difficult to work through because people are afraid that you will no longer be Swedish and English, and we respect that but - – so it takes a long time to work through these to where the management will still be enthused and supportive of the organization. And so he's just describing that effort.

[24] Pruitt then described that .5 to 1 debt to equity ratio should be altered by making non-interest bearing debt interest bearing and that would more

accurately reflect what the capital structure would be in the European operations.

[25] An exchange between counsel and Pruitt respecting the Canadian operation follows:

> Q: Now Mr. Pruitt, this is a plan that you've come up with regarding the Canadian operations. How did you communicate this type of information to the Canadians? Did you just go and tell them this is what's going to happen...?
>
> A: Well, first of all, I wouldn't characterize it as a solution for the Canadian situation because that would not be an accurate characterization. It was a solution that addressed the challenges in Europe as well as Canada in some of the U.S. tax issues in terms of the risk of deemed dividends from the U.S. taxing authorities. So, it's really more than a Canadian issue. But the communication was really, I mean, the reality is that then as we do today, there's a team environment and the Canadian management people Pat Tole and Fred Hermesmann the finance people more so than the commercial operating people as well as the same their counterparts in Europe, were all involved in working through the various solutions with legal advisors, tax counsel and their own efforts as well as myself, Dave Olsen and Wayne Lundberg out of my office in terms of working through the various complexities. So that's how it was - - so that the communication is really - - it was a joint management effort to work through the various elements. Not everybody knew all the elements, certainly. But everybody knew the concept in total, and then they would work more in their area of expertise. And so, then of course, it would be - - more senior management would be briefed from time-to-time, and then the Boards of Canada as well as the Boards of European - - the European subsidiaries would be briefed as well as our Finance Committee and ultimately the Board of Univar before it was actually executed.

Pruitt stated that he was not a director of the Appellant.

[26] In response to counsel's suggestion that it sounded like Pruitt was telling the Canadian company what to do, Pruitt replied:

> …No, what I was doing was sharing this plan with them and it's in its infancy in concept, of course, with the Board. But this would have been after we had worked with the Canadian management as a part of this team that I described and so this was where I was informing - - not informing them like telling them what they're going to do, but sharing. That would not be - - my character, it wouldn't be the character of our company ever. And number one - - number two, the Canadian company that we have and the Canadians I know in that company are pretty independent individuals as they should be and proud of what they're doing. They're not going to - - you're not going - - you're going to work with them. That's my point, yeah.

[27] Pruitt then said that he was in charge of the project and that he used various people to work with him in coordination of efforts. He stated he predominantly used Wayne Lundberg as a key coordinator. [6] He continued:

> I've been working with him for many, many years. He is a very detailed oriented guy, and but many others were involved as well ... but Wayne was... on this particular project… the key coordinator that involved Olsen working with the banking side and the treasury issues. Very often Wayne would go actually visit subsidiaries to explain what was going on because he had spent a lot of time in each of their offices working with them on various tax issues, so he's familiar with them.

With respect to Lundberg's presentation described in the minutes of UC Finance Committee dated June 22, 1994 Pruitt:

> I had asked Mr. Lundberg to make the presentation… as to the overall status of the recapitalization effort and plan, which he did, and typical - - I mean it would be expected that Wayne would focus more on tax issues than anything else. He was the Tax Director and so that's where most of his comments were. The Committee well understood, because this has been talked about many times, what the effort was all about, why we were doing it, and so this was really at the relatively final stages as I recall.

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[6] He was Manager/Director of corporate taxation at UC.

[28] Appellant's counsel referred to James Fletcher, who was senior vice-president of UC, saying that he had presented an overview of two potential European acquisitions currently under review. The minutes to which he had referred read in part:

> The proforma post-Pakhoed put the financial position of consolidated Univar Corporation. The debt-to-equity ratio is anticipated to be 0.8 to 1, demonstrates that there is sufficient financial capacity to consummate both transactions.

When asked whether the paragraph tied into the strategies he had described, Pruitt said:

> Yes. First of all, I mean, the comment speaks for itself with respect to the consolidated debt-to-equity ratio and the capacity to make these acquisitions. The underlying - - or the plan in terms of financing one or both of those would have been to utilize the financing subsidiary in Barbados to finance those acquisitions.
>
> Q: Which acquisitions are you talking about?
>
> ...
>
> A: Impag and Berk is really these two were referring to on the - -
>
> Q: Oh, I see, so there was a discussion about Berk possibly as early as this stage.
>
> A: I believe so.
>
> Q: Now this talks about two acquisitions that are under review in the second line, BP Norway and Impag in Switzerland.
>
> A: Yeah. BP was a terminal activity in Switzerland, or I mean in Sweden, that was also looked at and consummated. That ended up being strictly a real estate transaction. And Impag was an operating activity, which would have been a candidate but did not end up going through.

[29] Then follows:

> Q: …Now can you tell me anything about the concept that management consider investigating a new corporate structure whereby Univar would incorporate offshore?
>
> A: Yeah. This resulted in me as well as Wayne Lundberg meeting with a tax advisor in New York that Mr. Kesseler had arranged for a meeting that was, I think, referred to by him as a flip transaction. I evaluated that and did not recommend that we go forward with it, that there was no underlying business reason to do that, to enter into that kind of transaction and it was strictly a tax mechanism. And we simply have not in our history and do not today do things strictly for those reasons.
>
> … my experience is that typically they don't work out because laws change, circumstances change, these kind of strategies and plans come under attack, and we simply passed.

[30] After some discussion between Appellant's counsel and Pruitt and reference to a Finance Committee of August 23, 1995 respecting the Berk Ltd. acquisition which was said to be financed by Barbadosco with additional funding provided as an equity contribution from Univar, Pruitt then stated that Berk in the United Kingdom, had been acquired by UE. It was consolidated with K&K Greff into a single United Kingdom company. Part of the transaction was to involve Barbadosco purchasing a UC interest-bearing note payable in respect of that transaction. The management of the Canadian company was seeking Board approval to provide additional equity funding to Barbadosco but this was never achieved because UC was acquired by Royal Pakhoed, UC becoming a wholly owned subsidiary of the Netherlands company "and they did not want to approach the financing in this fashion."

[31] Pruitt explained, in answer to Counsel's question that, Barbadosco did not buy the notes of Berk corporation "or whatever the successor of Berk was" because Pakhoed had its own investment company and its own approach and organization respecting financing this type of acquisition and

> ...had its own approach to corporate governance - - a different philosophy than… Univar.

[32] Pruitt's description of the Pakhoed's philosophy was declamatory. He said that:

> Royal Pakhoed had a very different approach to multi-national businesses. Their approach is essentially to pillage the companies, extracting all of the cash, all of its debt capacities, crippling them. Their subsidiaries as well as the parent company of Univar had no sensitivity whatsoever to the management of the companies or what their feelings were, or the direction that they may feel that the companies need to go forward with.

[33] Counsel discussed a memorandum dated November 13, 1997 with Pruitt. It was entitled "Elimination of Van Waters & Rogers (Barbados) Ltd." It was a memorandum from Lundberg to Hugo Brink[7] at Pakhoed. Pruitt said that:

> …Pakhoed had the approach where they would simply decide and instruct that this is what you will do, and although we would engage them in discussions and try and debate the wisdom, my experience was that once they made up their mind it was - - maybe you could delay the time through discussions but they would make the decision and you'd be instructed to go execute it.

That memorandum contained a discussion about liquidation of Barbadosco.

[34] When Pruitt was asked by Appellant's counsel whether proposed changes to section 17 of the *Income Tax Act* ("Act") was a primary reason for winding up Barbados. Pruitt's answer was:

> No. The primary reason for winding up of Barbados was it was part of the process of extracting the funds from the subsidiary back to Royal Pakhoed. It was part of their process to take the money.

[35] Pruitt also testified that Pakhoed caused the payment of dividends of $70,000,000 from the Appellant to UC. Pruitt then said that in 2001 he was appointed to the executive board of the ultimate parent corporation in the Netherlands. He became the Chairman and Chief Executive of that company following which he set upon a strategy to separate the companies between the terminal business and its distribution business. He hired a new chief

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[7] Vice-president of tax for Royal Pakhoed.

executive for the terminal business and the corporation involved became a separate publicly held company. UC then, once again, became a separate publicly held company in June 2002. He said that at that time they reinstituted their previous policies and tried to recapitalize the companies overall.

[36] On cross examination, Respondent's counsel, Luther Chambers ("Chambers") asked Pruitt whether the debt to equity ratio improved from 1997 to 1998 due to the payment of a huge dividend to UC. After Pruitt answered affirmatively, counsel asked whether it would not be correct to say that instead of entering into the transactions which are in issue in this case the Appellant could have improved its debt to equity ratio in 1995 by borrowing a large sum of money and paying a large dividend to UC. Pruitt replied:

> Not under Univar Corporation's policy.

Pruitt restated that the dividend payment was the result of Pakhoed's instructions after the acquisition of UC. Pruitt then said:

> The challenge is that if there are taxes as a result of moving monies around that incrementally cause tax burden that isn't a result of earning money and operating the company, then you deteriorate the shareholder value at the public share holder value, in our opinion. And thereby the philosophy was that we do not make these dividend declarations.
>
> The other and more important factor is that the key that you need to try to do is to keep the capital under the responsibility of the management that earned that capital and grew that business, to encourage them to further find ways to grow that business and invest that money within their operations. And that's the crux of the philosophy that we have, which is totally different than the transactions that you saw here.

Counsel then asked questions apparently designed to elicit information from Pruitt as to the comparative return on investment if Univar had purchased the notes instead of Barbadosco having purchased them. The following exchange took place:

Q. … For the Barbados company the only source of income was the interest received from Europe?

A. At this time, yes.

…

Q. So the Barbados company did not carry on any chemical distribution business, did it?

A. No, it was an investment company.

Q. Yes. So I thought your policy was that the Canadian subsidiary was to find new investments that were related to its core business?

A. Related to operating company business, yes, as contrasted to investing in public securities.

…

A. Marketable securities, like on the New York Stock Exchange or something like that.

Q. Yes. Now you will see from all these financial statements that there were some expenses from Barbados, not inconsiderable amounts, the Barbadian corporation income tax payments albeit only two and a half percent, amounted to - - were in the range of $60,000 per annum. The other expenses in excess of $100,000, so that only the net remained available for distribution to the Appellant by way of dividends, correct?

A. Yes, sir. Yeah, the balance of the net income after those expenses would be the only amounts that would be available from that year, yes. And dividends were paid, in this year of $2,000,072.

Q. Right, in ’97, right.

A. In 1997, yes, sir.

Q. Whereas if the Appellant had acquired these European notes itself, it would have received interest income of $2,000,488. So the interposition of the Barbados company decreased the Appellant’s income, didn’t it,

> because its dividends were less than the interest income received.
>
> A. No. These notes were never owned by Van Water & Rogers Limited[8] so did not decrease - - I don't understand the question.
>
> …
>
> Q. I'll merely pose the question of that if that happened, you would agree that the interest income - - that the income to the Canadian company would have been larger than what it received from Barbados.
>
> A. I don't know that because I don't know what all of the costs associated with it would be in that kind of structure. It had never been evaluated so I never - - it was never - - I simply - - it had never been proformaed so I had no idea what - - I don't know what the impact would be because there may be all kinds of considerations it would have to have, have to be made. It has never been presented, never been considered to be done.

Counsel then, in reference to Barbadosco said:

> So this was a tax plan, wasn't it, in essence?

Pruitt responded:

> No, that's not true. These were tax people that were talking about specific tax rules and the implementation of the plan and so every transaction that I've ever been aware of and that we've been involved in, has tax aspects to it. And so you always need to have lawyers, tax advisors and various technical people that have to address those elements of the plan. It does not make it a tax plan, it simply makes it a - - I acknowledge that there are tax aspects to everything, including this one, that need to be carefully planned and worked through by the tax professionals. And that's what they're doing.

Counsel for the Respondent, after reading two paragraphs from the October 26, 1994 UC Finance Committee meeting had this exchange with Pruitt:

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[8] Univar.

> Q: … My question, Sir, is: These two paragraphs taken in conjunction show that there was at least a tax element in this NEWCO plan, if it was not the only purpose of it.
>
> A: The primary purpose was that of debt restructuring and recapitalization which we have gone through. This was being described by Mr. Lundberg which I'd asked him to cover the description. Mr. Lundberg is a tax person so everything he describes is going to be described from a tax perspective; its natural, and the first paragraph that you referred to he was describing for the Finance Committee - - I remember this very specifically – the overall structure of his department, how he goes about things, what he's doing - - typical, appropriate governance of the Committee to understand how we manage our tax compliance and who does what, where and how its organized. That's really what this - - and what strategies and exercises are going through or being worked on. I had also asked him to address the restructuring and recapitalization project that we had been working on.
>
> Many of the issues of implementation related to tax issues of implementation, and so I felt that it was best that he be the one that sort of is most heavily involved in this discussion in the event that there were questions. For example, in one instance we had a ruling from the U.K. that was necessary to obtain. A number of other issues that needed to be dealt with so he was the logical person to kind of coordinate the description of this. Naturally, his words would be tax oriented and that's also when we asked for approval from the Finance Committee to go forward with the overall character - - or the overall project. So, it does not mean or reflect that this is primarily a tax issue at all. There were tax elements to it, of course, as with all transactions.

Pruitt then described the process of obtaining a revenue ruling from the United Kingdom tax authorities to make sure that they had clarity with them as to how the reclassification from non-interest bearing loans to interest bearing loans were going to be treated within the UK. He then said there were some issues in Scandinavia and said that Canada was considered, the U.S. was considered, and Barbados was considered. Respondent's counsel then said:

> Q: I'm not interested in the U.S. or Scandinavian or UK tax considerations. I'm asking you specifically: What Canadian tax considerations were there?
>
> ...
>
> A: Frankly, I relied on tax experts and I honestly - - the only specific ones I remembered I mentioned to you and they did not relate to Canada so…

Counsel after reading a portion of the minutes of Univar Board of Directors meeting on October 15, 1993 said:

> I put it to you, Mr. Pruitt, that the core intention here was that it was the Appellant that was to purchase this interest bearing debt and that this purchase was to be affected through this Barbados company.
>
> A: That would not be an accurate statement. It would not be true.

Counsel did not continue with that line of questioning.

[37] Pruitt also said:

> ... I think that the characterization and the same would apply with my comments on the early one that we apply to the characterization of a tax strategy more had to do with the implementation elements which by that time, I think it was - - the language got to be somewhat careless on occasion because so many of the issues that get talked about had to do with taxation issues. And I give you - - a good example is the revenue ruling or Inland Revenue ruling that we needed to have in the UK and so forth. But where so much of the discussion centered around tax approvals and tax issues. With this comment that he made as well as the comment on the minutes that … you just had me read where they referred to tax strategies really that was not the only element.
>
> Certainly tax was a portion of it, but the primary element, again, was to the recapitalization process, the debt-to-equity ratios that needed to be aligned, that had to do with alignments of targets and alignments with incentive compensation. So there were many, many factors that

> needed to go on here and so - - and everybody understood that well including Mr. Rogers and myself in the previous one, just because Bill Butler may have used the term "tax strategy" does not change its purpose or its primary purpose at all.

This exchange followed:

> Q. … My question to you, sir, is this: You said in response to this that the Appellant's performance was still outstanding but that because there was no leverage at all in the Appellant the excess cash continued to climb and therefore the Appellant had difficulty finding investments, correct? He was looking for investments but had difficulty finding investments that were close to the core of the Appellant's business, chemical distribution business, correct?
>
> A. They were having trouble finding adequate investments that related to operating businesses, yes, and in sufficient amounts to utilize their excess cash or debt capacity. And even though their returns are exemplary, certainly, and the operations of the existing business was very, very good, no complaints, but the challenge is that if you're under utilizing your capital base you're not expanding the share value associated with the investments in that enterprise and so you need to be able to go out and grow your business faster so that you could appropriately utilize the capital that's available in the business. That was the challenge.

[38] Respondent's counsel then suggested that it was open to the Appellant to ask UC to allow it to make investments yielding interest income similar to the notes purchased by the Appellant. Pruitt responded that "lots of things could have been done."

This exchange followed:

> Q. I'm suggesting to you, sir, that the reason the Appellant - - sorry, the Appellant's parent company, Univar Corporation, was not interested and the Appellant was not interested in doing this because this would have created interest income in Canada that would have been fully taxable in Canada. Would I be right, sir?

> A. I don't accept that as a premise because we had a tremendous amount of business in Canada and increasing business in Canada, increasing taxable income and we were fully willing to pay the full tax charge on that income, so I don't understand the relevance - - I mean, well, that's not for me to say, it's a speculation on speculation that - - so I don't know how to answer it. I'm sorry. If the answer would be is if there's taxable income in Canada would the company have paid its appropriate tax on taxable income in Canada, absolutely yes.
>
> Q. I'm suggesting to you, sir, that one of the principal reasons for going through with this NEWCO plan, Barbados Company plan, was to prevent the arising of interest income in Canada. Would I be right, sir?
>
> A. I don't recall that being a key point in discussion, sir. I just don't recall that being a key point of discussion. Whatever income is in Canada we're very willing and have always been willing to pay tax on that.

[39] In a discussion as to why Barbadosco was not liquidated until January 2000, and after reference by counsel to a memorandum dated October 15, 1999 in which the following appeared:

> In the beginning of the year 1999 the Canadian authorities published new tax legislation, effective January 1, 2000. This change in the tax law makes the structure with Van Waters Ampersand Rogers (Barbados LTD) no longer advisable.

Pruitt's response to this was:

> But that was written by Hugo Brink which was an employee of Pakhoed and was never around during that period of time at all. I mean this is in 1999. He wasn't there when Pakhoed - - when we developed Barbados, and so I wouldn't - - I wouldn't put much credibility to it although I wouldn't argue with the technical accuracy. But it wouldn't be reflective of what was in the minds of the people that actually did - - created it and were trying to go through it. He's a tax person, would explain it from a tax perspective, and he wasn't there at the time.

[40] On re-examination Pruitt testified that Royal Pakhoed was much larger than UC and was capable of buying UC, he assumed, without debt. He said that UC had 3,000 employees and that Pakhoed would have had many more.

[41] Pruitt was then asked, with respect to the winding of Barbadosco on January 3, 2000 why it took so long. His reply reads as follows:

> … it was tied to the major dividends to a degree and the extraction of monies out of Europe and North America, and frankly, some of us were trying to negotiate that they wouldn't take as much as they did, and that - - it was part of the reason for the delay as well as I know. And, you know, again it's not the major item. I mean, you know, you would discuss it and then they would put it on the back burner for a while and come back to it.

EVIDENCE OF WAYNE ARVID LUNDBERG

[42] Wayne Lundberg ("Lundberg"), a certified public accountant, was vice-president of Corporation Taxation. He joined UC in May 1977 and left in February, 1984, returned in December 1987, and is still with that company. His title, initially, was Manager of Corporate Taxation. In the mid-1990's he stated that he was Director of Corporate Taxation and in 2001 became Vice-President of Corporate Taxation. He said that his primary responsibility is the management and oversight of all issues of corporate taxation, managing the function of US corporate taxation, any aspects of international taxation or

> tax matters that would - - basically between more than one jurisdiction.

He said that during the 1992 through 2000 period there were more European operations than in the early 1990's. He said:

> In order to perform the functions we have engaged the accounting firm of Coopers & Lybrand to be the, what I call the umbrella tax service providers. On special occasion we would also employ the law firm of Baker MacKenzie as our consultants on both U.S. domestic and international tax matters.

He stated that the consulting accountants were Arthur Anderson until 1992. He also stated that he reported to Pruitt. He said that the Tax Department was considered an integral part of the Finance Department. He said that UE joined the group of companies in 1991 and that it used local companies providing tax services within a particular country. He then said that his role was to manage and coordinate the services that were provided. He stated further that he had no expertise in areas outside U.S. tax law.

[43] Lundberg said that UC filed its tax return on a consolidated basis, the only companies being consolidated with it for that purpose being its main subsidiary, the U.S. operating company ("Inc") and one or two other small U.S. companies.

[44] Lundberg said that Univar had paid only one dividend, namely, a dividend in 1980 of 6 million dollars and that UC claimed a U.S. foreign tax credit with regard to withholding tax and the underlying Canadian tax that had been paid on the income that was distributed. He said that:

> …the dividend would have been what we call grossed up, so it was treated as having been on a pre-tax basis, and then a U.S. tax would have been applied on that amount of grossed up dividend, and a foreign tax credit claimed up to the amount of the U.S. tax on the dividend income.

He then testified that there would have been excess foreign tax credits to the extent that the withholding tax and the taxes that came with the dividend, the deemed taxes paid, were in excess of the U.S. thirty-five percent tax rate.

[45] He said that UC was sensitive to the fact that Univar had, over a period of time, incurred Canadian taxes at a rate greater than the U.S. tax rate. He explained that to the extent that the credits could not be used in full, they would have become excess foreign tax credits, subject to a carry-back period of two years and a carry-forward period of five years.

[46] Lundberg then said:

> The management of Univar Corporation had had a long standing policy that a dividend would not be taken from any foreign subsidiary if it could not be taken in manner that would be at least tax neutral to the company on a consolidated basis.

[47] Notes to the financial statements of UC respecting the 1993 taxation year, with comparative figures for the previous two years stated in part:

> No provision for foreign withholding or United States federal income taxes is necessary as it is management's intention that dividends will be paid only under circumstances which will not generate additional net tax cost.

Lundberg, after reviewing the Summary of Accounting Policy stated that UC management had a policy that it would not make dividend payments in any situation if the result would be an increase in income taxes. He also referred to UC's

> …inability to fully utilize the credits that would come with such a dividend from Canada… either these deemed taxes or the withholding tax.

He also said:

> The philosophies of the Tax Department of the Univar Group were to manage the effective income tax rate for the Univar group on a worldwide basis. An underlying policy that we would want to do tax transactions or enter into transactions that had tax results only if they fit into the general purposes of the company and they had a business purpose that would be applied. The phrase that we used was that in our company the tax tail wouldn't wag the business dog.

[48] Lundberg was then referred to the agenda of a Univar Tax Planning Meeting and especially to the following agenda item:

> 3. "Recent U.S. ordinary tax business developments", the Univar multinational tax management strategy.
>
> 4. "Canadian Financing, purchase of Univar Europe debt."
>
> 8. "Creation of international sourcing company", referred to as ISCO.

> 9. Regard UC, and its U.S. operating subsidiary to charge test subsidiary for services provided (engineering, environmental, legal, insurance, human resources).

He was then referred to an item in an inter-office memorandum from him to Pruitt dated November 22, 1994. It referred to an outstanding notice of objection filed by Coopers & Lybrand respecting Revenue Canada's assertion of guarantee income to Univar as a result of that Canadian company guaranteeing U.S. debt.

[49] The second item dealt with the reduction of Canadian withholding tax from ten percent to five percent with the resulting lesser amount of withholding tax on any future dividends:

> …and therefore a lesser amount of Canadian taxes that would be subject to utilization in the U.S. as foreign tax credits, and it would be subject to any potential carry-forward if they couldn't be utilized to the fullest extent.

Lundberg then said that for a period of time UC had been looking at means of trying to generate qualifying foreign source income to UC that would be either low or untaxed by foreign jurisdictions, therefore becoming available for use of the excess foreign tax credit carry-forwards. He said:

> One of the things that we had looked at and discussed was having the possibility of the U.S. operating company make sales directly into Canada to existing Canadian customers that would be taxable in the United States currently but would be structured in such a manner that they wouldn't be taxed in Canada. Therefore, they would become valuable foreign source income to the U.S. company for its U.S. international tax, foreign tax credit issues.

He then said that such plan was not ultimately adopted because of potential perceptions by customers of the Canadian company that would not be favourable, and Univar's objection based on its independent business operating method.

[50] Appellant's counsel then returned to agenda item number four asking if "the NEWCO plan was implemented." Lundberg said that is was connected to excess borrowing tax credit utilization and then followed with:

> From a U.S. foreign tax credit utilization point of view, this NEWCO plan was effective in that it did not impair the ability of the U.S. company to utilize its foreign tax credits. It did not create a transaction that would have been determined to be a deemed dividend, which would have in itself then triggered additional foreign tax credits and related to excess foreign tax credit problems in the U.S., and as part of the overall NEWCO plan there had been a recapitalization in Europe. The result of that recapitalization was a higher level of interest bearing debt, and therefore interest income payable by those companies.
>
> And then finally, the results of the NEWCO transaction enabled the U.S. company to receive cash as a result of the sale of those notes to the Barbados company. That cash was used to pay down debt in the U.S., and as a result of the pay down of the debt there was less interest expense in the U.S., and there was a procedure, a calculation under U.S. tax law that made it beneficial for us to - - for us, the U.S. company, Univar Corporation, to have a lower level of domestic interest expense.
>
> …
>
> Under a U.S. tax rule, under Internal Revenue Code Section 861, beginning in 1986 there has been a process, a calculation that was made whereby annually the U.S. consolidated group of companies would do this, a calculation and a certain portion of expenses that were incurred were considered to have been incurred in the process of creating foreign income. The net result was that a portion of foreign source income that would have otherwise qualified for U.S. foreign tax credit benefit was disallowed that benefit. As a result, in and of itself in that transaction, there would have been a higher excess foreign tax credit. Paying down the interest expense in the U.S. helped - - or alleviated some of the adverse impact of that calculation.

He then said that the NEWCO plan would not result in a deemed dividend and was therefore beneficial from the U.S. excess foreign tax credit point of view. He referred to the Internal Revenue Code having provisions that addressed certain circumstances that could result in a dividend being deemed paid by a foreign subsidiary, "in this case the Canadian company, to the U.S. parent company". He explained that in approximately 1988 Univar had been asked to sign as guarantor on credit facilities of UC and under the Internal

Revenue Code, a guarantee by a foreign subsidiary of the U.S. parent's debt was deemed to be a dividend payment from the foreign subsidiary, i.e. from Univar to UC

[51] Lundberg went on to say that although the Canadian company ceased to be a guarantor on the line of credit, in its place a credit facility was established where the Canadian company, along with other companies in the Univar group, became a joint and several liability borrower under the credit facility. He said that professional advice indicated that there was a significant exposure and a significant chance that the condition of joint and several liability on the debt would be considered, at least by the U.S. Internal Revenue Service, as being equivalent to a guarantee "and therefore would have resulted in the same deemed dividend situation." He said that Univar ceased to be a joint and several borrower on June 1, 1995 when a new multi-currency line of credit was established and Univar and other foreign subsidiaries of UC were the designated borrowers on that credit line. When asked by counsel why then Univar would not buy the notes receivable from UC, the multi-currency line of credit having solved the deemed dividend question, Lundberg replied:

> I don't know that there was ever an opportunity for the Canadian company to borrow those - - to buy those notes directly. My concern, based on advice that I had received, was that there was a possibility that purchase of those notes by the Canadian company directly could in fact amount to a deemed dividend distribution and investment in U.S. property or an indirect loan to the U.S. company, which would have triggered the conditions of Internal Revenue Code Section 956. In addition, the structure that was in place beginning in 1991 when these interest bearing notes receivable were first put in place, were done so specifically so the interest income would be qualifying foreign source income to the U.S. company.
>
> …
>
> If the interest bearing notes receivable had been held directly by the Canadian company that would have no longer been in and of itself a qualifying foreign source income to the U.S. company, and we would have lost a very valuable benefit in how we were managing the exposure for excess foreign tax credits
>
> …

> It was part of the reason why the Barbados subsidiary was incorporated. There were - - the plan that had been designed by Baker and MacKenzie, and then further Cooper's & Lybrand for the company, for the companies combined was to basically solve some underlying Treasury concerns that were in place for the company. Mr. Pruitt had been, as I understand it, from conversations with him, had been concerned for some period of time about the balance sheet of the Canadian company and the fact that it had a great deal of equity and had virtually no interest-bearing debt, which was not in accordance with what I understood to be the company's policy on treasury management. I also knew from conversations with Mr. Tole over a period of time that Van Waters & Rogers Limited[9] had become very profitable, was accumulating a significant amount of cash, expected to be doing so in the foreseeable future, and needed to have a vehicle by which it could effectively invest that excess cash in a manner that was acceptable to the company.
> …
>
> and from the - - purely from a tax management side, that I was concerned with, it was a solution that allowed the transactions to take place without creating adverse tax consequences to the U.S. company with regard to this foreign tax credit position and without incurring additional tax that would have caused harm to the company.

[52] After some further evidence, the following exchange took place between Appellant's counsel and Lundberg:

> Q: And you gave evidence, I recall, that the Barbados company was necessary to avoid the 956 problem because Canada shouldn't buy it directly? Am I understanding that correctly?
>
> A: You are understanding that correctly from the standpoint of based on the advice that we had received, there was a concern that having the Canadian company buy the notes directly would have produced an exposure for deemed dividend treatment under Internal Revenue Code Section 956. But that wasn't as a guarantor. That is under the other provisions of that Code section.

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[9] Univar

> And as I also mentioned previously, another reason that would have been detrimental to us from a foreign tax credit management point of view was the interest on these notes receivable had to be directly included in the U.S. corporate income tax return as qualifying foreign source income, and it gave us some relief or some favourable benefit in the overall management of this excess foreign tax credit position.

[53] After some discussion with the Court Lundberg said that:

> … the interest income received on those notes by definition of U.S. tax law was qualifying foreign source income. It was not taxed by any non-U.S. jurisdiction.
>
> So as such, it came into the U.S. return without foreign tax directly.
>
> …
>
> It was earned by the U.S. company, the notes were held in the U.S.
>
> …
>
> And as such, there was no taxation of that interest income other than in the U.S.

He then affirmed that this gave UC foreign source income that would help its excess tax credit problem, that is having the problem of the U.S. consolidated group.

[54] Mr. Lundberg explained that if the notes were held by the Barbados company the rules and calculations resulted in the interest income being included in the U.S. return in the same manner as they would have been had they been made directly. He explained that this was because they bore a very low rate of taxation in Barbados. He said further that those same rules would determine that if the income was received directly by the Canadian company, the Canadian tax on such income would have been high enough to prevent the inclusion of that interest income in the U.S. returns simultaneously. He explained that the distinguishing factor was that if the taxation of the income was at a rate less than ninety percent of the U.S. rate, then the income was automatically included in the U.S. He stated that the Canadian tax rate was greater than ninety percent of the U.S. rate

> and accordingly there was no inclusion in the U.S. tax return at the same time.

In other words he was stating, as he explained, that it would have not been foreign source income for the U.S.

[55] Lundberg explained that all of this information would have been relayed to Pruitt.

[56] He then referred to some documentary material with respect to professional advice respecting the formation and use of "Barbados as an international financing company" because:

> We wanted to have some assurance as to what the results and the ramifications were from forming such a company.

[57] Lundberg said:

> This is part of an integrated plan. There were Canadian issues that were being looked after, to make sure that we were in compliance with the rules and regulations. There were U.S. issues that were being looked at. There were United Kingdom issues that were being looked, and there issues in Scandinavia, as well as the Netherlands, those were being looked at. So this is just part of what was a coordinated plan relative to the business transactions that were being undertaken as proposed and actively being done by Mr. Pruitt and Mr. Tole.

The following exchange then took place between Appellant's counsel and Lundberg:

> Q: So are you telling me that this wasn't primarily done, the NEWCO plan, for Canadian tax reasons?
>
> A: The NEWCO plan and the formation of this new international financing company was not being done for exclusively or particularly, primarily for Canadian tax purposes. It was being done for treasury and for cash management purposes. It had certain tax functions that were associated with it, but those were by far not the primary purpose and plan why the NEWCO plan and the NEWCO structure was put in place.

[58] Mr. Lundberg was referred by counsel to a memo written by him dated January 31, 1995 relative to the NEWCO plan and the establishment of the finance company. He said that the discussions were with regard to the economic profitability of NEWCO, the Barbados company to be organized, interest rate spread, combination of cash and borrowed funds to be invested in NEWCO, the long-term nature of the investment versus the temporary leverage or borrowing that would take place that would be subject to pay down – historic interest rate movements, potential for NEWCO as the treasury centre

> or this international financing centre that was being planned for the use of that company.

When asked by counsel why he was generating a lot of memos and letters he said:

> Well first of all, I'm a pretty detailed person. I deal with a lot of fairly complex tax issues. I write notes to myself or detailed memoranda so that I can document what the issues are, what concerns if any I may have, to leave a trail for myself, and where appropriate to advise the people who were also participating in this plan as to what certain circumstances or conditions were. But effectively I write a lot of these things just because it seems to be the nature of the beast of tax administration and that's how I just conduct my affairs personally… I think this is very typical of what I would do insofar as anything pertaining to management of U.S. tax, overseeing the integration of international tax plans.

[59] Lundberg then was referred to RECO, a U.S. real-estate company. It was a plan that would have allowed the Canadian company to use its balance sheet and its leverage capacity to make investments in real property in the United States. He described it as a plan in which Pruitt was interested. He said it had nothing to do with the generation of foreign source income. He said it further was not adopted, it being a less viable planning alternative to NEWCO.

[60] He described an international sourcing company ISCO which was on the agenda. He said it would have direct application to the creation of qualifying foreign source income within the U.S. company. He said that the concept was an international sourcing company, an international purchasing

company which would be set up to acquire chemical products, generally in foreign jurisdictions and then sell the products to Univar and to Inc. It would be entitled to generate income and it would come under U.S. tax rules, would be a qualifying foreign source income and would have been an assistance in managing UC's foreign tax credit position.

He also discussed the concept of charging certain expenses from UC and Inc. to Univar in order to position those expenses in a forty-five percent rather than a thirty-five percent environment. He said that it had nothing to do with foreign source income or foreign source tax credits but was merely a discussion of charging expenses from UC to Univar for services that UC provided, in a staff capacity, to Univar. He said that that was undertaken for a year or so and then terminated. He summarized the foregoing by saying that the company policy was not to enter into transactions that have "a tax payoff" if it didn't make business sense.

[61] Lundberg then described minutes of a UC Finance Committee meeting on October 26th, 1994 in which his presentation was, in his words:

> …consistent with the overall tax profile of the company and with my role in managing that profile. The presentation was made basically at the request of one of the members of the Finance Committee to try and have an overview presentation of how the corporate tax affairs were being managed.

That memorandum referred to a "flip" transaction described as a method of overcoming certain tax provision problems that would require UC to be greater than fifty percent foreign owned. He said that it was not pursued because it didn't "make sense for our company", it having been brought to the meeting's attention by a member of the Finance Committee who had asked for a general overview of the tax management of the company. He then referred to the discussion of excess tax credits which he described as being very valuable to the company, and continued:

> …and we needed to try and find ways to plan the business of the company and to plan for sufficient and appropriate foreign sources of income that could be used to utilize these credits.

[62] Lundberg was then referred back to the UC Finance Committee Minutes of October 26th, 1994 which contained the following words:

> Mr. Lundberg described in detail one strategy that involved the restructuring of the Univar Europe shareholder loans from the holding company level to the European operating level.

When asked by Appellant's counsel whether that was a "Canadian tax strategy" he answered that it was a strategy that was both European and related to the formation of the foreign offshore financing subsidiary of Canada. He said that the benefit from a U.S. strategy was as these loans were being restructured, as the recapitalization was occurring into Europe, UC was creating more interest-bearing debt in the European structure and as a result, created more qualifying foreign source income to UC related to that interest income. The following exchange then took place:

> Q: Now sir, were these transactions that are described here primarily done for tax reasons?
>
> A: No sir. These transactions that were done were the tax implementation processes of accommodating the business plan… to accommodate the concerns of Mr. Pruitt over the balance sheet position of the Canadian company, to accommodate Mr. Tole with regard to the cash position for the Canadian company, and to allow that kind of a transaction to go forward without creating additional adverse tax results.

[63] He then was referred to a memorandum from him to Mr. Lougee ("Lougee"), Financial Director of UE. He said that this was sent because they had planned a meeting with the board of MB Sveda AB, the Swedish operating company, that was one of the companies to be involved in the recapitalization of the European balance sheets. Lundberg said that with respect to any transactions involving a local country or local jurisdiction personnel, he kept those people involved in the process.

[64] Part of Lundberg's memo read:

> Hopefully, this would make it apparent that the Canadian tax rate of 45 percent makes it very advisable to structure a plan that will allow the company to reduce the impact of Canadian taxes on a multi-national consolidated basis.

With respect to that he said that one of his responsibilities was to manage the effective tax rate of the UC group on a worldwide basis. He said he was pointing out that tax rate to Mr. Lougee and other people from the MB Sveda AB board so that they would understand the process involved,

> …the leveraging up of the Canadian company and that there would be a tax benefit related to that that would be beneficial to the company.[10]

[65] In a memo from Lundberg to Mr. Elwood, Lougee and Pruitt, he said:

> … that critically important operational considerations should not be overlooked and that no action should be taken to achieve a tax result which was counter-productive to operations.

[66] He explained, regarding a discussion with Ingvar Severin, president of the Swedish company, with respect to his concerns about debt reorganization that

> no tax related transaction would be undertaken if it didn't meet sound qualifying business purposes.

Lundberg explained that the amount of debt placed within the Swedish company was reduced in order to help meet the UC's overall policy.

[67] Lundberg was then referred by counsel to a memorandum dated January 18, 1995 indicating the then current status of plans to restructure debt in the Netherlands, the United Kingdom and Sweden and to place new debt in Denmark. He said that it was necessary, as part of the European debt restructuring, to collapse tiers of companies. He explained that as a result of the manner in which the European companies were acquired in 1991 there were four tiers of foreign companies in the United Kingdom and in Sweden, some of the operating companies being at the fourth tier. He explained that this was a concern because under U.S. foreign tax credit rules, foreign tax credits could only be claimed "down to a third tier of a foreign entity." Lundberg explained that the first step was with regard to putting the interest expense directly at the operating company level in the United Kingdom, in Sweden and in Denmark, to consolidate operations and to eliminate idle

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[10] "company", in context refers to UC.

companies or unnecessary companies. He said the second reason, based upon advice received from advisors in respect of NEWCO was that:

> …it would be appropriate for the debt to be placed at the operating company levels in Europe.

He said that the purpose of the European debt restructure wasn't primarily for Canadian tax purposes but that the reasons for the creation of NEWCO were predominantly treasury related. He said:

> They had to do with the Canadian company and its excess cash position, and it had to do with Mr. Pruitt's concern about recapitalizing or appropriately leveraging the companies throughout the Univar worldwide group.

Lundberg was then referred to a number of memoranda which had to do with the implementation issues in the United Kingdom and in Sweden and in Denmark. With respect to same, the following exchange occurred:

> Q: Did Canadian tax considerations primarily motivate the European debt restructure based on your comments in the December 28th, 1994 memo?
>
> A: No, Canadian tax considerations didn't primarily motivate that. There were motivations for tax issues that had to be considered and implementations that had to occur in the United Kingdom, in Sweden, in Denmark. They had connection to the transactions or the arrangements that were in place relative to making sure we were in qualifications for the rules and regulations on the NEWCO structure. But these were basically representing - - or discussing a number of tax considerations … not primarily, exclusively with regard to Canadian tax.

[68] Lundberg then described UC's foreign tax credits as an asset of the company in that they could be monetized through the creation of qualifying foreign source income within the U.S. consolidated group, thereby using the tax credit carry forwards.

[69] Lundberg also said:

> The NEWCO plan itself was going to assist with the foreign tax credit issues because as a part of the overall

> plan that I referred to or that we referred to as the NEWCO plan, there was additional interest bearing debt put in place in Europe. That increased the amount of interest qualifying foreign source income in the United States and therefore gave us a better basis for utilizing foreign tax credits in the future.
>
> …
>
> Adding interest bearing debt in Europe increased the amount of interest income that the U.S. company received, and that interest income was qualifying foreign source income that could be used to absorb excess foreign tax credits. So the greater amount of interest income we had coming from Europe, the greater benefit we had for our foreign tax credit purposes.

[70] Lundberg said further that there was a second component, namely that through the NEWCO plan, UC was going to receive cash in exchange for the notes that it sold and use that cash to pay down its domestic debt. He said:

> As a result of this transaction, the NEWCO transaction to its conclusion, the U.S. company paid down debt, therefore had less domestic interest expense that was subject to allocation to that foreign source income.[11]

[71] In response to counsel's question as to why UC did not deal with the leverage issue by just causing the Canadian company to declare a dividend, Lundberg replied that a deemed dividend or an actual dividend would produce the same results, namely that UC would receive them, the taxes would be fully creditable but there would be a limitation on the U.S. side which would create excess tax credits - - foreign tax credit carry forwards. He reiterated that the existence of the Barbados company was important in helping monetize the excess foreign tax credits.

[72] He then described the acquisition by the Barbados company, as an international finance subsidiary. Respecting Berk, he said:

> …the plan that we developed and were counting on was that the Berk acquisition would be the next investment in what we hoped would be a succession of investments, using the international financing company in Barbados.

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[11] Lundberg explained that there was, therefore, more foreign source income available to use the excess tax credits.

> … and the Berk acquisition actually occurred, I believe December 1st, 1995.

Lundberg stated that, as Tax Manager, he knew that certain reductions had been vested and that he, of his own accord, not having been asked by Pruitt, brought this to Pruitt's attention, saying:

> I provided this information to Mr. Pruitt. I saw this just as a responsibility that I had under the normal role that I was playing…
>
> There were some procedural things that had to occur in order for us to get the right structure in place, and so the plan was that Barbados was going to finance -- or acquire the interest bearing note in the same way it had acquired the original interest bearing notes.

He then described the purposes of creating foreign source income to UC from these interest-bearing "notes receivable", and therefore enhancing the utilization of foreign tax credits by UC in its consolidated tax return.

[73] With respect to tax ramifications both in the United Kingdom and Canada Lundberg said:

> It was my responsibility, in managing the international tax function, to try and understand any potential issues that would come into play on any of our transactions, take advice from the appropriate people, in this case it was the people at Coopers & Lybrand, and make sure that we structure transactions and implemented transactions in a way that would be in accordance with the rules and then I relied upon the opinion of Mr. Hornsby[12], Mr. Bergen relative to this transaction.

[74] Lundberg then discussed the sale of a Berk interest-bearing note to Barbadosco. He said that transaction did not take place because, although it had been approved, in July, 1996, UC

> which had been an independent company, was acquired 100 percent by a company by the name of Royal Pakhoed, and on that particular day the operations and the policies,

[12] With Cooper's & Lybrand in London, England.

> everything with regard to Univar Corporation and the tax management, the treasury management, everything else changed dramatically because as we came to learn, Royal Pakhoed had a very different manner of managing their corporate affairs.
>
> …
>
> They were very much interested in extracting cash any place and every place that they could. And they managed all of their affairs just very differently... from Univar Corporation.
>
> …
>
> I had been having meetings with Mr. Brink[13]… and his particular point was they had no desire to maintain the Barbados company would like to liquidate it and take the investments out of Barbados and ultimately put them into Europe where they managed their financial affairs.

Lundberg described the negative monetary effects on moving all money up to Royal Pakhoed including the adverse effect of the U.S. overall foreign tax loss, concerns with regard to the foreign tax credit issue, et cetera. Lundberg explained that the overall foreign tax loss ties into the excess foreign tax credit system because it eliminates the ability of UC to claim foreign tax credit on a certain portion of foreign income that would otherwise be eligible for foreign tax credit treatment. He said:

> The overall foreign loss ties in to that question because it eliminates the ability of the U.S. company to claim foreign tax credit on a certain portion of foreign income that would otherwise be eligible for foreign tax credit treatment.
>
> The U.S. rules go through the calculation, as I indicated before, and conceptually treat certain domestic expenses as if they were associated with the production of foreign income. In that regard they offset the foreign income with those allocated expenses, and that then eliminates the ability of the U.S. company to claim the foreign tax credit on that amount.
>
> For instance, if the calculation was of $10 million of allocated expense, either in the current year or cumulatively over a period of time, and if a $20 million dividend was

[13] V.P. tax, corporate secretary of Royal Pakhoed N.V.

> paid from the Canadian company, these rules would eliminate the ability of the U.S. company to claim a foreign tax credit on that $10 million. In essence it would produce an additional U.S. tax expense of $3.5 million.

He said that this concept of overall foreign tax loss was relevant in 1994 in planning the NEWCO transaction in that it affected the ability of the U.S. parent company to utilize foreign tax credits on a carryover - - either on a current year or as carryforward into the future.

Lundberg then said that beginning in very late 1998, in a 13 month period of time, Royal Pakhoed took $113 million out of the Canadian company.

[75] When Lundberg was asked what impact Canadian laws had on the winding-up of Barbadosco and the distribution of cash of $113 million from Canada to Royal Pakhoed, he replied that the dividend payments in that amount were not affected in any way by the proposed amendment of Section 17 of the *Act*. He said that Canadian tax was not the only reason why Barbadosco was wound-up, specifying:

> The changes in the law that came about were … not necessarily more important or less important than the overall consideration that Pakhoed had and how they wanted to manage the company.

Lundberg said that the liquidation of Barbadosco was already being discussed in October, 1997 before the income tax changes respecting Section 17 were announced. He also reiterated concern over Section 956 or any other provision of the U.S. Revenue Code respecting the use of foreign tax credits because of no qualifying foreign source income.

[76] With respect to a memo from Mr. Brink, of Pakhoed, which read as follows:

> History – Van Waters & Rogers (Barbados) Ltd. was created in 1995. For the founding of the company there were several reasons:
>
> - placing debt in Canada
> - returning cash to the U.S.A.
> - no Canadian withholding tax.

Lundberg said:

> Well, I think with regard to the first point of placing the debt in Canada, that certainly was the treasury objective that Mr. Pruitt had in mind. As a result of placing the debt in Canada it did, in fact, return cash to the United States, which was again part of the treasury transaction. And the transaction was put in place, there was not a Canadian withholding tax associated with that, which was related to the fact that the Barbados transaction as it was structured needed to be done in the way that it did not create additional tax to the company, which would have in turn given us a problem with regard to foreign tax credits.

He then reiterated that Royal Pakhoed had been intent on liquidating the Barbados company from the time it acquired UC.

[77] On cross-examination, Lundberg was referred to a memorandum and asked whether he generally understood the advice received from Coopers & Lybrand respecting the definition of "foreign accrual property income" ("FAPI") and the significance of active business earnings in the payor corporation. He was then asked if he understood if NEWCO "which turned out to be Barbadosco was to earn interest income from Europe, and pass it up to the Appellant by way of dividend. Lundberg replied that, generally, that was his understanding as explained by the advisors. Respondent's counsel then referred him to portions of the memo which listed three jurisdictions, namely Cyprus with a 4.5 percent tax corporate tax rate, Ireland, with a 10 percent corporate tax rate, and Barbados with a 2.5 percent corporate tax rate. Counsel then asked whether Barbados was selected as the jurisdiction for NEWCO based on the fact that it had the lowest tax rates. Lundberg replied:

> The selection of Barbados was exclusively based upon the recommendation of the advisors, predominantly Coopers & Lybrand, who were managing this project. I couldn't say that the selection of the lowest tax rate was necessarily a factor plus or minus. It was the recommendation of the advisors that in order to implement the NEWCO plan, that the appropriate jurisdictions for NEWCO would be Barbados.

Lundberg also said that the Appellant would borrow funds for the equity investment in Barbados, that the debt would be in Canada and that the

corporation had about $10 to $12 million on hand and would borrow some $27 million to purchase the debt owing to UC. He said he recalled seeing reference to a draw on the multi-national line of credit facility of $37,360,00 and stated that it had drawn another $15 million. Lundberg then said that his understanding was that on that day:

> …they made an investment of $37 million in the Barbados company through their bank account in combination of cash and borrowed money.

[78] When Respondent's counsel suggested that there were:

> …certain benefits, such as the deductibility of interest in Canada and the non-taxability of dividends expected in Canada.

Lundberg responded that those were the conditions explained by Coopers & Lybrand in their advice in getting together the treasury and cash management plan that was suggested that became the project known as NEWCO.

[79] Respondent's counsel then referred to minutes of the Finance Committee of UC of October 26, 1994 and read the following:

> Next, Mr. Lundberg presented an overview of the Corporation's tax strategies. He began by reviewing the objectives of the Corporation's multi-national tax management strategy, how the objectives are being implemented and the makeup of the tax team that assists in strategy development and execution. He then provided an overview of the current tax circumstances in each of the four primary tax areas facing the Corporation: U.S., Canadian, European and consolidated tax planning provision, and return issues. In addition, he reviewed the significant factors affecting the consolidated income tax provisions of the Corporation and methods to reduce the effective tax rates. He then provided an overview of previously implemented or in process tax strategies. Additional strategies with probable high payoffs and other strategies on a continuing consideration… Mr. Lundberg described in detail one strategy that involved the restructuring of the original Univar Europe shareholder loans from the holding company level to the European operating company level. In addition there was a

> conversion of some non-interest bearing debt into interest bearing classification. Those transactions were in preparation for the subsequent sale of those shareholder loans by Univar Corporation to a new Barbados subsidiary of Van Waters & Rogers Ltd., upon implementation of the multi-currency line of credit. After discussion it was moved and seconded and approved that the Corporation and each of its direct and indirect subsidiaries were authorized to execute any and all documents.

At this point Mr. Lundberg said that this was the NEWCO matter which was discussed at that meeting.

[80] Counsel then referred to a memorandum from Mr. Tole to Pruitt, Lundberg and certain other persons. He read the following portion:

> This presentation specifically concentrated on the impact of the 45 percent tax rate in Canada and the planning opportunities available to reposition profitability from Canada to the United States and to reposition expenses from the United States to Canada.

When asked what this meant, Lundberg said that they were general statements and that one of the responsibilities that he had in his role as Director of Corporate Taxation was to manage and oversee the effective tax rate of the company. He said further that this generally referred to issues that he would tend to look at and how they would evaluate the tax rate of any of the countries that were involved or any transactions they did – "just an effective tax rate management". The following exchange then took place:

> Q. But just on repositioning of - - reposition of profitability from Canada to the United States aspect, it was planned, was it not, that the Appellant was to borrow money, incur interest expense, and therefore reduce - - thereby reduce its profits in Canada, right?
>
> A. That would have been the result of the treasury strategy that was put in place that Mr. Pruitt was managing…to manage the balance sheet of the Canadian company so that there was going to be leverage put in place on that balance sheet. The end result would be that the interest would be deductible in Canada no matter what the purpose was, that the funds that were borrowed were used for.

When Respondent's counsel referred to another memorandum written by Lundberg he said:

> …it sounds like Coopers & Lybrand were telling you and the Appellant that this tax strategy complied with Canada income tax laws.

Lundberg replied:

> This is consistent with any of the advice that we had taken from Coopers & Lybrand over a significant period of time relative to the transactions I mentioned this morning in my testimony. Univar Corporation as an entire group does not enter into transactions that are tax motivated only, that there must be a business purpose for the transaction. We're particularly careful of being in compliance with the rules and this was not the first time that Mr. Bergen had advised that the NEWCO plan that had been devised by Baker MacKenzie and by Coopers & Lybrand was not considered to be an aggressive plan.

[81] Respondent's counsel then referred to an memorandum from Dieter Rechel ("Rechel"), an accounting manager with Univar, dated December 9, 1994. Counsel read the following:

> Various proposals were submitted by Rod for Ltd to purchase Univar Europe's debt from Univar.[14]

Lundberg said that that comment was not correct. He said:

> There was not an intention for the Appellant to purchase Univar's debt from Univar Corporation. The intent - - that's just Mr. Rechel's misreading of that. The intention from the very beginning was that those debts instruments, those interest bearing notes receivable were to be purchased by the Barbados company, not by the Appellant. …the only proposal that I was aware of was the plan that was being developed just as we have discussed it throughout the day relative to NEWCO.

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[14] Ltd, in context, refers to Van Waters & Rogers Ltd. which is Univar, the Appellant.

[82] Lundberg referred to steps that were going to occur to restructure the debt within the Swedish company and within the Danish company. When asked about non-interest bearing loans to Univar Europe, Lundberg said:

> That goes back to the original acquisition itself in 1991. The capitalization that was put in place was accomplished in three pieces. A very small portion of share capital, and then amounts of interest bearing debt and non-interest bearing debt. The real benefit of the interest bearing debt was to Univar Corporation in the United States because it amounted to qualifying foreign source income that we discussed this morning for foreign tax credit purposes.
>
> The reason for the use of the non-interest bearing debt was the intention at the date of the acquisitions that we would make the best estimate possible of the ability of the Swedish company and the U.K. company to service the debt that was in place, realizing that at a later point in time, one time only, we would make a recapitalization of those companies when it became clear exactly what their financial strength was and how their balance would look. …you could think of the non-interest bearing debt basically as an equity contribution. But because it was non-interest bearing, we had the ability to make a final adjustment and a recapitalization.

Lundberg said that the interest bearing debt created qualifying foreign source income that was of great value to UC. Lundberg also stated that the Danish company had not originally had any debt "in place" and in recapitalizing, there was an opportunity for us to utilize the debt capacity of the Danish company so that it could bear its fair share of debt on the balance sheet. He added that this increased the amount of interest bearing debt and, therefore, the interest income to UC for its foreign tax credit planning purposes. He then emphasized that the same would be true for all the other restructured European debts which included the Swedish debt, the UK debt and the Danish debt.

[83] When asked why it was important that interest expense payments made from operating companies be treated within the local jurisdiction as interest payments rather than dividend distributions, Lundberg replied:

> As I recall right now, it was just a general condition that we wanted to ensure the deductibility of the interest at the local

> company level. There was value to - - from a tax perspective and from a tax management perspective, to have the interest expense deductible as such by the operating companies, rather than some way having it to be interpreted as being dividend income and not deductible locally.

[84] Respondent's counsel then asked questions respecting the deductibility of interest in Canada being important, the monies received from Barbadosco not being FAPI, "non taxability in Canada of this interest on the Univar Europe notes" being an important consideration for the Appellant and UC. He also referred to a memo from Lundberg to Pruitt and to James Bernard[15] respecting Coopers & Lybrand advising that the management of Barbadosco should effectively reside outside Canada. He then asked the following:

> So these were tax reasons, were they not…?

Lundberg replied that he was relying on the advice received from that firm.

[85] Lundberg then, in respect of yet further questions respecting excess foreign tax credit issues, explained the significance of that concern to UC. In response to other questions from Respondent's counsel Lundberg said:

> As we had talked about yesterday during my testimony, there were several reasons for the development of the NEWCO plan, one of which was Mr. Pruitt's treasury concerns. One reason was Mr. Tole's concerns over the effective use of cash. And the NEWCO plan as it was designed was very helpful to us in that the implementation of the plan itself did not produce additional tax expense to the company that it would be unable to use. …we actually incurred a two and a half percent tax in Barbados, it was a relatively small tax, and we were able to, through the estimation of generation of foreign source income in the future, were able to record that two and a half percent tax as a tax credit that we would use in a future period of time, and although it could not be used in the tax returns at the moment, it became what is referred to as a deferred tax asset, an asset on the balance sheet of a company that was available for future use.

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[15] President and CEO until late 1995 and Director of UC.

Lundberg explained that the overall foreign loss is an allocation of U.S. domestic expense deemed to be attributed to foreign income and, therefore, disallowing the use of foreign tax credit to a certain extent. As a result of NEWCO purchasing debt owed to UC in the sum of approximately $27 million U.S., UC would pay down its debt with the result that it would have lower interest expense and therefore a lower allocation of interest expense in the overall foreign loss calculation. This was beneficial to the overall plan for use of the foreign tax credits, the overall foreign loss being reduced. Lundberg said:

> The overall foreign loss was a bad thing for foreign tax credit purpose uses.

because it eliminated the ability to take the foreign tax credit. Respondent's counsel continued, with the following question:

> If Univar Corporation had sold its Univar Europe notes to the Appellant and received proceeds to pay on the debt the result would have been the same, wouldn't it?

Mr. Lundberg replied:

> No sir. My understanding of the operations of the Subpart F provisions of the Code, of the U.S. Internal Revenue Code would have been that the interest income would not have been taxable in the United States if those notes had been sold to the Appellant directly, because one of the conditions of Subpart F of the U.S. Internal Revenue Code is a calculation, and it says if the income is being subjected to a tax rate at least 90 percent of the U.S. tax rate, then it's not considered Subpart F income and would not be included in the U.S. tax return. …if the notes had been sold directly to the Appellant, as opposed to Barbados, the income would have no longer been directly included in the U.S. corporate income tax return and Univar Corporation would have lost the value in its foreign tax credit management of the annual inclusion of approximately $2.5 million of interest expense.

[86] On re-examination, Lundberg reaffirmed that if the notes were going to be held other than directly by UC, it was important for them to be held by the Barbados subsidiary:

> …because under the provisions of Subpart F of the U.S. Income Tax Rules, that income would continue to be taxed to the U.S. company in the same manner as if it had been held directly by the U.S. company.

[87] In response to further questions Lundberg re-emphasized what he had said about overall foreign losses as follows:

> This was, as I was trying to describe earlier in my testimony, as Univar Corporation received the cash in the transaction of the sale of the notes, it now had cash available in the U.S. - - that it could use to pay down debt, whatever the source of debt was, and to pay down the debt. Paying down the debt then resulted in the U.S. company having less interest expense than it would have otherwise had. The OFL is - - comes about as the result of allocation of certain U.S. expenses, the most substantial of which was interest expense. So to the degree U.S. interest expense is reduced, the amount of that interest expense that would be allocated to the OFL is reduced, and the build up of the OFL is reduced accordingly.

[88] The witness, Patrick Tole ("Tole") is a chartered accountant, having joined Univar in 1983 and having been employed by the Univar group of companies since that time. He commenced as a senior accountant, became Vice-President of Finance and in 2002 became the Chief Financial Officer of the then ultimate Dutch parent corporation. He testified that he attended all meetings of the Board Directors of Univar in the period 1987 through 2000, in the capacity of controller. He said at that time that Larry Bullock ("Bullock") was Vice-President, western Canada, Fred Hermesmann ("Hermesmann") was Treasurer of Univar and Gary Pruitt was Vice President, Finance of UC. He also said that Paul Hough ("Hough") was President of Univar and A.C. McNeight ("McNeight"), who was formerly President, was Chairman of the Board of Univar. In May, 1994 James Fletcher ("Fletcher") was the Senior Vice-President of UC and James W. Bernard ("Bernard") was President of UC. William Butler ("Butler") was Vice-President, General Counsel and Corporate Secretary of UC and had become a director of Univar. By May 7, 1996 Hough had moved to the U.S. and had become President of UC while Bullock had become President of Univar.

[89] Tole testified that the Appellant was a distributor of industrial and agricultural chemicals throughout Canada. He said the Appellant's cash position in 1990 was approximately $13.9 million and in 1991 was approximately $16.2 million. It had short-term trade accounts payable, accrued liabilities and income taxes payable and a small amount of deferred income tax but no debt whatsoever, the company being very profitable.

[90] He said that UC and its operating subsidiary were borrowers under a credit facility with Univar guaranteeing those loans, it not being a borrower under that credit facility. In December, 1991, Univar acquired a competitor, Harcross Chemicals Canada, using its existing cash to acquire same.

[91] At the end of Univar's 1993 taxation year, its cash position was approximately $20.6 million. At the end of its 1993 year Univar, under a second credit facility, had borrowings of $18.7 million. Tole said that because of U.S. tax advice, Univar borrowed money under the second credit facility and, having no pending acquisitions or major capital spending requirements at that time had invested the monies in interest-bearing bankers acceptance notes. Tole then described the seasonal nature of its business in Canada leading to Univar's need to borrow under credit facilities that were available in order to pay suppliers because most of its customers would not, until the crop harvest production, be in a position to pay amounts owing to Univar. As at February 28, 1994 Univar had a cash position of approximately $5.6 million and had no bank borrowings. At that time, however, Univar was jointly and severally liable for any outstanding borrowings of UC and or its subsidiary even though Univar was not an authorized borrower thereunder. As at the end of February, 1995 Tole testified, with reference to financial statements that Univar had $11.4 million in cash, this sum not being used at year end.

[92] Tole, having been referred to a memorandum from Hermesmann to Rogers, McNeight, Bernard, Samson, Pruitt and Tole dated December 22, 1987, said that it was simply providing an estimate of surplus cash to be available at year end and said that Univar had paid off all its debt, had a healthy cash flow and "needed to begin thinking about what we should be doing with that". Tole explained that although the memo suggested that $7 million could be available to UC, no such distribution was made, Tole saying:

> No, it was not done. Well, the problem was that the company had a policy that it wouldn't take dividends out of the subsidiary companies if they were going to attract a sizeable amount of income tax or withholding taxes…and the philosophy of the company remains today, that to the extent that if we are able to leave funds within the operating companies as long as they have good investment opportunities, that can generate reasonable returns that's where the cash will stay, but, essentially, there was a policy to not repatriate dividends if they were going to attract additional income tax.

He also said that there had been only one dividend, namely a dividend of $6 million in 1980, that being the only dividend between the incorporation in 1950 and 1995.

[93] Tole then explained that Univar had purchased an agricultural distribution company in Canada in 1987, acquired Harcross in 1991 and acquired a small agricultural corporation, Wilber-Ellis of Canada in 1992, and had a lot of growth due to those acquisitions.

[94] Tole testified that UC had a larger corporate staff than Univar and was providing a number of services, including engineering services, when Univar was building new facilities and also services respecting health and environmental matters as well as international tax planning. He said:

> …we were a relatively sizeable international company and so we had to coordinate international tax issues, so they had someone on staff that we worked with in those areas.

Tole also stated that the group of companies had sales of approximately $1.8 billion in the 1993 year from the sale and distribution of a broad range of chemicals. A portion of the prose in a document that appears to be the annual report of UC was a statement that Univar

> is well positioned for future profitable growth in Canada. Our facilities, information technology systems, and experienced management team are well-suited to projected business opportunities.

[95] Tole expanded upon a statement under the heading "Business Acquisitions" in that report which read in part:

> During fiscal 1992, the Corporation completed acquisitions which provided entry into the European market and enhanced its competitive market position in the north eastern United States and in Canada.

He referred to Univar Europe and a number of operating companies in the UK, Sweden and Denmark, as well as companies in Italy and Switzerland. In the foregoing chain of companies, UC owned 51 percent of UE and Royal Pakhoed owned 49 percent thereof. In 1995 Royal Pakhoed sold its said 49 percent to UC.

[96] The aforesaid report, under the heading “Income Taxes” stated:

> No provision for foreign withholding or United States federal income taxes is necessary, as it is management’s intention that dividends will be paid only under circumstances which will not generate additional net tax cost.

[97] Tole then testified that as at February 28, 1995 Univar was jointly and severally liable for outstanding borrowings under the U.S. facility under which it could also borrow. Tole was referred to the consolidated financial statements of Univar as at February 28, 1991, a note which stated that as at February 28, 1991, UC and its operating subsidiary had outstanding borrowings of $96,700,000 U.S. under various credit agreements in which Univar was a co-guarantor.

[98] Tole then referred to the financial statements of Univar for the year-ended February 29, 1996. A note to the financial statements stated that Univar and its non-U.S. affiliated companies were authorized borrowers under a U.S. $90 million multi-currency credit facility. At February 29, 1996 Univar had borrowed $18 million Canadian under this facility.

[99] The witness was then referred to a certificate of incorporation showing the incorporation of Barbadosco on May 26, 1995. The directors of that company were Butler, General Counsel for UC and Mr. Carmichael (“Carmichael”) who was an attorney living in Barbados. He said that Barbadosco had issued 10,000 shares to Univar for a total price of $27,036,600 U.S. In describing the reasons for its incorporation Tole said:

> From the Canadian perspective it had to do with the excess cash that we've been talking about and the fact that cash was building and was going to be available, and the Canadian company was looking for investments. We haven't talked much about - - although we've made reference to the U.S. situation, whether it was a fair amount of debt on the balance sheet of the American company, as well as on the American subsidiary – little or no debt in Canada. So one of the issues that my friends in Kirkland were trying to address was to distribute the debt of the corporation appropriately onto the balance sheets of the various subsidiaries, including Canada.

He explained this by saying that it was an objective to achieve an equal amount of debt between the various operating units, to utilize the Canadian cash situation effectively. He said that it was an inefficient situation to have excess cash available and they wanted to have debt appropriately allocated throughout the corporation. He said also that they were in the process of converting some non-interest bearing debt in Europe to interest-bearing debt.

[100] Tole said that the objective of debt re-organization, from UC's perspective was:

> …that was a treasury function of the parent company and what they were trying to do was to allocate debt throughout the corporation, not have it all in the U.S. They wanted there to be an appropriate balance of debt and equity, to have strong balance sheets throughout each of the operating companies.

He said that Pruitt was the one that was most concerned about addressing the leverage.

[101] Appellant's counsel then referred to the Canadian issue of cash as one reason and leverage as a second reason and then asked whether there were any other reasons prompting the formation of Barbadosco. Tole said, referring to leverage, that it meant the amount of debt as compared to equity on the balance sheet of a company. He then said that the third reason was income tax. He stated:

> There were tax issues associated with the Canadian company's guarantee of the credit facilities, tax issues both in Canada and in the U.S. …my understanding was that

> there was a concern that by the Canadian company being either a guarantor or being jointly and severally liable under U.S. debt but not participating in borrowing under those credit facilities, there was a significant concern that there could be some sort of deemed dividend issue that would have resulted in a significant amount of tax being paid in the U.S.

He stated clearly that this was not a Canadian tax issue but was a U.S. tax issue. Tole then described a Canadian tax issue in 1989, 1990, 1991 and, he thought, 1992 when Revenue Canada felt that there should be a fee that would be charged under the circumstances where the Canadian company was a guarantor but not a borrower. He then said that Univar had been assessed a deemed guarantee fee. Tole said that the U.S. banks had requested UC to pledge its assets as security for a credit facility and it had planned to do so but as a result of securities problems UC found it easier to have Univar provide a guarantee to those banks rather than pledge shares. Tole then said that the Canadian tax problem was settled by the company agreeing to pay 15 percent of the amount originally assessed.

[102] When asked what purpose Barbadosco was to serve, Tole said:

> …there were essentially…three reasons. The excess cash that we needed to do something with, needed to find a reasonable investment; the issue of Mr. Pruitt trying to re-balance the debt and equity within the company; and then we were trying to address this tax issue, as well as the U.S. tax issue that I described. …it was essentially the setting up of the Barbados company was to me a rather elegant solution to really all of those issues. From our perspective, the primary one being the excess cash that was being generated. It was going to result in an investment in a subsidiary that was going to generate a flow of dividend income that would generate a better return than we were receiving than from just investing in short-term term deposits or banker's acceptances, et cetera. …From Mr. Pruitt's leverage situation, what it did is it gave us not only a use for the cash that was being generated, but it provided a vehicle for us to increase the borrowing in Canada. The proceeds from those borrowings would have ended up in the United States, which would have resulted in lower debt in the U.S. …so that we'd have more debt in Canada, less debt in the U.S.

Tole then explained that they took the cash on hand along with borrowed funds to capitalize or acquire shares of Barbadosco. Then Barbadosco used those proceeds to acquire the interest-bearing notes that were payable from UE to UC. Tole said that it addressed the leverage issue in that fashion. It generated a stream of dividend income to Univar:

> …and we felt was going to go a long way to addressing the tax issues that we had, because now, now the Canadian company would be not only a guarantor and jointly and severally liable, but would in fact be borrowing under the facility. …where their concern being that if there was a subsidiary that was providing a guarantee but wasn't borrowing, that the IRS might deem there to be some sort of deemed dividend, and again, because of the fact that the Canadian company was now borrowing under these credit facilities, the risk of that occurring was somewhat reduced.

[103] Tole said that there was no finance company other than Barbadosco in the Univar group. He said that it was not considered to be a short-term solution and that Univar still had the issue of continuing to generate a significant amount of cash. He said:

> …in setting up an international financing company, as Barbados was considered to be, it was essentially going to become a vehicle within the Univar group for providing financing to other companies within the group. At the same time, Canada would be able to utilize cash as it became available, generate a stream of dividend income that provided a better return than we could by just investing in short-term notes, and so it was kind of an elegant solution for all of those issues – that it wasn't just these notes that - - the three notes in question here. We were, over the longer term, we being Canada, looking at how we would invest the cash that we had, but also the U.S. parent was looking for ways to provide financing elsewhere within the corporation.

Tole then said that instead of investing in the stock market, Univar would make an investment in the shares of a subsidiary company and make an international financing company to be owned by Univar to generate a reasonable, low-risk level of return. He said:

> I mean, a stock market investment would, I think you would agree, have a certain amount of risk associated with it. That's not what we do, invest in a stock market.

He also said that there were other U.S. issues and inter-company financing but from the Canadian perspective it represented a reasonable investment.

[104] In the minutes of a meeting of the Board of Directors of Univar on May 14, 1993, under the heading "Other Business", the following appears:

> Mr. Pruitt informed the Board of a transaction being contemplated whereby V.W.&R. Ltd. would purchase from Univar a portion of the Interest Bearing Debt due from Univar Europe. The amount of debt being recommended for purchase is approximately U.S. $8.2 million. The transaction would involve V.W.&R. Ltd. capitalizing an offshore subsidiary with funds borrowed under the Univar Revolving Credit Agreement. The subsidiary would use these funds to purchase the debt from Univar Corporation. Mr. Pruitt indicated that planning for this transaction was in a preliminary stage and that the Board would be kept apprised of its status and that approval would be requested prior to implementation.

Tole said this was a general description of transactions which occurred on June 14, 1995 and that the company was making an investment in Barbados and Barbados would be the entity that was acquiring the notes. He then explained why the sum of $8.2 million rose to approximately $27 million. He said that borrowing under the Revolving Credit Agreement would assist the leverage concept of which he had spoken in that Univar would take a combination of cash on hand and borrowed funds to acquire the shares of the Barbados company. On the acquisition of loans from UC, UC would have cash that it could apply against its own debt and Univar's debt would increase. He explained that Univar was never given the opportunity to acquire the debt, that the investment was going to made in Barbados and the idea from the outset was that it would be the financing company that would acquire the debt. He said that the acquisition by the Canadian company of the debt was never part of the plan because it would not have satisfied all three of the issues that he had earlier mentioned and would have resulted in additional tax being paid in Canada. Tole then explained that the investment also concerned the consolidation activity of conversion of non-interest bearing notes payable by UE to UC in to interest bearing notes.

[105] Tole stated that the original proposal for the Barbados company came from UC, it knowing that Univar was generating cash and looking for good investment. He stated that:

> They had these other issues, tax, treasury that I referred to earlier and so it was their suggestion that we work with them and look at setting up the financing subsidiary.

[106] When asked why Univar chose Barbados as the jurisdiction, Tole replied:

> Well once, as the plan was developing we were working with outside advisors and the suggestion was that we needed to decide an appropriate jurisdiction for setting up a company such as this. And there were, I believe, four or five different jurisdictions that were proposed, and Barbados was on that list. Barbados happened to have the lowest corporate tax rate of those particular jurisdictions. And it was a jurisdiction that was - - where this type of international financing company there was a lot of these sorts of companies that were in place in Barbados and they had the accounting and the legal and the other professionals necessary to make sure that these things are run properly. So it was essentially acting upon advice that we were receiving from our advisors.

When asked whether the Canadian board of directors abdicated its authority to Mr. Lundberg to handle the transaction without consultation, Tole replied:

> Not at all. I mean I had the ultimate responsibility from the Canadian company's point of view to make sure this was properly implemented and I was quite comfortable in having Mr. Lundberg work through some of them. I mean, after all, there were legal issues here, there were tax issues, there were accounting, and we had no one better equipped than Mr. Lundberg to take care of this part.

[107] Tole said that that was just the beginning of the investment activity that Barbadosco would undertake. He said that within the first several months of the initial investment in the three notes there was another acquisition that was being anticipated in Europe. This was a UK company called "Berk" conducting a chemical distribution business. There would be interest bearing notes, he said, that had a good rate of interest and would

make an “interesting investment for Barbados”. He stated that an additional capital contribution to Barbadosco would have to be made to fund the acquisition of those notes.

[108] Tole was referred to an agenda for a November 21, 1994 meeting which outlined the number of potential transactions and planning ideas for a tax planning meeting. He said that none other than the Barbados proposal were implemented because:

> …there were none that had good, solid commercial reasons…

He also referred to a memorandum respecting “NEWCO Profitability Analysis”. He stated that Univar was embarking on an investment in an international financing company and wanted to analyze the amount of cash and the amount of borrowed funds that would be invested and whether the dividend income receivable would be an acceptable amount of return. He said that the company wanted to know if the dividend income would be a good return even if all of the money was borrowed.

[109] In response to Appellant’s counsel’s query as to how Univar paid for the shares of Barbadosco, meaning with what, Tole replied:

> The shares in Barbados were paid for with a combination of cash that was on hand immediately prior to that purchase, which was approximately $12 million, was in the bank account. And the balance would have been borrowed under the multi-currency credit facility.[16]

[110] With respect to how the $37,360,000 used to subscribe for Barbadosco shares was constituted, extended discussions took place in the attempt to analyze the true meaning of bank statements respecting that transaction. Tole’s evidence was that the cash balance in Univar’s account was approximately $11.9 million and that Univar borrowed the sum of $15 million on the multi-currency line of credit together with a second borrowing on that day under that line of credit of $37,360,000. Tole said that Univar had, therefore, borrowed $52 million in one day, that it paid $37,360,000 to acquire shares in Barbadosco and needed $26,958,863 on hand to pay significant trade accounts owing to suppliers. The following exchange

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[16] This was the $90 million U.S. multi-currency credit facility.

between Appellant's counsel and Tole describes the Appellant's position respecting payment:

> Q. So Mr. Tole, when the Canadian company made a share subscription and sent the money to Barbados for its shares in the Barbados company, how much cash was on hand in the Canadian bank account?
>
> A. Approximately $11,970.

Tole then testified that as at December 31, 1997 there were no outstanding amounts under the multi-currency line of credit, the debt having been retired with company earnings. In fact, Tole said that the borrowings in June 1995 began to be reduced almost immediately and were repaid in full in early 1997.

[111] Tole's final words respecting the make-up of the monies paid to acquire shares of Barbadosco are:

> …there was $12 million in the bank account and … there were in fact two draws under the credit facility on that date, which we saw, totalling just over $52 million. So there were a number of things that were happening at the same time – cash plus the borrowings, less payments to various agricultural suppliers, less the investment. It was all - - all of the cash and the borrowings were pooled in one bank account and all the transactions were taking place through there.

[112] After discussion about Barbadosco acquiring the Berk acquisition notes Tole testified that no such acquisition was made because "our world changed in June of 1996" when it was announced on that day that Royal Pakhoed would be acquiring all of the outstanding shares of UC. He said that at that time UC was de-listed from the New York Stock Exchange and that Royal Pakhoed had its own international financing company and was no longer interested in using Barbadosco to provide financing. Tole then stated that over the next couple of years Univar made dividend payments in excess of $100 million to UC.

[113] Tole then said that Barbadosco was wound-up on January 3, 2000. He gave as reasons that Royal Pakhoed wanted to hold all of the European

assets within Europe under the European structure, there being no longer a need for an international financing company such as Barbadosco.

[114] Appellant's counsel referred Tole to a document faxed from Pricewaterhouse Coopers dealing with the windup of Barbadosco. It stated in part,

> This delay exposes VWRL to the provisions of section 17 for a period of two days.

Tole said he did not understand what that was referring to but that the changes in legislation, in his understanding, would have resulted in some additional income tax being payable in Canada. Tole said that there were no further investment opportunities being considered for Barbadosco and that it would have been wound-up in any event.

[115] On cross-examination, Respondent's counsel posed questions respecting the retained earnings of Univar having been increased from $54 odd million to $57 odd million in 1992 to $61 odd million in 1993, to $67 odd million in 1994, to $79 odd million in 1995 and $93 odd million in 1996. Counsel then said the retained earnings were only about $6.6 million at December 31, 1996 and sought reason for same. Tole replied that on change of control the balance is transferred to "contributed surplus", it being "accounting gymnastics". Tole said that further decreases in retained earnings were due to the dividend paying requirements imposed by Royal Pakhoed.

[116] Counsel then referred to Univar's return on capital as a result of earnings.

[117] In discussing the conversion of the European debt to interest-bearing from non-interest bearing note Respondent's counsel said:

> The objective was that the interest that these European companies generated was not to be taxable in Canada?

Tole replied that there was never any contemplation that interest would be payable to Canada, that it was making an investment in Barbados and

would be receiving dividend income. He then said:

> So I don't - - wouldn't characterize it as you suggest.

[118] Counsel then asked whether it was the objective that the Appellant be able to deduct interest on the money borrowed in Canada for funding Barbadosco. Tole responded that it was one of the considerations. He said that, as would be the case with any investment, one concern was the extent that borrowing was necessary and that interest be deductible for tax purposes. Tole also said that Univar was a party to the fixing of interest to be paid on the European debt.

[119] Respondent's counsel then entered into the following exchange:

> Q. Now, we know that the Appellant borrowed $37,360,000 roughly for this injection into Barbados, capital injections?
>
> A. No, I don't know where we saw that. On the date of the investment we started with just under $12 million in cash, and during the course of that day borrowed a little over $52 million under the credit facility and utilized the cash plus the $52 million in borrowings to make payments to our suppliers and from that pool of cash to make the initial investment in Barbados.

[120] Counsel then pursued, with much repetition, a line of questioning concerning alternative investment use of "this $37 odd million". This was terminated upon objection by Appellant's counsel, the question already having been answered. Respondent's counsel then asked questions respecting whether Tole had been advised that the re-structuring would not affect Univar's ability to deduct interest payable on its borrowings, and that the interest received by NEWCO would not constitute foreign accrual property income. Tole then referred to prudent advice obtained to the effect that since the income was being earned and taxed in Barbados it would not also be taxable in Canada. Tole said that the dividends received by Barbadosco would be paid out of earnings already taxed in Barbados and it was therefore important that they not be taxed again when they were distributed to Canada.

[121] Respondent's counsel then asked Tole whether the concept of transferring U.S. debt from the United States to Canada was discussed at the

time of a UC Finance Committee meeting in June, 1994. Tole answered the question affirmatively saying that:

> …the whole leverage issue that we've talked about where the parent company was looking to end up with more debt in Canada and less debt in the U.S. Yes, I was familiar with that.

Respondent's counsel asked if that was because the tax rate in Canada was higher than in the U.S. and Tole replied that that would have been one of the reasons from the tax director's point of view.

[122] Counsel then asked Tole whether he was familiar with the concept of active business income and passive investment income, "frequently referred to as FAPI". Tole answered that his concern once again was that the income not be taxed twice and said that as to the underlying details, that was for the "tax advisors to help us deal with". When asked about whether he was apprised of what was to happen in the United Kingdom and Sweden regarding the level of debt, Tole replied that he was only aware of the fact that some re-structuring was taking place that would result in interest bearing notes being available for purchase by Barbados. Tole also told Respondent's counsel that no consideration was ever given to the Appellant acquiring the debt from UE.

[123] Respondent's counsel then sought, through more questions, to characterize the acquisition as being one which would have resulted in interest income taxable in Canada had it been received by Univar. He even went on to ask Tole whether he agreed that there would have been tax payable in Canada by Univar at the 45 percent rate. This hypothetical question was met with the consistent response that the acquisition by Univar of the debt was never a consideration.

[124] Respondent's counsel then discussed with Tole the matter of the Revenue Canada reassessment which had been settled at 15 percent. This led to the reference to Univar being removed as a guarantor and the suggestion by Respondent's counsel that the dispute with Revenue Canada was thereby resolved. Tole said that Lundberg still considered that there was a significant exposure in the U.S. even under circumstances where Univar was either a guarantor or jointly and severally liable under credit agreements of the parent company – that there was a risk of deemed dividend issues in the U.S.

[125] Respondent’s counsel, in repeated plodding fashion, asked whether the deductibility of the interest expense to the Appellant was a “crucial part of the scheme”. Tole simply responded that it was an important consideration for any borrower to ensure that interest would be deductible for tax purposes.

[126] Continuing, Respondent’s counsel asked why Tole might have thought the arrangement would not be acceptable to Revenue Canada. Counsel asked Tole whether Subpart F of the U.S. Revenue Code was a counterpart to Canadian FAPI rules. Tole replied that it was entirely a U.S. income tax issue. Counsel then pursued a series of questions having to do with the different currencies involved in the Barbados transaction during which he was advised by the Court that that was irrelevant, the reassessment having been made in Canadian dollars.

[127] Respondent’s counsel then sought to characterize the transaction as creating a benefit to Univar because it had higher debt, the benefit arising because of interest deduction in Canada. Tole responded that that was a minor benefit and that there were a number of benefits involved in the transaction, treasury, the utilization of cash generated in Canada and the whole areas of taxation.

[128] Respondent’s counsel even asked why Univar’s share subscription for shares of Barbadosco was in U.S. dollars.

[129] At one time the following exchange took place:

> Justice:So, why are you doing it again? If you want to use the information from these, they are already in evidence, which is what Mr. Kroft’s point is. You referred to them in your submissions.
>
> Mr. Chambers: Alright. I just have some questions, sir.
>
> Justice: I know, you keep saying that. You will not listen to me. Now, why do you want to keep on asking questions when the information is there and it’s in evidence? Are you challenging the credibility of this witness who’s already answered questions about these matters?

Mr. Chambers: No, I'm not.

[130] Respondent's counsel then asked whether the Appellant considered using the $37,600,000 in its business, which was very successful, and earn it 30 percent or 20 percent rather than just 8 or 7 or even less. Mr. Tole stated that there was excess cash available and more was going to be generated. He said that more cash was being generated than was necessary to invest in the chemical distribution business and that Univar was doing everything available in that regard. He said that they were investing excess cash in term deposits which were not generating a very high return. He then said, referring to Barbadosco, that it generated a higher rate of return and assisted the corporation in achieving a number of other objectives. Then Respondent's counsel pursued a line of questioning as to why the notes were not brought into Canada. This was followed by the suggestion that the winding-up of Barbadosco was because of changes to the *Income Tax Act* which would have been disadvantageous to Univar. Tole said that the parent company, Royal Pakhoed, was not interested in this structure.

[131] Respondent's counsel continued, after many other attempts, to characterize the share subscription of Barbadosco by Univar as being entirely with borrowed funds. His cross-examination ended with the following exchange:

> Justice:You keep - - Mr. Chambers, you will not abandon your line of questioning to, with your very own words, characterize the sum of money that went to purchase the notes. You have never ever, ever, ever, done anything but characterize that in your questions as borrowed money. And I'm not going to listen to any of that evidence when the question is answered that's posed in that fashion. It's irrelevant to me. I mean, establishing that that money was borrowed is not going to happen through a question that is phrased in that fashion, not at all. If there is evidence around to indicate that result, that's a different matter because I like to look at the evidence as it exists. But characterizing a transaction by the form of a question is not in my book.
>
> Q: You will acknowledge, Mr. Tole, that the bulk of the $37,600,000 that was injected into Barbados was borrowed money?

> A: I would, there was just under $12 million cash in the bank, so the bulk would have to be borrowed, I would agree.

Respondent's counsel asked no questions with respect to this response.

[132] The re-examination of Tole presented Tole's statement that the simple borrowing of money does not generate tax benefits. It has the ability to deduct interest but it still costs the company money and there has to be a purpose for borrowing. Appellant's counsel referred to a UC inter-office memo dated January 11, 1995 to David E. Olsen from Lundberg, the subject being the removal of Univar from revolving credit agreements. He reminded Tole of the reference by Respondent's counsel to the guarantee by the Canadian company of some of the facilities extended to UC by its lenders. He then asked if there was any discussion in that memorandum of Canadian tax consequences. Tole replied that there were none, that it was strictly a treasury issue and that the only tax issues mentioned in that memo were U.S. taxes.

[133] Appellant's counsel then summarized Tole's evidence respecting three different credit facilities. One was effective in 1991-1992 in which Univar was not a borrower but only a guarantor. In 1992 a new facility available to the U.S. under which Canada was a joint and several borrower was established. Thirdly, in June 1995 the non-U.S. subsidiaries became borrowers on a sole basis, not joint and several, under the multi-currency line of credit.

Signed at Ottawa, Canada, this 3rd day of November 2005.

"R.D. Bell"

Bell, J.

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