Docket: 2015-2998(IT)G

BETWEEN:

LOBLAW FINANCIAL HOLDINGS INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeals heard on April 23 to May 15, 2018, and July 17 and 18, 2018 at Toronto, Ontario

By: The Honourable Justice Campbell J. Miller

Appearances:

Counsel for the Appellant:	Mary Paterson, Mark Sheeley, Pooja Mihailovich, Al Meghji, Lipi Mishra
Counsel for the Respondent:	Elizabeth Chasson, Isida Ranxi, Aleksandrs Zemdegs, Gary Edwards, Laurent Bartleman, Cherylyn Dickson

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JUDGMENT

WHEREAS I have decided the following:

1. the large corporation rules in subsections 165(1.11) and 169(2.1) of the *Income Tax Act* of Canada (the "*Act*") are not applicable to preclude the Appellant from making certain arguments.

2. Glenhuron Bank Limited ("GBL") was a regulated foreign bank with the equivalent of greater than five full time employees in 2001 to 2005, 2008 and 2010 but was principally conducting business with non-arm's length persons and

consequently its income was from an investment business and is to be included in the Appellant's income as foreign accrual property income ("FAPI").

3. Pursuant to paragraph 95(2)(*b*) of the *Act*, GBL's fees from managing assets for non-arm's length persons is deemed to be income from a separate business other than an active business. The fees from Weston Acquisitions Inc., Weston Foods, Inc., Weston Foods US, Inc. and JFS Inc. are also FAPI as if not caught by paragraph 95(2)(*b*) of the *Act* they would otherwise be caught as part of GBL's investment business.

4. The calculation of the foreign exchange gains/losses in respect of GBL's investment in short term securities was on income account.

5. Although it is unnecessary to address the application of the general anti-avoidance rules ("GAAR") given the above decisions, I do so for completeness' sake:

i. The waivers for 2001 – 2005 taxation years preclude the Respondent from relying on GAAR in those years.

ii. For the 2008 and 2010 taxation years, GAAR is not applicable because, while there was a tax benefit (the avoidance of FAPI) and transactions that could reasonably be considered to result in a misuse of the FAPI provisions, the transactions were not avoidance transactions as they could reasonably be considered to be undertaken primarily for *bona fide* purposes other than to obtain the tax benefit.

NOW THEREFORE it is ordered and adjudged:

1. The Respondent's Motion pursuant to subsections 165(1.11) and 169(2.1) of the *Act* (the large corporation rules) is dismissed.

2. The Appeals for 2001 – 2005, 2008 and 2010 taxation years, are allowed and referred back to the Minister of National Revenue for reconsideration and reassessment on the limited basis that foreign exchange gains or losses arising on GBL's investment in short term securities shall be on income account.

3. The Parties shall advise within one week of receipt of this Judgment whether or not they wish to make written representations on costs, and if so, they shall do so within 60 days of the date of this decision, limiting their written representations

to a maximum of 15 pages. If they do not wish to make written representations, I make no award of costs.

Signed at Ottawa, Canada, this 7th day of September 2018.

"Campbell J. Miller"

C. Miller J.

Citation: 2018 TCC 182
Date: 20180907
Docket: 2015-2998(IT)G

BETWEEN:

LOBLAW FINANCIAL HOLDINGS INC.,

Appellant,

and

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REASONS FOR JUDGMENT

C. Miller J.

[1] It was suggested at the outset of this case by the Appellant's counsel, reaffirmed in closing argument, that, at its core, this was a general anti-avoidance rule ("GAAR") case. The Respondent appeared to take this opening salvo to heart as she proceeded to paint a picture of an organization intent on avoiding the foreign accrual property income ("FAPI") rules found in subsection 95(1) of the *Income Tax Act of Canada* (the "*Act*"). After a lengthy trial, with lengthy expert evidence on foreign banks, followed by lengthy written argument and two days of oral argument, I have concluded this case is not, at its core, a GAAR case. It is a FAPI case.

[2] The primary issue in this dispute is whether, during the 2001 to 2005 and 2008 and 2010 taxation years, the income of Glenhuron Bank Limited ("GBL") was FAPI and, therefore, taxable in its parent Loblaw Financial Holdings Inc.'s ("Loblaw Financial") hands. FAPI includes income from an investment business. The definition of "investment business" in the *Act* exempts a business, other than a business conducted principally with non-arm's length persons, of a regulated foreign bank with greater than five full-time employees or the equivalent thereof.

[3] In a nutshell, on the FAPI issue, Loblaw Financial's position is that the Government of Canada made a policy decision to exempt income from a regulated foreign bank (as that term had already been defined under the *Bank Act* of Canada) from being FAPI, and that GBL was a regulated foreign bank that met the added

conditions. The Respondent's position, put concisely, is that GBL was not a foreign bank and, even if it was, it did not meet the added requirements of greater than five full time employees and not conducting business principally with non-arm's length persons, as it was simply not in competition with anyone.

[4] If I find that GBL meets the requirements of a qualified regulated foreign bank, and consequently does not carry on an investment business, only then does the case morph into a GAAR case – from my reading of the evidence this is very much a secondary issue. The Respondent argues that Loblaw Financial is caught by the GAAR (section 245 of the *Act*), as it received a tax benefit (not having to pay tax on FAPI) arising from an avoidance transaction, (the incorporation of GBL, its name change, licensing etc.) constituting an abuse of the FAPI provisions in the *Act*. The Appellant counters there was no tax benefit (as no diversion of capital), no avoidance transaction (as how do you intend to avoid a law that is unknown at the time) and no misuse (as Government policy was to relieve these banks from FAPI).

[5] It may be disconcerting to readers of this decision, other than the Parties themselves, who presumably will understand, that a great deal will be written on the issues raised by them that ultimately has had little or no impact on my decision, given the narrow basis upon which I am hanging my hat. I do not apologize. The Parties deserve a comprehensive review of all the matters they deemed important. Who knows how it might assist down the road. There are many twists and turns in this case so I felt it useful to provide a roadmap outlining how I intend to render this decision.

I. FACTS

A. List of persons involved

B. Corporate structure and background prior to the years in issue (1992 – 2000)

C. What was the nature of GBL's activities in 2001 to 2010

(1) Receipt of funds

(2) Short-term debt securities and asset management

(3) Distributor or independent operator loans ("I/O Loans")

(4) Intercompany loans

(5) Equity forwards

(6) Cross-currency and interest swaps

(7) Reporting income from activities

D. How did GBL operate in 2001 to 2010

(1) Introduction/Office Structure

(2) Employees and responsibilities

(3) Board meetings

E. Central Bank of Barbados involvement

F. Waivers

G. Assessments and objection

H. Expert evidence

II. ISSUES

A. Is Loblaw Financial precluded from relying on certain arguments due to the application of the large corporation rule (subsections 165(1.11) and 169 (2.1) of the *Act*)

B. Was income earned by GBL in 2001-2005, 2008 and 2010 FAPI pursuant to subsection 95(1) of the *Act*

(1) Was GBL carrying on an investment business as defined in the preamble to the definition in subsection 95(1) of the *Act*?

(2) Was GBL exempted out of the definition?

(a) Was it a foreign bank?

(i) Pursuant to the definition in subsection 2(a) of the *Bank Act* of Canada?

(ii) Pursuant to the definition in subsection 2(c) of the *Bank Act* of Canada?

(b) Was it conducting business principally with persons with whom it did not deal at arm's length?

(c) Was it regulated under the laws of Barbados?

(d) Did it employ more than five full time employees or the equivalent thereof full time in the active conduct of the business?

C. <u>If Loblaw Financial received FAPI from GBL has it been correctly calculated?</u>

(1) Were the foreign exchange gains/losses arising on GBL's investments in short term securities on income or capital account?

(2) Does the inclusion in FAPI arising from the deemed separate business provision in paragraph 95(2)(*b*) of the *Act* include the fees received from Weston Acquisitions Inc., Weston Funds, Inc., Weston Foods US, Inc. and JFS Inc. (the "Disputed Entities")?

D. <u>If GBL was not carrying on an investment business is Loblaw Financial caught by the application of the GAAR?</u>

(1) Do the waivers for the taxation years 2001 to 2005 preclude the Respondent from relying on the GAAR for those years?

(2) Was there a tax benefit?

(3) Were there avoidance transactions?

(4) Was there an abuse of the FAPI provisions, specifically subsection 95(1) of the *Act*?

E. <u>If the GAAR applies how is Loblaw Financial to be taxed?</u>

III. REASONS (following order of issues as set out in Section II)

IV. CONCLUSION

I. FACTS

A. List of persons involved

[6] It is helpful to set out at the outset the cast of players, and there are many, both individual and corporate. Reference should be made to this list for noting the abbreviated names I have attached to many of the entities, as well as a brief description of their role. I therefore attach Appendix A breaking down the entities into the following categories:

a) Corporate entities

b) Corporation's with assets under management by GBL

Later in these Reasons, I will review investment management agreements that GBL had with several related parties. Suffice it to say at this introductory stage, that each of these related parties whose assets were managed by GBL, was:

i. Both a foreign affiliate and non-resident, directly or indirectly wholly-owned subsidiary of Weston Foods Inc., Weston Foods (Canada) Inc., George Weston Limited ("GWL"), Provigo Distribution Inc., Loblaw Inc. ("LINC"), and/or Loblaw Companies Limited ("LCL"); and

ii. A controlled foreign affiliate of the above companies other than Provigo Distribution Inc.

c) GBL directors and employees

d) Loblaw officers

e) Experts

f) Others

B. Corporate structure and background prior to years in issue (1992 – 2000)

[7] By way of brief overview, GBL was incorporated in Barbados on September 28, 1992, as Loblaw Inc., a wholly-owned subsidiary of Loblaw Financial. During the years assessed, Loblaw Financial was a direct wholly-owned subsidiary of LINC, a Canadian company (unfortunately with the same name as the Barbadian company), which in turn was a wholly-owned subsidiary of LCL, a public company traded on the Toronto Stock Exchange, the controlling shareholder of whom was GWL. GWL's shares also traded on the Toronto Stock Exchange. It owned the majority (60%) of shares of LCL. LCL concentrated on the grocery business.

[8] Loblaw Financial held several Canadian and foreign subsidiaries including GBL.

[9] Mr. Zoetmulder, a former director of GBL, provided evidence surrounding the incorporation of GBL. In 1992 he was also a director of GOBV, a Dutch subsidiary of Loblaw Financial. He described the business of GOBV as a passive business used to finance Loblaw's (when I use that term, I refer generally to the overall Loblaw Group: where it is critical to identify a specific entity within the group, I will do so) US operations by borrowing interest free from Canada and lending at interest in the United States. For example, in 1992 GOBV had interest free loans from Loblaw Financial (then called Loblaw International Holdings Inc. ("LIHI")) of approximately $133 million and lent the same amount to NHI at 9% or 10%. It held all of the preferred shares in NHI while Loblaw Financial held all the common shares. NHI owned National TEA Company which operated supermarkets in the United States. According to Mr. Zoetmulder, Loblaw was not the only major Canadian company to have a Dutch company serve as a holding company. He explained this was primarily due to the attractive withholding rates and treaty treatment.

[10] Mr. Mavrinac, as Vice-president of tax at Loblaw (which title applied to all the subsidiaries as well) attended GOBV's board meetings in late 1980s and early 1990s. He also described GOBV as the vehicle for financing Loblaw's US operations, acknowledging that the structure provided a tax advantage, one that was never questioned by Revenue Canada. He further indicated that the US operation was not a strong business in the early 1990s and it had been Loblaw's intention to sell since the late 1980's, not an easy task given the business was not doing well.

[11] In the early 1990s, the favourable regime for Canadian companies to establish Dutch holding companies was put in peril due to negotiation of the

Dutch-US Treaty and, to a lesser extent, the Canada-Dutch Treaty. Loblaw explored the possibility of establishing a Barbados corporation which, unlike the passive nature of GOBV, was intended to be an active operation. Mr. Mavrinac's memory of the organizational meeting of GBL was that the focus was on establishing a captive reinsurance company that would benefit the US operations by relieving the cost of workers' compensation issues then insured by third parties. According to Mr. Mavrinac, the financial vehicle (GBL) was not a well-developed idea, a twinkle in the eye, as he put it. He explained that GOBV simply lent money to the US operations, all done in accordance with the foreign affiliate rules at the time. He believed that the Barbados company could replace GOBV in that regard, but that the foreign affiliate rules required that the Barbados financial vehicle would have to be an active business, unlike GOBV. Mr. Mavrinac described the active business contemplated as that of a treasury centre involved in a finance type business. Though GBL was seen as a replacement to GOBV in a low tax jurisdiction, he believed that Barbados had people with the right skill set, was in the right time zone and that the Barbados tax regime was simpler than some of the alternatives. He put it this way:

> … what we were doing is we were positioning ourselves that, in the event that the rules changed and we no longer had the benefit of a reduced tax rate in our offshore structure, that we would be able to either replicate that structure or come up with a new structure that fit within the foreign affiliate regime at the time, that's what we were trying to do….
>
> … Because the FAPI rules were quite, I won't say they were simple, in their application, they were complex, but the principles were pretty simple. If you had an active business in the treaty country, right, you had the benefit of exempt surplus….

[12] Mr. Zoetmulder confirmed that Loblaw was considering establishing a Barbadian subsidiary in the insurance business which it in fact did under the name Glenmaple Reinsurance Company Limited ("GRCL"), as a subsidiary of GBL. The Director of Insurance for LCL, Glen Leroux, had suggested Barbados for the re-insurance business. GRCL was incorporated in January 1993 pursuant to the *Exempt Insurance Act* of Barbados licensed to conduct business as an exempt insurance company, not required to pay Barbadian tax on insurance income or capital gains.

[13] Mr. Zoetmulder confirmed that Loblaw was indeed turning to Barbados as it had a reliable legal system, proper tax system and appropriate infrastructure. Advice was sought from local legal counsel, Mr. David King. At the November 12,

1992 Directors' Operational meeting of GBL (then still Loblaw Inc.) Mr. King reported:

> … that the Company had been incorporated as an International Business Company on the 28th day of September, 1992 and was in the process of applying for a licence under the International Business Companies Act No. 24 of 1991. Such a licence would empower the Company to hold foreign currency accounts, transact international business and would also exempt it from the provisions of the Exchange Control Act.

[14] It was determined that the Barbadian companies would be capitalized to the extent of $20 million U.S., $15 million of which was intended for the GRCL's reinsurance business. The Appellant subscribed for 1000 common shares for $100,000. In February 1993, GOBV subscribed for non-voting preferred shares for $20 million U.S., for another $12 million U.S. worth in June and another $35 million U.S. worth in August. (unless otherwise noted dollars are U.S. dollars)

[15] Mr. Zoetmulder testified that Canadian tax played no role in these subscriptions. Mr. Mavrinac confirmed the initial $20 million was invested primarily for the insurance business and was not an avoidance of Canadian tax. In the organizational meeting of November 12, 1992, it was discussed in general terms that the new company would carry on the business of entering into financial transactions, including interest rate and foreign exchange swap transactions. Initially, GBL hired PricewaterhouseCoopers to manage these affairs until it hired its own staff.

[16] Mr. Welch, who was hired in 1993, and Mr. DiFilippo, later the president of GBL, both claimed that to the best of their knowledge there were no Canadian tax considerations during the incorporation of GBL or the subsequent obtaining of the licence under the *Offshore Banking Act* ("*OSBA*"). Mr. Mavrinac acknowledged that he was certainly aware at the time of the 2.5% Barbados tax rate, though he looked to Barbados counsel, Mr. King, for advice generally with respect to Barbados law.

[17] On October 15, 1993, Mr. King wrote to the Central Bank of Barbados ("CBB") seeking a meeting to discuss setting up an offshore bank, describing his client as a major Canadian food retailer that has in place an international business company and an exempt insurance company. On November 12, 1993, Mr. King again wrote to the CBB as follows:

> My client is now of the view that the financial activities which they propose to engage in ought properly to be conducted through the vehicle of a Barbados off-shore bank, rather than through the International Business Company (IBC) as was originally contemplated. Accordingly I submit to you on behalf of my client a proposal herein contained for the abovenamed Company Glenhuron Bank Limited to become licensed as a Barbados off-shore bank.

[18] At the GOBV board meeting on November 18, 1993, it was reported that "as yet, there is no follow-up on the Auditor General's report concerning the loopholes in Canadian tax law with respect to the international activities of Canadian multinationals." Mr. Mavrinac testified he was likely aware of the Auditor General's report (about which I will have more to say later in these Reasons) but claimed neither it nor the Standing Committee on Public Accounts report published in April 1993 impacted on the interaction with the Barbados subsidiary. He also testified that neither report played into the decision to obtain a licence under OBSA.

[19] On the same day, November 18, 1993, the directors of GBL (at that point still called Loblaw Inc.) also met and discussed GBL's status as an international business company, agreeing that "the nature of the company's actual business was more in keeping with that of a bank." Mr. Zoetmulder suggested this related to the financial swapping business and dealing with other multinational banks on the counterparty side. The directors also agreed the company's name would be changed "as required under Barbados banking legislation." Again, Mr. Zoetmulder testified that Canadian tax was not a factor in this decision.

[20] The shareholders of GBL also held a three minute meeting on November 18, 1993, in the presence of Mr. Thompson (a GOBV director and executive vice-president of Loblaw), Mr. Reid (CFO Loblaw), Mr. Mavrinac (VP tax Loblaw, representing LIHI), and Jurriaan Zoetmulder, Mr. Durtsche and Mr. Mann, representing GOBV, with Neil Walker and David King, who initiated the request for a license, according to Mr. Mavrinac, also present. It was resolved that the company obtain an *OSBA* licence and amend its articles to change its name to Glenhuron Bank.

[21] Mr. Walker reported to the GBL board in May 1994 that the company had changed it status from that of an international business company to that of an offshore bank and added the company obtained its licence from the Central Bank of Barbados on December 22, 1993, under *OSBA*.

[22] In applying for that *OSBA* licence in late 1993, GBL described its business as follows:

> The bank will focus primarily on investment banking together with selected commercial banking activities involving third party financial institutions of superior credit rating. No retail or deposit taking banking activities are currently planned.
>
> Investment banking activities will initially be in the area of secondary investments where the bank, as principal, will concentrate on holding or trading derivative products such as interest rate swaps, cross currency swaps and options. The bank will undertake all derivative transactions as a stand alone credit based on the strength of its own capitalization, all of which will be in-house. Other investment banking transactions such as equity and debt instrument trading and investment, merger and acquisitions activity and advisory services may be considered in future.
>
> Commercial banking activities will be initially limited to secured mortgage lending, initially in North America. Expanded commercial activities such as leasing and commercial leans may be considered in the future.

[23] On December 20, 1993, Mr. King again writes to the CBB indicating "we require the licence dated prior to December 31, 1993".

[24] On May 5, 1994, Mr. King wrote to the CBB as follows:

> You will be aware that proposed changes to Canada's Income Tax Act will require subsidiaries of Canadian companies doing investment business in Barbados to increase employment to more than five (5) persons in order to retain certain tax exemptions under the Canadian Income Tax Act. Partly to justify this increase in staff, the Bank intends to expand its present business to include processing such items as payroll, credit card applications and investment data for companies with which the Bank is related through its Canadian parent company.

[25] With the introduction of the *International Financial Services Act* in 2002 ("*IFSA*") the licence under the *OSBA* simply transferred from one Act to the other. According to Mr. Berry, President of GBL at the time, it remained business as usual.

[26] In February 1994, the Canadian government released its 1994 budget which introduced the "investment business" definition and included an exception to the FAPI inclusion for regulated financial institutions. In a GOBV board meeting of May 26, 1994, it was reported:

> This budget introduced major amendments to the foreign affiliate provisions of the Canadian *Income Tax Act*, in response to the report of the Auditor General to the House of Commons in 1992 and the report of the House of Commons Standing Committee on Public Accounts delivered in June 1993. Based on the budget proposals as they stand today, it would appear that the proposed Loblaw's franchisees interest swap program would have to be cancelled as being no longer feasible. ...it would appear that budget proposals, as they stand today, would not affect the finance operations of GBL or the claim handling of GRCL.

[27] The Auditor General Report referred to was released in November 1992 and it examined interest deductibility, taxable dividends from foreign affiliates and other related problems including FAPI. The report of the Standing Committee on Public Accounts released in April 1993, recommended that the Department of Finance immediately clarify what constitutes active business income in the context of the rules on FAPI.

[28] In February 1994, revisions to the FAPI were proposed by the Department of Finance: such revisions included the financial institution exemption. Draft legislation with such proposals was introduced in June 1994, followed by some amendments in January 1995 and the final enactment in June 1995.

[29] The February revisions also included a minimum employee requirement for the regulated financial institution exemption. Mr. Zoetmulder testified he was not aware this had been proposed and stated that employee requirements were dictated by what the business needed, not any legal provision. Three employees were hired in April and May, 1994: Wendel Mason, Donna Rogers and Antoinette Patel.

[30] Mr. Berry joined GBL on January 1, 1997, as Vice-President and Chief Investment Officer ("CIO"), bringing with him considerable financial experience primarily in the fixed income markets. His mandate was to create an investment department, bringing in-house the portfolio then being managed by Wilmington Trust Company. He became President of GBL in February 2002 and remained with GBL until its liquidation in 2013. His view on joining GBL was that it wanted to secure funds and grow them within the parameters of reasonable return and low risk.

[31] While I will go into greater detail later as to GBL's activities during the years in issue, Mr. Berry provided a good summary of those activities by referring me to the chart attached as Appendix B. The top level (Intercompany Loans, USD Short–Term Debt Securities and Distributor (I/O) Loans) represents a deployment from a treasury perspective of GBL's assets, investing in the USD Short-Term

Debt Securities, the US loans to several thousand independent driver operators distributing Weston Baked Goods in the US and intercorporate loans. This all produced US dollar revenue. Mr. Berry indicated that better returns could be had by using swaps to change the nature of the floating rate US dollar income into fixed rate Canadian dollar income. This involved using the money from the investments to enter cross-currency swaps which would yield Canadian income, and then use interest rate swaps to exchange Canadian floating rate payments for Canadian fixed rate payments. It was the swap activity that yielded greater income. The profits from the activities at the top level were intended to cover the swap activity at the bottom level. Mr. Berry also described two other pieces of GBL's business being managing other entities' assets for a fee and equity forwards.

[32] With respect to the short-term US deposits, some were held as security for counterparties in the swaps and some were unencumbered. This overall strategy was guided by statements of investment policy and guidelines ("SIPG") which limited investments to US treasury bills, issues from supranational agencies (for example, World Bank), US government guarantees or implied guarantees with government sponsored entities (for example, Federal Home Loan Bank) and A1 Corporate Securities, limited to under 183 days, or, with US treasury bonds, under two years. It appears the average term was not greater than 120 days. This would keep the portfolio fairly liquid in the event projects came along in which GBL would want to invest, for example, the I/O Loans.

[33] Briefly, a cross-currency swap is an agreement between two counterparties (GBL and a global bank with whom GBL had an international swap and derivatives association ("ISDA") agreement), in which GBL agreed to pay three month US Dollar LIBOR (London interbank offered rate) and the counterparty paid GBL a three month Canadian dollar B.A. (Banker's Acceptance) rate. These rates were calculated quarterly and paid semi-annually.

[34] Under the ISDA agreements, GBL was required to post security (initially cash deposits, later using securities as collateral), though the counter-parties were not required to do the same.

[35] Mr. Berry described the interest rate swaps as swapping the Canadian B.A. income for a fixed rate of return akin to investing in a long-term loan. In effect, the income from the short-term securities was used by GBL as much as possible to fund the cross-currency swaps. Mr. Berry testified that no one from Loblaw head office was involved in authorizing or approving the swaps though he did

acknowledge that GBL was subject to certain provisions of the Loblaw companies' derivative policy.

[36] Mr. Berry drafted the SIPGs, being operating manuals for the investment managers, initially being just himself, to lay out boundaries as to how the money could be invested, including the kind of securities, the minimum credit ratings and the maximum maturity length. One element of the policy was to minimize or eliminate payment of withholding tax. There was also a constraint in some of the SIPGs entered prior to 2000, that read:

> Constraints implicit in the FAPI rules pertaining to the *Income Tax Act* of Canada which may prescribe investments and obligations, direct or otherwise, of Canadian persons.

[37] Mr. Berry attempted to explain this constraint as follows:

> Well, to be honest with you, I didn't actually know really what FAPI was back in those days, and I certainly wouldn't count myself as an expert today. And I am not sure what I was trying to do here in terms of FAPI, because FAPI didn't have any direct bearing on the bank. We weren't investing in Canadian securities anyway. We weren't permitted to. …I am not sure where this came from or why it was stuck in. But, in any event, I submit humbly, Your Honour, that was probably put there to sound good or to try and sound intelligent and impress people.

[38] As will be seen when discussing the business activity during the years in question in more detail, GBL managed its own money in a very similar manner to how GBL managed others' assets in accordance with the SIPGs.

[39] Where did GBL get its funds in the early years? There were subscriptions from GOBV for preferred shares in 1993 totalling $67 million. In 1994, GOBV subscribed for additional preferred shares throughout the year totalling close to $48 million. In 1995, GOBV subscribed for another $10 million worth of preferred shares. In 1997, GBL redeemed $94 million worth of the preferred shares, while in the same year a further $111 million worth of preferred shares were issued. Also, in 1997, GBL received $133 million in cash for an assignment of promissory notes from GOBV, representing interest-free loans from Canada. Mr. Holland explained this was to take the cash that was in GOBV and contribute it to GBL. He also explained it was unlikely the funds would have been repaid to Canada as it would have triggered a foreign exchange gain and that money was simply not needed in Canada.

[40] In 1998, GBL realized over $8 million of gain on its disposition of GRCL. Loblaw Financial subscribed for 420,000 common shares in 1998 for $42 million, in answer to a concern from the Central Bank of Barbados regarding GBL's capital adequacy issue.

[41] In 2000 there was a significant injection (approximately $292 million) of capital from Loblaw Financial as part of the wrapping-up of the US operations run through National TEA, which requires further explanation.

[42] Loblaw Financial held all the common shares of NHI, while GOBV held the preferred shares. NHI was the parent of National TEA which operated the grocery business in the US, the business which was struggling in the late 1980's and early 1990's, as indicated earlier. Indeed, a purchaser was ultimately found and an agreement to sell substantially all of the assets of National TEA was finalized in 1995, resulting in a cash receipt by National TEA of approximately $440 million. It was determined at a GOBV board meeting in late 1994 that rather than invest the money in GBL preferred shares or repay the funds by way of repayment of capital to Loblaw Financial (at that point still LIHI), the funds would be held in NHI "in anticipation of alternative US investment opportunities." In January 1995, NHI repaid $111 million that it owed to GOBV. Wilmington was hired to manage the proceeds to invest on a short-term basis. The resulting income was FAPI. Also in 1995, NHI contributed $207 million to Glendel, its wholly-owned subsidiary, which invested on a short-term basis, also triggering FAPI. Glendel was also subject to US tax. Mr. Holland indicated Glendel's Canadian tax was only 10% of the US tax.

[43] In June 2000, Glendel was dissolved into NHI and a few days later, GBL issued 291,786 common shares to Loblaw Financial in exchange for all the issued and outstanding shares of NHI, which was subsequently dissolved, resulting in GBL receiving approximately $291 million cash. Mr. Holland, who structured the transaction, admitted Canadian tax was a factor in undertaking the transaction but denied that FAPI was the primary driver, rather "the primary driver was … to put cash that was in the US into GBL for use in its business." He also indicated that structuring in this manner avoided US withholding tax on liquidating into GBL. Loblaw had sought an advance ruling regarding these transactions, receiving a letter dated December 31, 1999 from the Canada Revenue Agency (the "CRA") permitting the rollover treatment sought and confirming that GAAR was not applicable, though also stipulating that nothing in the letter "should be construed as implying Revenue Canada has reviewed, accepted or otherwise agreed to the nature of any business."

[44] Also in 2000, Loblaw Financial converted its 142,099 preferred shares in GBL, which previously it acquired on the wind up of GOBV in early 1999, into common shares. In effect, the preferred shares were paid off by GBL and GBL received $142 million worth of NHI's assets. Together these amounts ($291 million and $142 million) equate closely to the $440 million sale proceeds of the National TEA sale.

[45] To round out the picture of revenues received in the years prior to the years in issue, GBL was making money through its short-term investments and through its swap program. In 1993, just before being licensed under *OSBA*, GBL was investing in short term debt securities and entering both the cross currency swaps and interest rate swaps. In 1994, for example, revenues from interest swaps was $18 million compared to $1.5 million in 1993 and revenues from cross-currency swaps went from a few hundred thousand dollars in 1993 to over $13 million in 1994, with corresponding increases in associated expenses. Mr. Welch described this increase in the early years as requiring much more work.

[46] By 2001, GBL was earning about $49 million on interest swaps, $24 million on cross-currency swaps and $31 million on short-term investments and security deposits.

C. <u>What was the nature of GBL's activities in 2001 to 2010</u>

(1) Receipt of funds

[47] For the years in issue, GBL grew its asset base primarily through an increase in its retained earnings which went from approximately $100 million at the end of the 2000 taxation to approximately $700 million at the end of the 2010 taxation year. The share capital at the end of 2000 was $476 million and at the end of 2010 was $443 million, though there had been some capital distributions as well as injections to capital over that time period.

[48] As indicated on the chart on Appendix B, the business of GBL can be broken into a few components: short term debt securities, assets under management, intercorporate loans, I/O Loans, swaps and equity forwards. While there was considerable evidence in relation to each of these business activities, some of which I have already described for the 1992-2000 period, I intend to condense it to the essential elements for the years in issue.

(2) Short term debt securities and asset management

[49] The policy of obtaining US short term debt securities with short maturity dates continued from the 1990s into the years in issue. Only US securities were acquired, as Mr. Berry described the US market as the deepest, most liquid and most efficient. Also, GBL identified five types of debt securities in which it remained invested (see paragraph 32).

[50] GBL invested in short term debt securities on its own account and also had investment management agreements with companies whose assets it managed. The agreements stipulated how the investment manager may effect transactions, the standard of care imposed on the investment manager, when the agreement will commence and when it will terminate. The agreement contained three schedules: the SIPG, the fee schedule and the custodial option.

[51] As indicated earlier, Mr. Berry developed the SIPGs that specified the kind of securities that could be held, the minimum credit ratings, maximum maturity lengths and constraints. Every party with assets under management was related to GBL, except Waterman Insurance (see Appendix A for a list of these related companies). Mr. Holland testified that five of these companies, Weston Acquisitions Inc., Weston Foods Inc., Weston Foods US, Inc., JFS Inc. and GRCL, carried on active businesses and did not earn FAPI on assets managed by GBL.

[52] The fee schedule set out the fees. Waterman Insurance paid a fee of 30 to 36 basis points, while the related companies paid 17 basis points. Some related companies had their fee paid by another related company. The fees earned by GBL would be a few hundred thousand dollars a year in the early 2000s, peaking at approximately $1.7 million in 2009. Assets under management ranged from approximately $175 million in 2001 to $1.2 billion in 2008. This compares to GBL's portfolio growth of $708 million in 2000 to $977 million in 2010.

[53] The custodial option indicated the account's assets would be held at CitiBank unless another custodian was specified.

[54] There was a detailed process for the purchasing and settling of new short term debt securities, regardless of whether the securities were for GBL's own account or for the companies with assets under management. Sometimes GBL bought a security and split it amongst different entities' portfolios.

[55] With respect to the short term debt securities, the investment team would discuss their research and decide what to buy, ensuring it would comply with the SIPG. The investment analyst or manager would then contact brokers to determine

availability: normally there would be no negotiation as a broker (for example, Solomon or Merryl Lynch) would make it a take it or leave it offer. If the product sought was not available at the price sought, Mr. Berry indicated they might have to modify the plan. Once the security was bought, the broker would send a confirmation which would trigger GBL's investment team to write a "triplicate ticket." What followed was a three part settlement process before GBL paid for the security. This became the back office's responsibility. One employee input the transaction into GBL's CitiBank settlement platform, a second employee verified such input against the ticket and a third employee authorized the trade. Once GBL released the funds, the broker delivered the security to GBL's CitiBank custody account. The back office also then entered the purchase into GBL's accounting ledger and swap investment management system ("SIMS"). SIMS displayed each SIPG ensuring that only authorized short term debt securities were actually purchased.

(3) Distributor or independent operator loans – I/O Loans

[56] In 2001, GWL purchased Best Foods Baking Co. ("Best Foods") from Unilever, who, along with Bank of America and SunTrust held and financed the I/O Loans, being loans to distributors. The distributors were individual drivers who had purchased the rights to distribute Best Foods baked products along specified routes in the United States. GWL only wanted some of the I/O loans, allowing GBL to acquire approximately 1,875 I/O loans in 2001 for approximately $86 million. GBL expected a return of 8.5%, a greater return than it was making on its other assets.

[57] GBL acquired software which amortized the loans and calculated expected payments and also set up a 1-800 number so the distributors could get in touch.

[58] GBL hired two people, Francine Taylor and Michelle Medford to manage the loans, which required collecting payments, paying expenses, reviewing documents and treasury rates (as the loans were pegged to treasury rates) and completing the documents and invoices. The I/O loan portfolio was valued every 28 days for reporting to LCL.

[59] GBL also provided new financing, approximately 700 to 800 new loans a year, the average loan being about $40,000 to $50,000. GBL would not finance distributors with poor credit rating, as checked through Equifax.

[60] GBL received payments on the loans via George Weston Bakeries Inc., who deducted the amount owed to GBL from the distributors' paycheques and then made a monthly wire transfer to GBL. George Weston Bakeries Inc. also guaranteed the loan portfolio for a total value equal to 35% of the loans. GBL earned approximately $7 million to $8 million a year from the I/O loans.

[61] On March 31, 2005, GBL sold the I/O loan portfolio to Glendock Finance Company, a related Irish company for $106 million, as the US-Barbados tax withholding regime had changed, which made owning the loans less profitable. GBL returned $100 million to Loblaw Financial that year.

[62] GBL continued to manage the I/O loan portfolio as Glendock was not set up to do so.

[63] In 2009, Grupo Bimbo purchased the US bakery operations and the I/O loans from George Weston Bakeries Inc. and took over administering the portfolio. Shortly afterwards, Ms. Taylor and Ms. Medford were laid off.

(4) Intercompany loans

[64] GBL made two substantial short term intercompany loans in the relevant years. In 2002, it loaned $325 million to Weston Acquisition and was repaid 38 days later, earning $3 million in interest income. Over several days in February 2008, GBL loaned an aggregate of $300 million to LCL: $200 million was pursuant to its committed credit agreement and $100 million was pursuant to its uncommitted credit agreement. These agreements had been entered into in October 2007. Again, GBL was repaid in short order in March 2008 and earned $1.2 million in interest income.

(5) Equity forwards

[65] Equity forward contracts were a series of contracts that GBL entered with CitiBank where GBL paid CitiBank a three month B.A. rate plus a credit spread, and in return GBL received the rate of return on an underlying stock. That rate equaled the difference between stock market price on the day of entering the contract and terminating the contract, plus any dividends. The difference in market price was paid to GBL when the contract was terminated. The dividends were credited every three months against GBL's payment to CitiBank.

[66] GBL entered six equity forward contracts with LCL's shares constituting the underlying stock. The contracts were for 10 years. From March 2003 until March 2009, GBL's equity forward possession represented a notional amount of 4,793,600 shares of LCL.

[67] Manny DiFilippo was GBL's President when it entered into the first couple of equity forward contracts involving LCL shares. Previously, Mr. DiFilippo had worked for LCL and had helped implement its stock option program. He testified that it was his idea for GBL to enter into the LCL equity forward contracts and that GBL was not instructed to do so. He further testified that the LCL employee stock options may have been a consideration in entering these contracts, but that the equity forwards were not a hedge against LCL's employee stock options. Mr. Berry, however, testified that Mr. DiFilippo presented the equity forwards to GBL's board as a way to offset the cost of the LCL stock option program.

[68] Mr. Galen Weston testified that though he was Executive Chairman of LCL in 2006, he did not have first-hand knowledge of the GBL derivative policy nor GBL's equity forwards, as they were implemented before he began this role. He did confirm that LCL's annual report indicated that GBL's equity forwards "are used to manage exposure to fluctuations in the company's stock based compensation costs." He further clarified that he believed LCL's derivative policy applied to its operating business but not to GBL.

[69] Mr. Weston was also questioned about statements he made in May 2011 regarding GBL's equity forwards being implemented "as a way of managing the cost of LCL's stock options." He confirmed that this reflected his understanding at that time but reiterated that he had no first-hand knowledge of why the equity forwards were put in place. He also indicated that GBL's equity forwards were an ineffective way of managing the cost of the LCL stock option program.

[70] GBL calculated the accumulated dividends and stock price return every 28 days on the equity forward contracts and reported that to LCL. The share price of LCL's shares peaked in 2005 before declining. This was discussed at several of the GBL board meetings but it was not until March 2009 that GBL began to terminate the equity forward contracts. Some were terminated and others sold to Wittington Investments Limited, leading to a loss of some $30 million. Indeed, Mr. Welch reported to a board meeting of GBL on November 11, 2009, that on a cumulative basis the bank has recorded a $71 million Canadian unrealized loss and a $37 million Canadian realized loss on the equity forward position.

(6) Cross-currency and interest swaps

[71] I have already briefly described GBL's *modus operandi* with respect to swaps (see paragraphs 33-35), which continued throughout the years in issue. Interest rate swaps in particular were profitable in the 2000s as GBL received a much higher fixed rate than the floating rate. Also, the appreciation of the Canadian dollar in 2000s increased the profitability of the cross-currency swaps.

[72] Mr. Berry testified that although no one from LCL's head office was involved or had to authorize GBL's swaps, GBL was subject to certain provisions of the LCL's derivative policy.

[73] Once the investment team decided on a swap, they would contact two or three counterparties to determine a price. Then, after an agreement was reached, the accounting team would enter it into SIMS. Mr. Berry reviewed the outstanding swaps weekly, reviewing mark to market price as well as the credit rating for the counterparty. Every 28 days, the accounting team recorded and reported to LCL the accrued interest and cash received. Every three months, they also calculated for each swap the applicable US LIBOR and Canadian B.A. They reported annually on all outstanding swaps.

[74] An ISDA agreement and accompanying credit annex were mandatory before GBL entered a swap with a counterparty. The credit annex set out the deal between the parties, including the collateral security held by each party. GBL would provide some of its short term debt securities as collateral. Many of the GBL ISDA agreements would terminate if GBL was no longer directly or indirectly owned or affiliated with LCL.

[75] GBL netted approximately $125 million to $130 million over the years in issue from the cross-currency swaps and a similar amount from the interest rate swaps.

(7) Reporting of income from activities

[76] Mr. Holland went through several T1134 Controlled Foreign Affiliate Information Returns filed by Loblaw Financial for both GBL and GOBV. He confirmed the returns in connection with GBL reported its accounting net income before tax and that such income was not FAPI. The reasons checked for income not being FAPI was due to the regulated financial institutions exemption (95(1) of the *Act*) and also due to the application of paragraph 95(2)(l) of the *Act*. The

T1134s income reported is tracked to GBL's statements of earnings in the relevant tax years.

[77] Mr. Holland also confirmed that the T1134s filed by Loblaw Financial in connection with GOBV reported the interest and dividend income as FAPI.

[78] With respect to the lack of reporting of any FAPI arising from the fees from managing other entities' investments pursuant to paragraph 95(2)(*b*) of the *Act*, Mr. Holland testified that was an oversight. He indicated, however, that only applied to affiliates that did not carry on active business, which would not include GRCL, JFS Inc., Weston Foods, Inc., Weston Foods US Inc. and Weston Acquisition Inc. He indicated that other than Canadian-sourced income, GRCL's income was never assessed as FAPI. With respect to JFS Inc., he stated it was established in 2010 as the US retailer of Joe Fresh apparel. With respect to Weston Acquisition Inc. and its subsidiaries, he confirmed it carried on a baking business. With respect to Weston Foods, Inc., he indicated it and its subsidiaries carried on a fresh and frozen baked goods business. Finally, with respect to Weston Foods US Inc. and its subsidiaries, he testified they carried on a food processing businesses.

D. How Did GBL Operate – 2001 – 2010

(1) Introduction/Office structure

[79] An element of this case is the determination of the number of full-time employees of GBL during the years in question. I have attached as Appendix C copies of organization charts for some of the years in issue setting out the employees and their titles to give a flavour of the organization.

[80] These charts make clear there are basically two arms or departments: front office or investment department and back office or accounting department. Mr. Berry described a very clear separation between the two departments.

[81] GBL's physical premises in Barbados were shared with GRCL for most of the period in issue. Barbara Cummins was hired by GRCL when its operations were brought in-house in or around 2003. Ms. Cummins did the day to day work for GRCL, as well as for PVO Assurance, WFRG and Glenhuron Holdings (the latter two, starting in 2008), including preparing financial statements, which were reviewed by Mr. Welch. Ms. Cummins occasionally assisted GBL as one of the individuals responsible to verify trades, though she was never paid by GBL nor listed as an employee of GBL.

(2) Employees and responsibilities

[82] The following summarizes the employees' titles and terms of employment with GBL during the years in issue:

Name	Position	Term
Manny DiFilippo	Vice President/President	1998 – February/2002
Donna Rogers	Executive Assistant/Treasury Assistant	1994 – 2013
Wendel Mason	Investment Manager/Controller	1994 – 2013
Michael Berry	CIO/President	1997 – 2013
Carl Drayton	Accounting Officer/IO Loan Manager	1997- May 2005
Brenda Blackman	Accounting Treasury Clerk/Office Manager	1996 – after 2010
Julia Robinson	Accounting Manager	1999 – June 2005
Antoinette Patel	Treasury Manager	1994 – after 2010
Kirk Odle	Assistant Portfolio Manager	1999 – February 28, 2001
Trevor Welch	Vice President Finance and Administration	August 1, 2001 – after 2010
Francine Taylor	Loans Administration	February 1, 2002 – October 2009
Michelle Medford	Loans Accountant/IT Supervisor	January 1, 2002 – March 2010
Beverly Holder	Reception/General Administration	Temporary – November 27, 2001; permanent February 1, 2002 – 2013
Amanda McKenzie	Investment Manager	March 1, 2003 – 2007
Shane Whittaker	Financial Analyst/IT	September 1, 2005 – 2013
Jason Bayley	Investment Analyst	2007 – 2012

I will address each employee in greater detail.

Manny DiFilippo

[83] Mr. DiFilippo, a chartered accountant, joined LCL in 1992 in internal audit and in 1995 became the Vice President, Corporate Development for LCL and GWL. He was asked by Don Reid to join GBL in mid-1998 due to concerns with respect to timeliness, completeness and accuracy of GBL's financial information. Before the end of the year, Mr. DiFilippo replaced Mr. Walker as President of GBL, where he remained until December 31, 2001.

[84] Mr. DiFilippo described his job as full-time (eight to nine hours per day, 5 days a week throughout the year). He described three responsibilities:

1) Running the office, ensuring policies and procedures were followed.

2) Operations; contact with the CBB and overseeing the investment desk including entering the forward equity contracts.

3) Financial reporting and communicating with LCL on an as needed basis.

[85] Mr. DiFilippo, as President, reported to GBL's board. He was President when GBL acquired NHI and also when GBL acquired the I/O loan portfolio.

[86] Although Mr. DiFilippo testified that he had not worked for any other related entity, he did acknowledge that he was President and a director of GRCL while in Barbados. He testified his responsibility was limited to preparing for the quarterly board meetings. He was not paid by GRCL. He was also an officer and director of PVO Assurance.

Michael Berry

[87] Mr. Berry succeeded Mr. DiFilippo as President of GBL in early 2002, having acted as Chief Investment Officer to that point since joining GBL in 1997. As President, Mr. Berry reported to the GBL board, but also reported to an LCL "line officer," initially Mr. Mavrinac, then Ms. Lacchin and finally Mr. Holland. He testified it was only with Mr. Holland that he had regular contact of two to three times a week.

[88] Mr. Berry, for the years in issue, headed up the investment team (treasury manager, investment analysts and himself), with whom he met each morning to discuss securities research, what to buy and to review third party assets under

management. Quarterly reports were prepared for each entity with assets under management, which Mr. Berry helped write and edit.

[89] Mr. Berry worked with Ms. Patel on the swaps, determining what to buy and what counterparties to contact. He reviewed the swaps weekly. As President, he also had the head of the back office, Mr. Welch, report to him.

[90] As well as President of GBL, Mr. Berry was President of GGMI until it dissolved in 2003. GGMI was set up to attract third party clients but only obtained the one client, Waterman Insurance Inc. Mr. Berry was also President of GRCL as of January 1, 2002, spending less than a day per quarter in this supervisory role. Later he became President of PVO Assurance, WFRG Investment and Glenhuron Holdings, claiming he spent very little time in these companies, as his only responsibility was running annual board meetings. None of these companies paid Mr. Berry any employment income, though GBL paid him a bonus of 20% of net profit from work for Waterman, as it was attracted by GGMI, which Mr. Berry described simply as a marketing tool. WFRG paid Mr. Berry a few thousand dollar director's fee. Mr. Berry was a director of these related companies.

[91] Finally, Mr. Berry testified that he created a set of rules, "existing customs," he called it, establishing standard working hours for all employees, being 8:00 a.m. to 4:00 p.m. with some flex hours allowed. Overtime was necessary, especially in the accounting department due to the mandatory reporting requirements (28 day financial cycle to report to LCL).

Wendel Mason

[92] Mr. Mason switched from back office (accounting department) to front office (investment department) in 2002 and then back to the back office in June 2005. He described his work on the investment side as requiring full eight hour days, while as Controller, on the accounting side, he would put in more hours due to the requirements of monthly and quarterly reports.

[93] On the investment side, Mr. Mason would review portfolios daily, meeting with the investment team to determine what would be maturing and planning what to purchase. He suggested his objective with respect to the short term debt securities was "to make as much money as possible for Mr. Weston." He would check with Ms. Patel to see if more securities were needed in the collateral accounts. He reported to Mr. Berry.

[94] As Controller, Mr. Mason was the person primarily responsible for financial statements, consequently having to ensure the accurate recording in GBL's ledgers. He was also responsible for settling swaps and verifying trade tickets. In addition, he prepared the CCB quarterly reports. He reported to Trevor Welch.

Trevor Welch

[95] Mr. Welch, a CGA, worked for GBL in the 1990s but left for a brief period of time, returning in August 2001 to serve as Vice President Finance and Administration. He served as a director of GGMI in 2003. He was also a commissioner of the Barbados Fair Trading Commission from 2005 to 2012 and a Director of Glenhuron Holdings beginning in 2008. He helped prepare the latter's financial statements as well as for GRCL and PVO.

[96] When Mr. Welch rejoined GBL in 2001, there were "lots of things going on" as he put it. The I/O loan portfolio had just been acquired. The swaps were taking off and short term securities were maturing.

[97] Mr. Welch had overall responsibility for compliance, including overseeing internal controls, internal and external audits, statutory reporting, anti-laundering aspects of GBL, as well as having responsibility for human resources. He handled the reporting requirements, including the cyclical 28 day reports LCL, the basic financial reports to companies with assets under management and reviewing statutory filings with the CBB.

[98] Mr. Welch met quarterly by phone with the LCL finance group for 15 to 20 minutes. He acknowledged having interaction with the LCL IT group as they were on the same platform, but testified he had no interaction with the LCL International Tax Group. He would report to the board on GBL's financial results.

[99] Mr. Welch explained that his department, the accounting department, had responsibility for updating SIMS and also ensuring that, based on SIPGs, traders could not buy anything not approved by the board. It was Mr. Welch who prepared a schedule or roster for the three-step process for inputting information with respect to the trades, verifying them and finally authorizing them.

Donna Rogers

[100] Ms. Rogers was one of the early employees, acting as executive assistant to the president. She later also served as assistant to the treasury manager and back up

for swap transactions, sitting in on the morning front office meetings with the investment team. Part of her duties on the investment desk would be to receive confirmations from brokers that would be attached to the trade tickets prepared by an investment manager. She would also enter information into SIMS. She put together packages for the board meetings and annual general meetings for GBL and some related companies (eg. GRCL, PVO, WFRG) as well as maintaining their minute books. It was also her responsibility to maintain files, for any entity GBL had a relationship with, for example, those companies with assets under management.

Jason Bayley

[101] Mr. Bayley was hired by Mr. Berry in September 2007 as an investment analyst. He testified that he worked longer than standard hours, citing as an example in 2009 GBL diversified to two custodians, which created a large volume of securities to be moved over. He worked most closely with the investment team of Mr. Berry, Ms. Patel and Ms. Rogers, handling primarily the short term debt securities, including research (60% to 70% of his time) on investments and executing trades, approximately three a week. As well, he was responsible for doing the quarterly reporting for entities whose assets were managed by GBL.

[102] Mr. Bayley explained he was in constant contact with brokers to assist on deciding on the appropriate investment. He confirmed all investments had to be in compliance with the SIPGs.

[103] At the daily morning meetings of the investment team, Mr. Bayley would advise what was happening in the markets and give an update of where the investments stood. With respect to trades, Mr. Bayley confirmed a number of things. First, that there were no separate purchases for GBL's own account and those with assets under management: there would be a block trade and then it would be split on a pro rata basis amongst those that had cash or maturities on that day. Second, there would be a trade ticket for each trade for each company. Third, once there was confirmation from the broker and trade tickets issued, the accounting department inputted the trade, followed by a different person verifying it and then an employee who finally authorized it. He testified that he also did not understand the FAPI constraint in the SIPGs.

[104] Mr. Bayley was involved in preparing the quarterly reports for GBL and others such as GRCL, comparing their performance to certain benchmarks.

Carl Drayton

[105] Mr. Drayton was an accounting officer and network supervisor (IT) and in 2002 became the manager of the I/O Loans Group, which entailed inputting of the loans. One of his responsibilities was to verify that what got entered into the CitiBank's settlement system was correct against information from the broker. Mr. Drayton reported to Mr. Mason. He provided some IT support to GRCL.

Brenda Blackman

[106] Ms. Blackman started in the 1990s with GBL as a receptionist, but moved into the accounting department and later served as office manager looking after the general upkeep and ordering the supplies. Mr. DiFilippo described the amount of traffic coming through the office as minimal so the receptionist duties were minor. She was also on the schedule for the three-step process of inputting into the CitiBank system, verification and authorization of trades.

[107] Ms. Blackman also prepared financial statements for Glenhuron Holdings, which Mr. Welch described as a simple task given that it only held shares in a couple of companies.

Julia Robinson

[108] Ms. Robinson worked in the accounting department until June 30, 2005. One of her duties was, after a ticket was received from the investment department, to write up the voucher where cash will be debited and investments credited. She was also on the roster of the three-step settlement process, either inputting or verifying the input was correct. She assisted in the financial statement reports to LCL and also did trial balances for affiliated companies to whom GBL provided management services, for example PVO, WFRG and GRCL.

Antoinette Patel

[109] Ms. Patel was one of the early employees to have joined GBL commencing in 1994 as assistant treasurer, moving to treasury manager in 1998 in the investment department. She had primary responsibility for the swaps, meeting with Mr. Berry to develop a plan, contacting counterparties and then proceeding with the deal by making the bank transfers. Indeed, it was her job to monitor balances in bank accounts. On the banking side she assisted with wire transfers and routine

banking matters for WFRG though such were limited to just four incoming and four outgoing payments in a year.

[110] Ms. Patel would prepare information about the swaps for presentation at board meetings. She was also cross-trained to do purchase and sale of short term debt securities. She was a director of GGMI in 2003.

Kirk Odle

[111] Mr. Odle was with GBL briefly as assistant portfolio manager until February 28, 2001, mainly assisting Mr. Berry, who evidently did not find him of much assistance. Mr. Mason was moved from accounting department to investment department to replace Mr. Odle.

Francine Taylor

[112] Ms. Taylor was hired as an I/O Loans Administrator on February 1, 2002, and left GBL in October of 2009 when it ceased any involvement with the I/O loan portfolio. She would review the loan documents, verifying them against a checklist, before passing them on to Ms. Medford or Mr. Drayton. She was on the schedule for CitiDirect that was the system of settling short term debt securities into CitiBank's settlement platform.

Michelle Medford

[113] Ms. Medford was hired in January 2002 as the I/O Loan Accountant, and also later assumed some IT responsibilities as backup network administrator. She too was on the roster for CitiBank (the investment settlements) set by Mr. Welch for the inputting, verifying and authorizing of trades.

Beverly Holder

[114] Ms. Holder started in a temporary position in November 2001, moving to full-time on February 1, 2002. She held various positions, including reception, filing and general administrative duties. With respect to reception, the physical office for GBL was in the same office as GRCL, GGMI (until 2003), PVO Assurance and later WFRG and Glenhuron Holdings, who all rented from GBL. Anyone visiting the latter companies would pass through the GBL reception, though the other companies had their own phone lines.

Amanda McKenzie

[115] Ms. McKenzie worked in the investment department of GBL from March 1, 2003 to sometime in 2007. She replaced Mr. Mason when he returned to the accounting department. She backed up Ms. Patel on the swaps when Ms. Patel was away.

Shane Whittaker

[116] Mr. Whittaker was employed by GBL as a financial analyst in the accounting department, starting in September 2005. He was involved in the preparation of financial statements for GBL and some of the related companies (eg. GRCL). He also handled bank reconciliations and made entries in the general ledger, for example if a security moved from non-collateral to collateral. He also assisted Mr. Drayton with respect to IT. He too was on the roster for entering and verifying trades.

(3) Board meetings

[117] Officers of LCL would attend GBL board meetings mainly as observers, though if there was a specific issue such as a standby credit facility that would directly affect LCL, they would have some input. Otherwise, according to Mr. Welch, they had no impact on board decisions. As Mr. Mavrinac explained, he would attend representing the shareholder but only asked questions as appropriate. Mr. Holland went further in identifying unrelated world events (the bankruptcy of Barings in the mid-1990s and the fraudulent assets held by Parmalat in 2003) causing LCL to have a policy to attend Board meetings of its affiliates.

E. Central Bank of Barbados ("CBB") Involvement

[118] Given the Respondent's concession in argument that GBL was regulated, it is unnecessary to provide exhaustive evidentiary detail of the CBB involvement, but for completeness' sake, I highlight the following.

[119] GBL, as a licensee under *OSBA* and later *IFSA*, was required to pay annual fees to the CBB. It did so for the years in issue.

[120] Mr. Berry testified that by April 30 of each year, GBL was required to provide the CBB with audited and signed financial statements. Also, every quarter a report was given to the CBB to address the capital adequacy of GBL. Examples

of the quarterly reports were provided (the fourth quarter for each of the years 2000 to 2010). These reports covered areas such as large exposures, number of employees, bad debts and capital adequacy, and listed all securities held by the counterparties of GBL.

[121] According to Mr. Berry, there was a CBB inspection in 2002 and periodic interviews between CBB officers and GBL officers. With respect to the inspection, the CBB wrote to GBL on November 12, 2002, as follows:

> We enclose eight (8) copies of the Examination Report of Glenhuron Bank Limited at June 15, 2002. The Examination covered the period January – June15, 2002 and was performed following the enactment of the International Financial Services Act 2002 (IFSA). In accordance with Section 53(1) of IFSA, the Central Bank conducted an onsite inspection of the licensee to determine the safety and soundness of the licensee and to assess compliance with IFSA.
>
> The Central Bank had initially submitted a draft Examination Report dated October 30, 2002 for discussion purposes to the management of the licensee. The licensee responded promptly and based on a review of the response document and discussions with management on November 7, 2002, the licensee has addressed our concerns and accepted our recommendations. The Central Bank has noted the effort taken in collecting delinquent loans. This will be verified in a future examination.

[122] The CBB issued regular guidance and regulatory notices and would occasionally ask for copies of GBL policies and procedures.

[123] The directors of GBL met once a year with representatives of CBB, usually in November. A common topic was the financial health of LCL, as well as the operations of GBL, and how world events might impact on it. In 2006 or 2007, according to Mr. Mavrinac, Loblaw had had bad results and the CBB asked that a representative of GBL's parent attend the annual meeting. Mr. Mavrinac attended.

[124] As well as the annual external audit, the CBB required an internal audit, which Mr. Berry described as "a more detailed discovery of the proper use of the policies and the controls within the bank." GBL relied on an internal control group of GWL to send a team from Toronto once a year for such purpose.

[125] Mr. Berry went through several communications between GBL and CBB, some of which are as follows:

1) In October 1998, GBL advised the CBB of a capital deficiency to which the CBB required an auditor's confirmation of receipt of funds to restore the capital base.

2) In July 2004, GBL advised the CBB of the repayment of $133 million loan to Loblaw Financial (then LIHI) and assuring the CBB the share capital was still strong.

3) In December 2004, GBL wrote to the CBB requesting that the CBB "confirm the intention of GBL to reduce its capital by an amount of $100 million." The CBB granted "approval" by letter of February 8, 2005.

4) In October 2007, GBL wrote to the CBB advising that it had entered a US $200 million standby credit with Loblaw Companies.

5) On June 21, 2002, the CBB wrote to GBL as follows:

> As you are aware, the Offshore Banking Act, 1980 has been repealed and replaced by the International Services Act, 2002. Section 53 of this Act provides for an examination to be made by the Central Bank of Barbados of the affairs of a licensee, to inter alia assess compliance with the Act and to determine whether the licensee is in sound financial condition.
>
> In this regard, a team from the International Financial Services Inspection Unit (IFSIU) will be visiting your office on June 4, 2002, to commence such an examination. During the initial meeting with you, we will communicate our information requirements.
>
> It is also our desire to meet with your External Auditors at a mutually agreeable date and time. We look forward to meeting with you.

6) On August 3, 2007, the CBB wrote to GBL as follows:

> The Central Bank of Barbados (Bank) in furtherance of its responsibility for the regulation and supervision of licensees under the Financial Institutions Act 1996-16 (FIA) and the International Financial Services Act 2002-5 (IFSA), is issuing this letter to provide guidance and share with the industry the ratios used in the offsite surveillance of institutions.
>
> During the period between onsite inspections, the Bank Supervision Department conducts intensive reviews of financial and prudential data submitted by licensees. As part of this on-going monitoring, the prudential quarterly returns and

> monthly schedules submitted to the department are analysed to assess the stability of licensees.
>
> The Bank calculates prudential ratios and supplemental ratios. While the prudential ratios are generally applicable to all licensees, there is likely to be significant variations in the supplemental ratios because of differences in organisational structure and business lines. However these ratios can facilitate analysis on a bank-by-bank basis against historical trends and comparisons with similar banks (peer groups).

[126] According to Mr. Welch, the CBB would also make *ad hoc* requests. His view was that the CBB wanted a feel for what impact offshore companies were having on the local economy.

F. Waivers

[127] The Canada Revenue Agency (the "CRA") commenced the audit of Loblaw Financial's 2001 taxation year in early 2005. Mr. Holland explained that Loblaw had a good working relationship with the CRA and that because the CRA had not completed their work before the time expired for assessing, Loblaw provided a waiver. The waiver for the 2001 year was prepared by the CRA and signed by Mr. Holland on July 14, 2006. The waiver stated:

> The normal reassessment period referred to in subsection 152(4) of the *Income Tax Act*, within which the Minister may reassess or make additional assessments or assess tax, interest or penalties under the *Act* is hereby waived for the taxation year indicated above, in respect of:
>
> > 1. Subsection 91(1) of the *Income Tax Act* – inclusion of foreign accrual property income of the controlled foreign affiliate (Glenhuron Bank Limited).
> >
> > 2. Subsection 91(4) of the *Income Tax Act* – deduction in respect of foreign taxes paid on the amounts included under subsection 91(1) of the *Act*.

[128] Mr. Holland's understanding was that the audit was a technical audit concerning FAPI. He did not believe the audit or the waiver related to an application of the GAAR.

[129] On August 2, 2006, the CRA wrote to Loblaw Financial, attention: Mr. Holland, outlining CRA's preliminary conclusion that GBL carried on an investment business and requesting certain information. No reference was made to

GAAR in this request. Mr. Holland was of the view that the request for information was in connection with the technical audit with respect to FAPI. From that point on, and into 2009, there were a number of communications between Mr. Holland and the CRA regarding the collection of additional information from Loblaw.

[130] On July 5, 2007, Mr. Holland signed a waiver of Loblaw Financial's 2002 taxation year, again the waiver having been prepared by the CRA. Two items were specified in the waiver:

> 1. Inclusion of FAPI of Glenhuron Bank Limited under subsection 91(1) of the *Income Tax Act*.
>
> 2. Deduction in respect of foreign taxes paid on FAPI of Glenhuron Bank Limited under subsection 91(4) of the *Income Tax Act*.

[131] Mr. Holland confirmed it was his understanding that the audit and the waiver related only to FAPI, with no mention or suggestion from the CRA that GAAR was at issue.

[132] On May 13, 2008, the CRA wrote to Loblaw, attention: Mr. Holland, with a comprehensive request for information from LCL, Loblaw Financial, GWL and GBL (relating to both financial derivative transactions and other activities). The years referred to in this request were 2001 to 2005. On May 15, 2008, the CRA indicated more time would be given to meet these requests if "acceptable waivers" were provided. The CRA again provided waivers. On June 4, 2008, Mr. Holland signed a waiver for the 2003 taxation year that stated:

> 1. Inclusion of FAPI of Glenhuron Bank Limited.
>
> 2. Deduction in respect of foreign taxes paid on FAPI of Glenhuron Bank Limited.

[133] A further information request was made by the CRA in June 2008 including for the minutes of GBL for the 2001 to 2005 taxation years. Likewise, into 2009, the CRA continued to follow-up on this request, including seeking information regarding the licence obtained under the *IFSA*. There is no reference to consideration of the application of GAAR in these correspondences. In May 2009, the CRA sought a waiver in connection with the 2004 taxation year of Loblaw Financial. The CRA prepared a waiver which covered the same two areas as set out in the 2003 waiver.

[134] On July 15, 2010, Mr. Holland signed a waiver for Loblaw Financial's 2005 taxation year. A third item was added to this waiver:

> 3. Deduction taken under section 113 in respect of dividend income received from GlenHuron Bank Limited.

[135] Mr. Holland testified his understanding remained that the subject matter was FAPI, with no consideration of an assessment under GAAR.

[136] On June 28, 2011, Mr. Holland received what he called a proposal letter from the CRA, the opening paragraph of which read:

> We have completed our review of the information you submitted in response to our letters May 13, 2008, June 19, 2008 and May 14, 2009 in respect of the activities of Glenhuron Bank Limited ("GBL"), a foreign affiliate of LFHI. Based on our review of the information you submitted, the financial statements of GBL, the *Offshore Banking Act* ("*OSBA*") and the *International Financial Services Act* (*"IFSA"*) of Barbados, it is our view that during the relevant period under review (2001 to 2006 taxation years), GBLs income is foreign accrual property income ("FAPI").

[137] Mr. Holland expanded on his understanding of the nature of a possible assessment in that it was limited to technical issues with respect to what the term "regulated" meant, whether derivative transactions were adventures in the nature of trade and whether other sources of income also represent investment income. Again, no reference was made in correspondences about the application of GAAR.

[138] On August 26, 2011, the CRA again requested more information from Loblaw including swap reconciliations, investment policies and information with respect to GBL employees. On July 30, 2012, the CRA asked for GBL's Barbados tax returns and assessments along with any withholding tax certificates. The CRA also requested a waiver for the 2007 taxation year.

[139] On August 1, 2012, the CRA wrote to Loblaw Financial, attention: Mr. Holland, as follows:

> The following summarizes the basis of our proposed assessment as previously outlined in our letter dated June 28, 2011:
>
> 1. GBL is not "regulated" within the meaning of that term in subsection 95(1) of the *Income Tax Act*,

> 2. The income from GBL's derivative transactions is income from an adventure in the nature of trade,
>
> 3. Interest in similar returns earned by GBL is income from property, and
>
> 4. The principal purpose of GBL's business is to derive income from property.
>
> Based on the above, it is our view that GBL's business does not fall under the exception to the "investment business" definition in subsection 95(1) of the *Income Tax Act*. Accordingly, GBL's business constitutes an "investment business" and its income is a FAPI to LFHI.

[140] The letter also advised that the case had been referred to aggressive tax planning ("ATP").

[141] Mr. Holland signed a waiver for the 2007 taxation year on August 13, 2012, which specified the three items previously mentioned. The next day, August 14, 2012, he had a call from Ms. Lau at the CRA indicating that ATP requested an additional waiver that would include the GAAR. This is followed up with a letter the same day making the same request, attaching a waiver that specified the application of GAAR under section 245. Mr. Holland provided the waiver, signed April 29, 2013 for the 2008 taxation year which included specific reference to GAAR.

[142] The CRA conducted a site visit to Barbados in June 2013 where just Mr. Berry was provided to answer any CRA inquiries. On October 22, 2013, Loblaw counsel provided a binder to the CRA containing answers to undertakings given at that visit. On July 17, 2014, the CRA wrote to Loblaw Financial regarding the taxation years 2001 to 2010 as follows:

> The purpose of this letter is to put forth our position with respect to whether:
>
> 1. The business carried on by GBL qualifies as an exemption to "investment business" as defined in subsection 95(1) of the *Income Tax Act* ("*Act*"), more specifically, whether GBL carried on its business as a "foreign bank" in Barbados and that business is required to be regulated under the *International Financial Services Act* ("*IFSA*") of Barbados; and whether
>
> 2. The general anti-avoidance rule ("GAAR") applies to the series of transactions undertaken by LFHI and GBL (formerly Loblaw Inc. (Barbados)) to give the appearance of compliance with the exception to "investment business" as defined in subsection 95(1) of the *Act*.

[143] The CRA identified the following as avoidance transactions constituting the series of transactions that would be captured by the GAAR provisions of the *Act*:

> i. the incorporation of Loblaw Inc. in Barbados by LFHI as an international business corporation with an initial capital of US $100,000 in common shares;
>
> ii. the issuance of US $67 million in preferred shares to a wholly-owned foreign affiliate of LFHI that was subsequently transferred to LFHI when that affiliate was wound-up;
>
> iii. the name change of the Barbados subsidiary from Loblaw Inc. to Glenhuron Bank Limited so that the word "Bank" was in its name;
>
> iv. the application and obtainment of an offshore banking licence by GBL under Barbados OSBA;
>
> v. the continuation of the banking licence under the IFSA upon the repeal of the OSBA of Barbados;
>
> vi. the voluntary annual licence renewal and payment of the renewal fee to the CBB; and
>
> vii. managing its own funds and that of related parties, ie. GBL was not in the business of accepting funds from arm's length third parties.

[144] Ms. Lau testified that notwithstanding legislation amending the FAPI rules was enacted in June 1995, there was a backdrop of information (the Auditor General's Report and the Standing Committee Report) going back to early 1992 that the tax community was fully aware of. She described Loblaw's actions as a pre-emptive move regardless of how the final legislation might read. She acknowledged that GBL was incorporated (September 1992) a couple of months before the Auditor General's Report (November 1992). Similarly, with respect to the issuance of shares by GBL to GOBV in February 1993 and the application for a licence in November 1993, Ms. Lau confirmed that the CRA viewed these events as attempts to circumvent law that may come into place in the future, details of which were at that point unknown.

G. Assessments and Objection

[145] In Notices dated March 27, 2015, the Minister reassessed Loblaw Financial on the basis that income earned by its controlled foreign affiliate GBL was FAPI as defined under subsection 95(1) of the *Act*, as follows:

Loblaw Financial Taxation Year	FAPI Reassessed (Cdn Dollars)
2001	$84,145,457
2002	$95,522,133
2003	$63,898,088
2004	$43,602,018
2005	$43,468,016
2008	$128,948,511
2010	$13,838,390

[146] Loblaw Financial objected to these reassessments by way of Notice of Objection filed on April 1, 2015. In its reasons for objection, Loblaw Financial stated:

> 28. The Taxpayer disputes the correctness of the Reassessments. More particularly, the issues in dispute are whether the Minister was:
>
> (a) correct in concluding that the active business income of Glenhuron Bank constituted income from an investment business and therefore income from property and FAPI;
>
> (b) precluded from relying in the alternative on the GAAR in support of the Reassessments for 2001-2005 Taxation Years and, assuming the Minister was not so precluded,
>
> (c) correct in applying the GAAR to recharacterize the active business income from an investment business and therefore income form property and FAPI.
>
> 29. Assuming that the Minister was correct in concluding that some or all of the active business income of Glenhuron Bank for the Taxation Years constituted income from an investment business, and therefore income from property and FAPI, the issue is also whether the Minister correctly computed such FAPI.
>
> 34. For the purposes of the Act, "foreign bank" is defined by reference to the definition in section 2 of the *Bank Act*. Under this definition, a foreign bank includes an entity incorporated or formed by or under the laws of a country other than Canada that "is a bank according to the laws of any foreign country where it carried on business."
>
> 35. Glenhuron Bank was a bank according to the laws of Barbados and, as a result, it qualified as a "foreign bank" for the purposes of the "investment business" definition in subsection 95(1).

> 36. Since Glenhuron Bank carried on a single active business, all of its activities were carried on by it as a foreign bank. In addition, as a result of being a licensee under the OSBA and later the IFSA, Glenhuron Bank was subject to the oversight and regulation of the Central Bank in respect of all of its activities.
>
> 37. As a result, Glenhuron Bank satisfied the "regulated foreign bank" aspect of the relevant exception set out in each of subparagraph (a)(i) of the "investment business" definition in subsection 95(1) of the Act.
>
> 38. Finally, a regulated foreign banking business will not be an "investment business" as defined in subsection 95(1) if more than five full-time employees are employed in the active conduct of the business. At all relevant times, Glenhuron Bank employed more than five employees full time in the active conduct of its business.

H. Expert Evidence

[147] The Appellant produced two expert witnesses, Ms. Jones and Ms. Mahabir, both legal practitioners from Barbados. Ms. Jones testified on the issue of whether or not GBL is a bank under the laws of Barbados, while Ms. Mahabir addressed the area of regulations governing international banks. The Respondent produced one expert, Professor Antoine, Dean of the Law School of West Indies, who provided evidence on both the issue of whether GBL is a bank under Barbados law, as well as on the regulatory regime in Barbados.

[148] While there was extensive expert evidence, I distill it down to the following. There has developed two financial regulatory regimes in Barbados, a dualism as Professor Antoine suggested, one branch dealing with domestic or onshore financial activities and the other with offshore financial activities. The former I will refer to as commercial banks, as that term is used in the legislation itself, and the latter as international banks. International banks have evolved primarily due to a desire of Barbados to attract foreign investment and provide an innovative, safe and regulated environment within which to operate. Thus, back in 1980, the *OSBA* was introduced to establish laws surrounding this new offshore financial sector. This added to the then limited legislative regime which was based mainly on the *Banking Act* and *Central Bank Act*. The *Banking Act* was repealed in 1992 with the introduction of the *International Business Companies Act* and the *Financial Intermediaries Regulatory Act*. The latter Act was repealed and replaced by the *Financial Institutions Act* in 1997, applicable to commercial banks. The *OSBA* was repealed and replaced with the *International Financial Services Act* ("*IFSA*") in 2002. One of the effects of the introduction of *IFSA* was that pursuant to section

114, all banks licensed under the *OSBA* automatically became licensees under the *IFSA*. It is unnecessary to go into great detail of the policy reasons surrounding the move from the *OSBA* to *IFSA*, suffice it to say the term "offshore" may have held some negative connotations not highlighted in the term "international financial services." Likewise, "international banks" may have seen to be more benign and perhaps acceptable to the international community and organizations such as the OECD, than the term "offshore bank."

[149] Attached as Appendix D is a list of relevant legislation from Barbados that the experts referred to, showing the timing and evolution of financial related legislation including the *Banking Act*, *Central Bank of Barbados Act*, *OSBA*, *Exempt Insurance Act*, *International Business Companies Act*, *Financial Intermediaries Regulatory Act*, *Financial Institutions Act* and *IFSA*.

[150] As Professor Antoine pointed out, the only definition of "bank" is found in section 2 of the *Central Bank of Barbados Act* and section 2 of the *Financial Institutions Act*. It is noteworthy that the definition section in the *Central Bank of Barbados Act* is preceded by the words "for the purposes of this Act,":

> *Central Bank of Barbados Act*
>
> s.2 "bank" means a bank licensed to carry on banking business in Barbados under *The Financial Institutions Act*, Cap. 324;
>
> *Financial Institutions Act*
>
> s.2 "bank" means a company carrying on banking business;

Notwithstanding that limitation, Professor Antoine's view was that Barbados has legislated just the one definition of a bank and that is the one found in the *Financial Institutions Act*. She opines that if the entity is not captured by this definition, it is simply not a bank under Barbados law. Period, full stop. When questioned about this limitation, Professor Antoine responded as follows:

> A. Okay. So that is said there, and generally, in a statute, that would mean, well, several things, one, that if there's a contradictory definition elsewhere, then, of course, that would hold. In this case, there isn't.
>
> But, also, even if we were to accept what I said would be a narrow view of the phrase to mean that only activities and entities within the scope and purpose of this Act, i.e., the Central Bank Act, even it was to say that is the reason why that was there, then it would still include international bank by the virtue of the fact

> that the Central Bank does have regulatory jurisdiction over international banks. So it must mean logically that the definition of a bank under the Central Bank Act is to encompass entities and other financial institutions such as international banks.
>
> Q. I'm not sure that I understand. Could you break that down a little bit?
>
> A. Okay. So what I'm saying is that, first of all, the – for the purposes of this Act, if there were a contradictory definition of a bank elsewhere, that could probably – would be, say, containing to this Act. But also even if I were to say, okay, for the purposes of this Act means that the definition of a bank under the Central Bank Act is only to apply to those entities and activities which fall under the regulatory jurisdiction of the Central Bank Act or the jurisdiction and scope of the Central Bank Act, even if we say that is what it means, which I consider to be a very narrow definition of for the purposes of this Act, but I can see that you could look at it in that way.
>
> Even then I would say it encompasses an international bank because there's no question that an international bank falls within the jurisdiction of the Central Bank. So it must mean that the definition of a bank under the Central Bank Act includes, includes all of the entities that falls within the Central Bank Act. And since the bank, that definition, excludes international banks, one could not say that, for the purposes of this Act, excludes the concept of an international bank.
>
> The definition of a bank under the Central Bank is a universal definition. It is wide enough to include all entities and all financial institutions, including an international bank falls within the jurisdiction of Central Bank, and the definitions clearly excludes international banks. So we couldn't say, for instance, that the Central Bank definition is to be contained to the Central Bank only, and, therefore, when we look at the International Financial Services Act, you cannot use the Central Bank definition to determine what is a bank. Is that a little clearer?

[151] With respect, I do not find her position persuasive. Simply because the CBB has authority over international banks, it does not follow that the term "bank" that is limited to the *Central Bank of Barbados Act* applies to preclude an international bank from being considered a bank under Barbados law. The CBB authority over international banks does not arise under the *Central Bank of Barbados Act* but arises under either *OSBA* or *IFSA*. The legislative words are clear. The *Financial Institutions Act* definition does not extend its net to capture the other branch of legislated financial activities found in *OSBA* and later *IFSA*. The definition of a commercial bank as a bank under the *Financial Institutions Act* simply does not preclude "bank" encompassing an international bank under *IFSA*. I conclude that whether or not an international bank under *IFSA* is a bank is not answered by reference to the legislation that deals only with commercial banks. It flies in the

face of Professor Antoine's own recognition of the duality of the regimes. As Ms. Jones concluded:

> Under Barbados law, during the Relevant Years (and currently) the FIA determined (determines), whether any entity which conducted (conducts) Domestic Business was (is) a bank. Under the FIA, the definitions set out in section 2 prescribe the criteria that determine whether the activities of such an entity constitutes (constitute) the type of business that would qualify it as a bank.
>
> During the OSBA Years, the OSBA determined whether any entity which conducted International Business was a bank. Under the OSBA, the provisions of sections 4(1) and 4(2) prescribed the criteria that determined whether the activities of such an entity constituted the type of business that would qualify it as a bank.
>
> Thereafter, during the IFSA Years (and currently), the IFSA determined (determines) whether any entity which conducted (conducts) International Business was (is) a bank. Under the IFSA, the provisions of section 4(2) prescribe the criteria that determine whether the activities of such an entity constituted (constitute) the type of business that would qualify it as a bank.

[152] So, what is the thrust of the offshore legislation, and to be clear, I will concentrate on *IFSA*. There is no question *IFSA* considers financial institutions licensed under its regime to be international banks. Professor Antoine opines that in dealings with such entities you cannot separate the word "bank" from the word "international": you cannot talk of a bank providing international financial services but only an international bank can provide international financial services, or as the *IFSA* itself reads, international banking business.

[153] To be clear, neither *OSBA* nor *IFSA* define "bank" as such, but *IFSA* defines "international banking business" (subsection 4(2)) and *OSBA* defines offshore banking (subsections 4(1) and (2)).

> *IFSA* subsection 4(2)
>
> For the purposes of subsection (1), "international banking business" means
>
> (*a*) the business of receiving foreign funds through
>
> (i) the acceptance of foreign money deposits payable upon demand or after a fixed period or after notice;

(ii) the sale or placement of foreign bonds, foreign certificates, foreign notes or other foreign debt obligations or other foreign securities; or

(iii) any other similar activity involving foreign money or foreign securities;

(*b*) the business of using the foreign funds so acquired, either in whole or in part, for

(i) loans, advances and investments;

(ii) the activities of the licensee for the account of or at the risk of the licensee;

(iii) the purchase or placement of foreign bonds, foreign certificates, notes or other foreign debt obligations or other foreign securities; or

(iv) any other similar activity involving foreign money or foreign securities; or

(*c*) the business of accepting in trust from persons resident outside Barbados or from prescribed persons

(i) amounts of money in foreign currencies or in foreign securities or both;

(ii) foreign personal property or foreign movable property; or

(iii) foreign real property or foreign immovable property.

OSBA subsection 4(1) and (2)

4(1) Off-shore banking is

(*a*) receiving foreign funds through

(i) the acceptance of foreign money deposits payable upon demand or after a fixed period or after notice,

(ii) the sale or placement of foreign bonds, certificates, notes, or other debt obligation or other foreign securities, or

(iii) any other similar activity involving foreign money or foreign securities, and

> (*b*) either in whole or in part using the foreign funds so acquired for
>
> (i) loans, advances and investments, and
>
> (ii) the activities of the person carrying on that business, for the account of, or at the risk of, that person.
>
> (2) Subject to such regulations as may be made in that behalf, off-shore banking includes the acceptance in trust of
>
> (*a*) amounts of money in foreign currencies or in foreign securities or both,
>
> (*b*) foreign personal or movable properties, or
>
> (*c*) real or immovable property outside Barbados,
>
> from persons resident outside Barbados to be administered, managed or invested or otherwise dealt with for the benefit of persons resident outside Barbados, and includes any activities related, incidental or ancillary thereto.

[154] These definitions contemplate banking as the receipt of foreign funds and use of such funds for financial transactions involving foreign money, debt instruments, securities or assets conducted with foreign counterparties. And, only entities restricted to such activities can be licensed under *OSBA* or *IFSA*. Further, in keeping with the duality referred to earlier, the *Financial Institutions Act* (dealing with commercial banks) does not apply to licenses under *OSBA* or *IFSA*.

[155] There are other legislative clues both in *OSBA* and *IFSA* that support the view that entities licensed thereunder to conduct offshore or international banking are banks. When the *Banking Act* was repealed in 1992, it was first replaced by the *Financial Intermediaries Regulatory Act* which stipulated in section 108:

> The Minister may, in the public interest, direct any person other than a bank licensed under Part II or Part III, or the *Offshore Banking Act*, that is trading or carrying on business under any name or title of which the word "bank" or any variation forms part to delete from the name under which the business carried on the word "bank" or any variation thereof.

[156] Likewise, when the *Financial Institutions Act* replaced the *Financial Intermediaries Regulatory Act*, section 103 provided:

> Any person other than a bank that is a licensee under Part II or III or a person licensed under the *Offshore Banking Act* who, in connection with a trade or business carried on by him, uses the word "bank" …

[157] Further, both *OSBA* in section 67 and *IFSA* in section 105, stipulated that no person other than a business licensed under their respective legislation can use the word "bank" in its name.

[158] I conclude from a reading of *OSBA* and *IFSA* that the authority of the CBB to regulate international banks does not emanate from the *Central Bank Act*, (an Act that pre-dates *OSBA* and *IFSA*) but from *OSBA* and *IFSA*, the legislation governing the international arm of the banking regimes. This is apparent, for example, from the requirement found in section 47 of *IFSA* that the licensee submit quarterly statements to the CBB. This authority does not arise under the *Central Bank Act*, where the defined term "bank" is limited to commercial banks. Again, this impresses upon me Professor Antoine's opinion of two financial regimes, except her opinion concludes that a bank under Barbados law is exclusively the domain of the onshore regime. I find the legislation does not support that conclusion. My view is further cemented by the introduction of paragraph 5(8)(A) of *IFSA* which reads:

> For the purposes of this Act, an eligible company that is licensed under this Act to carry on
>
> a) International banking business under section 4(1)(a); or
>
> b) Any other financial service related or ancillary to international banking business under section 4(1)(b)
>
> shall be regarded as an international bank and shall be regulated by the Central Bank in accordance with this Act.

[159] Even if I were to turn to the *Financial Institutions Act* (the commercial banking arm of Barbados legislation), I find support for the view that it too reflects that an international bank under the international banking arm is a bank. For example, in section 100 it is stipulated that the Minister may direct any person "other than a bank licensed … under the *Offshore Banking Act*."

[160] It is noteworthy that the section uses bank in the context of a license under the *OSBA*, although "bank" is defined under the *Financial Institutions Act* as a commercial bank. This irregularity appears to be corrected in section 103 where the term person is used rather than bank.

[161] The impact of these provisions is that the legislation only allows a commercial bank and an international bank to use the word "bank" in its name. This does not suggest to me that the commercial bank definition found in the *Financial Institutions Act* is exhaustive of that term under Barbados law. Quite the opposite, it reflects the dual nature of banks under Barbados law – onshore (commercial) and offshore (international).

[162] The experts on both sides respectfully suggested that Barbados legislators could update and improve their drafting. Section 100 of the *Financial Institutions Act* is perhaps an example where an amendment is required to replace *OSBA* with *IFSA* and the word "bank" in the *OSBA* context to "person." Professor Antoine takes this view further and opines that the legislators and others incorrectly used the term "bank" loosely. It would be carrying that theory too far to conclude that allowing an international bank to call itself a bank is simply a matter of the legislators being loose with the term. I give them more credit. There are commercial banks and international banks and I conclude the terms are used deliberately to denote banks.

[163] Similarly, the CBB itself on more than one occasion used the term "bank" in their letters to GBL (see for example letters of June 30, 2000, May 31, 2001, July 5, 2002 and March 18, 2003). These are not instances of the term "bank" being used in conjunction with offshore or international. They are not referred to as financial institutions. It is one thing for the international financial community to be loose with the term, but when this emanates from the very regulatory authority of Barbados overseeing financial institutions, I conclude that this is not merely being fast and loose with an expression. The CBB viewed GBL as a bank.

[164] I disagree with Professor Antoine that international banks and commercial banks need to be treated as equivalent for an international bank to be considered a bank under Barbados law. I simply do not accept there is one universal legislative definition of bank in the so-called dualistic legislative landscape of financial institutions operating in Barbados. Banks licensed under the *Financial Institutions Act* and international banks licensed under *IFSA* are both "domestic" banks as they are both governed by domestic laws: one set of domestic laws deal with the onshore sector commercial banks and the other set of domestic laws deal with the offshore sector international banks.

[165] Section 5(6) of *IFSA* provides that a company is not required to be licensed where it receives foreign funds from affiliates or associates which are used for the purposes of loans or advances to or investments in affiliates or associates or for

purposes specified in paragraph 4(2)(b) of *IFSA*. I accept Ms. Jones view that the flexibility afforded in this provision to international banks does not impact the definition of "international banking business" or, as a corollary to that, the proper categorization of an entity which conducts such business as an international bank.

[166] It was pointed out that there are other Acts in Barbados that also refer to "bank" in connection with an international bank. For example, in the *International Trusts Act*, section 2 defines beneficiary to include "a bank licensed to carry on an international financial service under the *International Financial Services Act.*" Also in the *Exempt Insurance Act*, subsection 17(4) stipulates "notwithstanding section 30 of the *Companies Act*, paid up capital or contributed reserves may be in the form of valid irrevocable letters of credit drawn on or confirmed by a bank licensed under the *Banking Act* or the *Offshore Banking Act.*" I do not accept that the legislation referring to a bank under either the *OSBA* or *IFSA* is simply being loose with the term. This supports the view that "bank" under Barbados law is not limited to commercial bank, as "bank" is defined under the *Financial Institutions Act*, but does also include as a bank an international bank or offshore bank under *IFSA* or *OSBA*.

[167] I am also swayed by Ms. Jones' conclusion that:

> 31. The Central Bank has always regulated banks, with the Financial Services Commission, and previously, its predecessors, the Securities Commission and the Office of the Supervisor of Insurance, (collectively the "FSC") have regulated non-bank financial services entities. If licensees under the Acts were not banks under Barbados law, the Central Bank would not regulate them.

[168] Finally, I note an *IFSA* licensee, Cidel Bank and Trust Inc., gave notice of its intention to establish a Schedule II bank in Canada (Canada Gazette Part 1, 27 April 2013) in the following terms:

> Notice is hereby given that Cidel Bank & Trust Inc., a bank under the laws of Barbados, intends to file with the Superintendent of Financial Institutions (the "Superintendent"), on or after May 20, 2013, an application pursuant to section 25 of the Bank Act (Canada) for the Minister of Finance to issue letters patent incorporating a Schedule II bank pursuant to the Bank Act (Canada) under the name Cidel Bank Canada, in English, and Banque Cidel du Canada, in French, to carry on the business of a bank in Canada. Its head office will be located in the city of Toronto, Ontario.

[169] The expert evidence satisfies me that an international bank licenced under *IFSA* and an offshore bank licenced under *OSBA* are banks under Barbados law.

[170] The question then becomes, if an international bank is a bank under Barbados law, was GBL an international bank? I will discuss this under the "Reasons" section.

[171] With respect to the Barbados regulation, Mr. Mahabir's expert testimony was based on the correct assumption that GBL held a licence under either *OSBA* or *IFSA* during the years in issue. The import of this is that a licensee would be subject to certain statutory obligations, such as capital adequacy requirements, reserve funds, quarterly reports and audits required by *IFSA*, as well as subject to the CBB's guidelines. Ms. Mahabir saw little difference in the regulatory scheme governing international banking and commercial banking. She suggested the latter would provide more information to the CBB simply because they would have a larger portfolio and take deposits from the public.

[172] Crucially, *IFSA* legislation introduced the power of the CBB to examine and inspect. Ms. Mahabir opined that the CBB's practice, even under *OSBA*, was that they could and did exert a right to inspect.

[173] Ms. Mahabir pointed out that international business companies are not regulated by the CBB but by an entirely different Ministry.

[174] Generally, Ms. Mahabir described the CBB regulatory role was to ensure people engaged in interacting with a bank are protected against risk and, secondly, for Barbados to maintain its reputation in the international financial community.

[175] Ms. Mahabir confirmed that the introduction of paragraph 5(8)(A) (retroactive to 2002) in *IFSA* did two things:

1) confirmed a licensee should be regarded as international bank, and

2) that it should be regulated by the CBB.

[176] Ms. Mahabir also provided a Rebuttal Report to Professor Antoine's Report. Professor Antoine's view that the regulatory regime for commercial banks is stricter was distinguished by Ms. Mahabir. It was her view that there may be differences due to different risks, for example arising from the deposit taking nature of a commercial bank; that is, the difference is in what the CBB is looking

at. But, Ms. Mahabir maintained the regulatory and supervisory role of the CBB with respect to both commercial and international banks was the same. Frankly, I discern little difference between Ms. Mahabir and Professor Antoine as to the regulatory authority of the CBB over international banks, and given the respondent's concession accepting GBL was regulated, I need not explore the expert testimony on this point any further.

II. ISSUES

[177] For the sake of fluidity, I repeat the issues:

A. Is Loblaw Financial precluded from relying on certain arguments due to the application of the large corporation rule (subsections 165(1.11) and 169 (2.1) of the *Act*)?

B. Was income earned by GBL in 2001-2005, 2008 and 2010 FAPI pursuant to subsection 95(1) of the *Act*?

(1) Was GBL carrying on an investment business as defined in the preamble to the definition in subsection 95(1) of the *Act*?

(2) Was GBL exempted out of the definition?

(a) Was it a foreign bank?

(i) Pursuant to the definition in subsection 2(a) of the *Bank Act* of Canada?

(ii) Pursuant to the definition in subsection 2(c) of the *Bank Act* of Canada?

(b) Was it conducting business principally with persons with whom it did not deal at arm's length?

(c) Was it regulated under the laws of Barbados?

(d) Did it employ more than five full time employees or the equivalent thereof full time in the active conduct of the business?

C. If Loblaw Financial received FAPI from GBL has it been correctly calculated?

(1) Were the foreign exchange gains/losses arising on GBL's investments in short term securities on income or capital account?

(2) Does the inclusion in FAPI arising from the deemed separate business provision in paragraph 95(2)(*b*) of the *Act* include the fees received from Weston Acquisitions Inc., Weston Funds, Inc., Weston Foods US, Inc. and JFS Inc. (the "Disputed Entities")?

D. If GBL was not carrying on an investment business is Loblaw Financial caught by the application of the GAAR?

(1) Do the waivers for the taxation years 2001 to 2005 preclude the Respondent from relying on the GAAR for those years?

(2) Was there a tax benefit?

(3) Were there avoidance transactions?

(4) Was there an abuse of the FAPI provisions, specifically subsection 95(1) of the *Act*?

E. If the GAAR applies how is Loblaw Financial to be taxed?

III. REASONS

A. Is Loblaw Financial precluded from relying on certain arguments due to the application of the Large Corporation Rule (subsections 165(1.11) and 169 (2.1) of the *Act*)?

[178] The Respondent brought a Motion returnable the first day of trial for an Order:

> 1. Directing that the appellant cannot advance an argument or seek to have the reassessments at issue vacated or varied on the basis of, or otherwise seek relief with respect to, the issue of whether the appellant's controlled foreign affiliate Glenhuron Bank Limited ("Glenhuron") employed "the equivalent of more than five employees full time in the active conduct of its business…" as set out in definition of "investment business" at ss. 95(1)(c)(ii) of the *Income Tax Act* (the "*Act*") (the "Equivalent to Full Time Issue").

2. Directing that the appellant cannot advance an argument or seek to have the reassessments at issue vacated or varied on the basis of, or otherwise seek relief with respect to the issue of whether Glenhuron was "foreign bank" pursuant to ss. (c) of the definition of "foreign bank" in s. 2 of the *Bank Act*, which is incorporated by reference in the definition of "foreign bank" in ss. 95(1) of the *Act* (the "New Foreign Bank Definition Issue").

3. Directing that the appellant cannot lead evidence at the hearing of this appeal that relates only to the Equivalent to Full Time or the New Foreign Bank Definition Issues.

4. Awarding the costs of this motion to the respondent in any event of cause.

5. Such other or further relief as counsel may advise and this Honourable Court deem appropriate.

[179] I held a conference call the week before trial expressing concerns as to the timing and substance of this Motion. I advised the Parties that it would be impossible, from my perspective, given the nature of the evidence that I expected to hear, to separate out what evidence might relate solely to the equivalent to full-time issue and new foreign bank definition issue. I concluded, therefore, the Motion went more to limitations on argument, and that such could be deferred until argument at the end of trial. Thus, I now have to deal with this Motion.

[180] In bringing this Motion, the Respondent relies on the Large Corporation Rule found in subsections 169(2.1) and 165(1.11) of the *Act* which read as follows:

169 (2.1) Notwithstanding subsections 169(1) and 169(2), where a corporation that was a large corporation in a taxation year (within the meaning assigned by subsection 225.1(8)) served a notice of objection to an assessment under this Part for the year, the corporation may appeal to the Tax Court of Canada to have the assessment vacated or varied only with respect to

(*a*) an issue in respect of which the corporation has complied with subsection 165(1.11) in the notice, or

(*b*) an issue described in subsection 165(1.14) where the corporation did not, because of subsection 165(7), serve a notice of objection to the assessment that gave rise to the issue

and, in the case of an issue described in paragraph 169(2.1)(a), the corporation may so appeal only with respect to the relief sought in respect of the issue as specified by the corporation in the notice.

> 165(1.11) Where a corporation that was a large corporation in a taxation year (within the meaning assigned by subsection 225.1(8)) objects to an assessment under this Part for the year, the notice of objection shall
>
> (*a*) reasonably describe each issue to be decided;
>
> (*b*) specify in respect of each issue, the relief sought, expressed as the amount of a change in a balance (within the meaning assigned by subsection 152(4.4)) or a balance of undeducted outlays, expenses or other amounts of the corporation; and
>
> (*c*) provide facts and reasons relied on by the corporation in respect of each issue.

[181] The relevant portions of the Notice of Objection are found in paragraph 146 of these Reasons. It is also noteworthy that attached to the Notices of Objection was a copy of the CRA's proposal letter of July 17, 2014, which specifically addresses the application of the definition of foreign bank in subsection 2(c) of the *Bank Act*.

[182] The Respondent's position now is that Loblaw Financial cannot argue the reassessments can be varied or vacated on the basis of the Equivalent to Full Time Issue and New Foreign Bank Definition Issue as Loblaw Financial failed to:

1) reasonably describe these issues in its Notice of Objection, given there was no mention of subparagraph 95(1)(*c*)(ii) of the *Act* or subsection 2(*c*) of the *Bank Act*, and

2) provide any of the facts or reasons that it was relying on in respect of those issues in its Notice of Objection.

[183] Although Loblaw Financial brings a preliminary objection that the Respondent's Motion is an abuse of process and should be dismissed on that basis, I do not intend to rely on that position but rather decide on the merits.

[184] The Federal Court of Appeal was clear in *Devon v R*[1] that the purpose of the Large Corporation Rule was so the Minister knows the nature of the dispute and the quantum of tax at issue at the objection stage. It relied on the following

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[1] 2015 FCA 214.

comment in the Federal Court of Appeal decision in *Potash Corp of Saskatchewan Inc. v R*:[2]

> 4. The Large Corporation Rules were enacted in 1995 to discourage large corporations from engaging in a full reconstruction of their income tax returns for a particular year, after the objection or appeal process had started, based on developing interpretations and the outcome of court decisions in litigation involving other taxpayers…. Simply put, Parliament wants the Minister of National Revenue (the "Minister") to be able to assess at the earliest possible date both the nature and quantum of pending tax litigation and its potential fiscal impact.

[185] In *Bakorp Management Ltd. v R*[3] the Federal Court of Appeal confirmed the purpose of the Large Corporation Rule was to enable the Minister to assess the potential fiscal impact of the disputes.

[186] Frankly, I could stop here and dismiss this Motion, at it is clear to me that Loblaw Financial was not engaged in a full reconstruction (there was no reconstruction), the potential fiscal impact was known, the quantum at issue remained the same, as did the nature of the dispute, being whether or not income of GBL was FAPI, or even digging deeper, whether GBL satisfied the regulated foreign bank exception. The Respondent would have the large corporation dig even deeper and specify whether there is only one definition of foreign bank being relied upon, or whether the issue of employees should be broken down to full-time employees versus the equivalent thereto. With respect, especially in a case where the government is invoking the GAAR, which requires evidence of the nature of the business GBL carried on and, indeed, how it was carrying on that business through its employees, reliance on the Large Corporation Rule on these two fronts creates an unlevel playing field tilted to the Respondent, as it would deprive Loblaw Financial of arguments founded in the same evidence.

[187] To this view, I add my concern as to the lateness of the Motion, and I conclude that, while this may constitute what the Respondent believes is a normal thrust and parry of litigation in a large, complex tax matter, I find it stretches the very basis for the Large Corporation Rule beyond what the jurisprudence suggests is appropriate. It demands that I look into the minutia of what is meant by a reasonable description of an issue, and the facts and reasons relied on, to somehow

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[2] 2003 FCA 471.

[3] 2016 FCA 106.

justify the reliance on this Rule in the first place. There must be a threshold of fair play before doing so.

[188] Both Parties attempted to rely on excerpts from examinations (interestingly Loblaw Financial put forth questions of its own nominee in this regard). I do not need to consider these, as I am of the view that the Equivalent to Full Time Issue and New Foreign Bank Definition Issue are integrally intertwined with the broader issues over which there is no controversy (the definition of a foreign bank and the circumstances surrounding employment of the employees). The Respondent argues that the two issues must have at least an "intermediate level of detail," but this, I suggest, as noted by the Federal Court of Appeal in *Potash*, will vary in each case depending on the degree of specificity required by the Minister to know each issue.

[189] With respect to the new foreign bank definition issue, I note that paragraph 34 of the Notice of Objection does not mention section 2(a) of the *Bank Act* specifically, though it is implicit, but it states a "foreign bank includes an entity…." This leaves the same door open, without opening new doors, to claim GBL was a foreign bank under subsection 2(c). The Respondent describes Loblaw Financial's statement of the issue in dispute as vague. I disagree. The issue is whether GBL was a foreign bank. The Respondent knew full well that there would be considerable evidence as to what GBL did. This encompasses activities that might constitute the provision of financial services (part of the *Bank Act*, subsection 2(c)) definition. Further, the Respondent put into issue in its GAAR assessment, the insertion of the word "bank" in GBL's name, another element of the subsection 2(c) definition under the *Bank Act*.

[190] Similarly, maintaining in the Notice of Objection that GBL had greater than five full-time employees, without adding the words "or equivalent thereof" should not handcuff the Appellant. The Respondent knew the number of employees was at issue. The Respondent knew considerable evidence would need to be presented at trial surrounding the employees and their duties and work habits: whether there was the equivalent of five full-time employees is subsumed into the employee issue generally. To let me consider whether the working environment had greater than the equivalent of five full-time employees in no way prejudices the Respondent. Employees were in issue.

[191] The quantum in issue has not changed from the Notice of Objection to the trial. Two key factors in determining the overriding issue of whether GBL's income was FAPI related to employees and to the definition of a foreign bank. That did not change from the Notice of Objection to the trial. I have reviewed the

cases to which I was referred including *Bakorp Management Ltd. v R*,[4] *Devon* and *Potash*, and I draw a distinction between those cases where the Large Corporation Rule was successfully invoked and the case before me. The broadening of Loblaw Financial's argument to encompass the two issues is, in the overall ambit of this Appeal, minor. I conclude:

1) It does not go down a different path than the Parties were already on.

2) It does not take the Respondent by surprise.

3) It does not require the introduction of any additional evidence.

4) It does not prejudice the Respondent.

5) It is not the shift in direction that the Large Corporation Rule is meant to curb: there is no reconstruction.

The Motion is dismissed.

B. Was income earned by GBL in 2001-2005, 2008 and 2010 FAPI pursuant to subsection 95(1) of the *Act*?

(1) Was GBL carrying on an investment business as defined in the preamble to the definition of investment business found in subsection 95(1) of the *Act*?

[192] To set the legislative stage as to why this question is the starting point, I turn first to subsection 91(1) of the *Act* which stipulates:

> In computing the income for a taxation year of a taxpayer resident in Canada, there shall be included, in respect of each share owned by the taxpayer of the capital stock of a controlled foreign affiliate of the taxpayer, as income from the share, the percentage of the foreign accrual property income of any controlled foreign affiliate of the taxpayer, for each taxation year of the affiliate ending in the taxation year of the taxpayer, equal to that share's participating percentage in respect of the affiliate, determined at the end of each such taxation year of the affiliate.

[193] There is no issue that GBL is a controlled foreign affiliate of the Appellant.

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[4] 2014 FCA 104.

[194] The taxpayer, pursuant to subsection 91(4) of the *Act* gets to deduct foreign tax paid on the FAPI.

[195] Subsection 95(1) of the *Act* defines FAPI to include the affiliate's income from property, which in turn is defined in subsection 95(1) as:

> For the 2000 to 2008 taxation years
>
> income from property of a foreign affiliate of a taxpayer for a taxation year includes its income for the year from an investment business and its income for the year from an adventure or concern in the nature of trade, but, for greater certainty, does not include its income for the year that is because of subsection (2) included in its income from an active business or in its income from a business other than an active business;
>
> For the 2009 to 2010 taxations years
>
> income from property of a foreign affiliate of a taxpayer for a taxation year includes the foreign affiliate's income for the taxation year from an investment business and the foreign affiliate's income for the taxation year from an adventure or concern in the nature of trade, but does not include
>
> (*a*) the foreign affiliate's income for the taxation year from a business that is deemed by subsection (2) to be a business other than an active business of the foreign affiliate, or
>
> (*b*) the foreign affiliate's income for the taxation year that pertains to or is incident to
>
> (i) an active business of the foreign affiliate, or
>
> (ii) a non-qualifying business of the foreign affiliate;

[196] I note at this point that the deeming of income to be income from other than an active business for purposes of this case is found in subparagraph 95 (2)(*b*) of the *Act*. The Parties agree that clause 95 (2)(*b*)(i)(B) applies for the 2003 to 2010 taxation years of GBL. It reads in part:

> For the purposes of this subdivision
>
> …
>
> (*b*) the provision, by a foreign affiliate of a taxpayer, of services or of an undertaking to provide services

> (i) is deemed to be a separate business, other than an active business, carried on by the affiliate, and any income from that business or that pertains to or is incident to that business is deemed to be income from a business other than an active business, to the extent that the amounts paid or payable in consideration for those services or for the undertaking to provide services
>
> …
>
> (B) are deductible, or can reasonably be considered to relate to an amount that is deductible, in computing the foreign accrual property income of a foreign affiliate of
>
> (I) any taxpayer of whom the affiliate is a foreign affiliate, or
>
> (II) another taxpayer who does not deal at arm's length with
>
> 1 the affiliate, or
>
> 2 any taxpayer of whom the affiliate is a foreign affiliate …

[197] This carve-out addresses the business of managing relating entities assets for a fee, about which I will have more to say later. But, returning to the main thread of the FAPI scheme, income from property includes income from an investment business and excludes income from an active business. Turning to the active business first, income from an active business is defined as:

> Active business of a foreign affiliate of a taxpayer means any business carried on by the foreign affiliate other than
>
> (a) an investment business carried on by the foreign affiliate,
>
> (b) a business that is deemed by subsection (2) to be a business other than an active business carried on by the foreign affiliate, or
>
> (c) a non-qualifying business of the foreign affiliate;

[198] Pursuant to what is referred to as the exempt surplus system, active business income may be distributed to the Canadian shareholder as dividends free of tax (due to the operations of section 90 and paragraphs 113(1)(*a*) of the *Act)*.

[199] Returning to what is caught as FAPI, and specifically "investment business," the preamble to the definition of investment business for 2000 to 2008 reads:

> Investment business of a foreign affiliate of a taxpayer means a business carried on by the foreign affiliate in a taxation year (other than a business deemed by subsection 95(2) to be a business other than active business carried on by the affiliate) the principal purpose of which is to derive income from property (including interest, dividends, rents, royalties or returns or any similar returns or substitutes therefor), income from the insurance or reinsurance of risks, income from the factoring of trade accounts receivable, or profits from the disposition of investment property …
>
> For the 2009 and 2010 taxation years, the preamble reads:
>
> Investment business of a foreign affiliate of a taxpayer means a business carried on by the foreign affiliate in a taxation year (other than a business deemed by subsection 95(2) to be a business other than active business carried on by the affiliate) the principal purpose of which is to derive income from property (including interest, dividends, rents, royalties or returns or any similar returns or substitutes for interest, dividends, rents royalties or returns), income from the insurance or reinsurance of risks, income from the factoring of trade accounts receivable, or profits from the disposition of investment property…

[200] The definition then goes on to exempt certain businesses in the following language:

> … unless it is established by the taxpayer or the foreign affiliate that, throughout the period in the taxation year during which the business was carried on by the foreign affiliate,
>
> (*a*) the business (other than any business conducted principally with persons with whom the affiliate does not deal at arm's length) is
>
> (i) a business carried on by it as a foreign bank, a trust company, a credit union, an insurance corporation or a trader or dealer in securities or commodities, the activities of which are regulated under the laws
>
> (A) of each country in which the business is carried on through a permanent establishment in that country and of the country under whose laws the affiliate is governed and any of exists, was (unless the affiliate was continued in any jurisdiction) formed or organized, or was last continued,

(B) of the country in which the business is principally carried on, or

(C) if the affiliate is related to a non-resident corporation, of the country under whose laws that non-resident corporation is governed and any of exists, was (unless that non-resident corporation was continued in any jurisdiction) formed or organized, or was last continued, if those regulating laws are recognized under the laws of the country in which the business is principally carried on and all of those countries are members of the European Union, or

(ii) the development of real property or immovables for sale, the lending of money, the leasing or licensing of property or the insurance or reinsurance of risks,

(*b*) either

(i) the affiliate (otherwise than as a member of a partnership) carries on the business (the affiliate being, in respect of those times, in that period of the year, that it so carries on the business, referred to in paragraph (c) as the "operator"), or

(ii) the affiliate carries on the business as a qualifying member of a partnership (the partnership being, in respect of those times, in that period of the year, that the affiliate so carries on the business, referred to in paragraph (c) as the "operator"), and

(*c*) the operator employs

(i) more than five employees full time in the active conduct of the business, or

(ii) the equivalent of more than five employees full time in the active conduct of the business taking into consideration only

(A) the services provided by employees of the operator, and

[201] So, the first step is whether the income of GBL for the years in issue is caught by the wording of the preamble to the definition of investment business. On

this there is no debate between the Parties. GBL's business, (other than the separate business pursuant to paragraph 95(2)(*b*) of the *Act*) falls squarely within the preamble in this definition.

(2) Was GBL exempted out of the definition?

(a) Was it a foreign bank?

(i) Pursuant to the definition in subsection 2(a) of the *Bank Act* of Canada.

[202] The financial institution exemption from investment business applies to a foreign bank as defined in subsection 95(1) of the *Act* which in turn refers to the definition of foreign bank found in section 2 of the *Bank Act*:

> Foreign bank, subject to section 12, means an entity incorporated or formed by or under the laws of a country other than Canada that,
>
> (*a*) is a bank according to the laws of any foreign country where it carries on business,…
>
> (*c*) engages directly or indirectly, in the business of providing financial services and employs, to identify or describe its business, a name that includes the word "bank", "banque", "banking" or "bancaire", either alone or in combination with others words, or any word or words in any language other than English or French corresponding generally thereto,

[203] Looking first then at section 2(a) of the *Bank Act* and looking at the definition unencumbered by the preceding parenthetical notion of conducting business principally with non-arm's length persons, the definition is relatively straightforward: the words are unambiguous. Was GBL a bank according to the laws of Barbados? The Appellant's position is simple: an entity is a bank according to the laws of Barbados if it is permitted to use the word "bank" in its name and is regulated as a bank, both conditions clearly met by GBL. The Respondent's position was also simple: an international bank under Barbados law is not a bank under Barbados law.

[204] I have already concluded in my review of the expert evidence that an entity licenced as an offshore bank under OSBA or international bank under *IFSA* is a bank under Barbados law. It remains to be determined if GBL was such an international bank. Certainly it was licenced as such under *IFSA* which would appear to end the matter. The question is really whether the reason that GBL

sought a licence as an international bank has any bearing on its status as an international bank. The Parties concentrated more on this issue in the context of the GAAR analysis. I am inclined to follow suit and leave this analysis to the GAAR stage. Whether GBL sought the licence because it was a legal requirement to do so to conduct the type of activities it conducted or intended to conduct, or because it believed a regulated licenced financial institution would carry more weight in a successful investment strategy program, or because it would avoid Canadian FAPI does not detract from the fact it was a licenced international bank. As such, following my conclusion on the review of the expert evidence, it was a foreign bank as defined under section 2(a) of the *Bank Act*.

> (ii) Was it a foreign bank pursuant to the definition in subsection 2(c) of the *Bank Act* of Canada?

[205] Given my decision with respect to GBL's status pursuant to section 2(a) of the *Bank Act* it is unnecessary for me to review section 2(c) of the *Bank Act*.

> *(b) Was GBL conducting business principally with persons with whom it did not deal at arm's length?*

[206] There are many issues for which the Parties have presented elaborate arguments; frankly, some are more readily resolved than others. From my perspective, this is the key battleground over which the debate on the correctness of the assessments hinges. What is meant by "business conducted principally with persons with whom the affiliate does not deal at arm's length?" The Appellant suggests the Respondent inaccurately and misleadingly paints a picture, in colloquial terms, of Loblaw simply playing with its own money. The Appellant on the other hand portrays GBL as a foreign bank actively conducting business with major third party financial institutions, arguing, in any event, that the test is a negative test – was GBL conducting business principally with persons with whom it <u>does not</u> deal at arm's length. According to the Appellant, it does not have to prove it was conducting business principally with arm's length persons. Little turns on this distinction.

[207] How is this parenthetical term (other than any business conducted principally with persons with whom the affiliate does not deal at arm's length) to be interpreted? As we are all well aware, the accepted modern approach of statutory interpretation, confirmed by the Supreme Court of Canada on more than one occasion, is to consider the text, context and purpose of the provision that is harmonious with the *Act* as a whole.

[208] Textually, the key words "business," "conduct," and "principally" taken alone could support several interpretations, but taken together in their application to a banking business can narrow the meaning considerably. Neither side explored exhaustively the meaning of the words themselves. The Respondent relied on a competitive purpose to cast the words as requiring that GBL had to be in competition for customers to meet this requirement. The Respondent disagrees.

[209] There are two basic elements to a banking business: the receipt of funds and the use of funds. This is certainly recognized in the *IFSA* which defines international banking business as the business of receiving foreign funds and the business of using the foreign funds (see paragraph 153).

[210] Presumably, Canadian legislators recognized what a foreign bank does, and in requiring the conduct of business not to be principally with non-arm's length persons, the text suggests that both aspects of the business were contemplated. The receipt of funds is the side of the conduct of business that implies a measure of competitiveness. Banks seek money whether locally or internationally from customers. What they do with that money involves less competition, though if the bank uses its money to make loans it may compete for borrowers.

[211] Then the words "principally with non-arm's length persons" are added into the equation. What did the legislators have in mind as to how foreign banks could conduct business, in effect with the related parties, that would put the bank offside the exemption? Again, looking at the two sides of banking business, the words alone would suggest the bank must not principally have related customers and must not principally invest in related persons. The words themselves do not provide any guidance on what basis "principally" is to be determined, though there is some agreement it means greater than 50%: but 50% of what? It could be on a time spent basis, on a money engaged basis, on the basis of the number of entities with whom the bank is conducting business or on some combination thereof, infused with a good dose of common sense. Choosing the determinant could yield widely differing results.

[212] The Respondent suggests that the wording means that a bank cannot just play with its own money, yet that does not fully address the totality of a banking business. Had the legislators wanted to make competition for customers the key ingredient, the Appellant suggests they could have used wording similar to the wording employed in subsection 95(2.4) of the *Act*. So, let us look at context.

[213] Subsection 95(2.4) of the *Act* needs to be read together with paragraph 95(2)(*a.3*). These provisions read as follows:

> 95(2)(*a.3*) in computing the income from a business other than an active business for a taxation year of a foreign affiliate of a taxpayer there shall be included the income of the affiliate for the year derived directly or indirectly from indebtedness and lease obligations (which, for the purposes of this paragraph, includes the income of the affiliate for the year from the purchase and sale of indebtedness and lease obligations on its own account, but does not include excluded income)
>
> (i) of persons resident in Canada, or
>
> (ii) in respect of businesses carried on in Canada
>
> unless more than 90% of the gross revenue of the affiliate derived directly or indirectly from indebtedness and lease obligations (other than excluded revenue or revenue that is not included in computing the income from a business other than an active business of the affiliate under this paragraph because of subsection (2.31)) was derived directly or indirectly from indebtedness and lease obligations of non-resident persons with whom the affiliate deals at arm's length and, where this paragraph applies to include income of the affiliate for the year in the income of the affiliate from a business other than an active business,
>
> (iii) those activities carried out to earn such income shall be deemed to be a separate business, other than an active business, carried on by the affiliate, and
>
> (iv) any income of the affiliate that pertains to or is incident to that business shall be deemed to be income from a business other than an active business;
>
> 95(2.4) Paragraph 95(2)(*a.3*) does not apply to a foreign affiliate of a taxpayer in respect of its income derived directly or indirectly from indebtedness to the extent that
>
> (*a*) the income is derived by the affiliate in the course of a business conducted principally with persons with whom the affiliate deals at arm's length carried on by it as a foreign bank, a trust company, a credit union, an insurance corporation or a trader or dealer in securities or commodities, the activities of which are regulated under the laws
>
> (i) of the country under whose laws the affiliate is governed and any of exists, was (unless the affiliate was continued in any jurisdiction) formed or organized, or was last continued and of each country in which the business is carried on through a permanent establishment in that country,

(ii) of the country in which the business is principally carried on, or

(iii) if the affiliate is related to a corporation, of the country under the laws of which that related corporation is governed and any of exists, was (unless that related corporation was continued in any jurisdiction) formed or organized, or was last continued, if those regulating laws are recognized under the laws of the country in which the business is principally carried on and all of those countries are members of the European Union, and

(*b*) the income is derived by the affiliate from trading or dealing in the indebtedness (which, for this purpose, consists of income from the actual trading or dealing in the indebtedness and interest earned by the affiliate during a short term holding period on indebtedness acquired by it for the purpose of the trading or dealing) with persons (in this subsection referred to as "regular customers") with whom it deals at arm's length who were resident in a country other than Canada in which it and any competitor (which is resident in the country in which the affiliate is regulated in the country under whose laws the affiliate was formed or continued and exists and is governed and in which its business is principally carried on) compete and have a substantial market presence,

and, for the purpose of this subsection, an acquisition of indebtedness from the taxpayer shall be deemed to be part of the trading or dealing in indebtedness described in paragraph (b) where the indebtedness is acquired by the affiliate and sold to regular customers and the terms and conditions of the acquisition and the sale are substantially the same as the terms and conditions of similar acquisitions and sales made by the affiliate in transactions with persons with whom it deals at arm's length.

[214] These provisions bring into FAPI income of a foreign affiliate derived from indebtedness or lease obligations of Canadian residents, but exempting income if certain conditions are met. Two of those conditions are with respect to a market presence in the country and the requirement that the affiliate deal at arm's length with a resident of the foreign country that carries on a regulated business that competes with the affiliate in the foreign country. The language goes further than "conducting business principally with non-arm's length persons." Had the government wanted to be more explicit in the foreign bank exemption, it could have written similar language. One conclusion is that the broader language was intended to be just that – broader in its application, covering not just the requirement to be competitive but recognizing there is more to banking than

competing for customers. In effect, there must be a weighing of all aspects of the banking business. It is noteworthy the requirement relates to whether the affiliate deals at arm's length with the competitor, it being implicit the affiliate must be competing. I see the use of the language in these provisions addresses a specific situation, requiring more explicit detail, which is, I would suggest, unnecessary in the financial institution exemption.

[215] Initially, the 1994 amendments included in the "investment business" definition activities of a corporation the principal purpose of which was trading or dealing in debt obligations on its account or on the account of related parties, but this created difficulties for Canadian banks with foreign subsidiaries so a new rule was introduced:

> 95(2)(l) in computing the income from property for a taxation year of a foreign affiliate of a taxpayer there shall be included the income of the affiliate for the year from a business (other than an investment business of the affiliate) the principal purpose of which is to derive income from trading or dealing in indebtedness (which for the purpose of this paragraph includes the earning of interest on indebtedness) other than
>
> (i) indebtedness owing by persons with whom the affiliate deals at arm's length who are resident in the country in which the affiliate was formed or continued and exists and is governed and in which the business is principally carried on, or
>
> (ii) trade accounts receivable owing by persons with whom the affiliate deals at arm's length,
>
> unless
>
> (iii) the business is carried on by the affiliate as a foreign bank, a trust company, a credit union, an insurance corporation or a trader or dealer in securities or commodities, the activities of which are regulated under the laws
>
> (A) of each country in which the business is carried on through a permanent establishment in that country and of the country under whose laws the affiliate is governed and any of exists, was (unless the affiliate was continued in any jurisdiction) formed or organized, or was last continued,
>
> (B) of the country in which the business is principally carried on, or

(C) if the affiliate is related to a non-resident corporation, of the country under whose laws that non-resident corporation is governed and any of exists, was (unless that non-resident corporation was continued in any jurisdiction) formed or organized, or was last continued, if those regulating laws are recognized under the laws of the country in which the business is principally carried on and all of those countries are members of the European Union, and

(iv) the taxpayer is

(A) a bank, a trust company, a credit union, an insurance corporation or a trader or dealer in securities or commodities resident in Canada, the business activities of which are subject by law to the supervision of a regulating authority such as the Superintendent of Financial Institutions or a similar authority of a province,

(B) a subsidiary wholly-owned corporation of a corporation described in clause (A),

(C) a corporation of which a corporation described in clause (A) is a subsidiary wholly-owned corporation;

[216] So, if a foreign affiliate's income was exempted out by the operation of the financial institution exemption in the definition of "investment business," it may still have to clear the hurdle of paragraph 95(2)(*l*) of the *Act*, if determined its principal purpose was trading in indebtedness. This effectively allows only foreign affiliates of regulated Canadian financial institutions to trade in indebtedness without attracting the FAPI rules. And, because in this case Loblaw Financial is the sole shareholder of PC Bank, clause 95(2)(*l*)(iv)(C) of the *Act* kicks in to relieve Loblaw Financial from the application of this provision. This may have greater implications in the GAAR analysis, but from a contextual perspective it confirms it is not enough to be a regulated foreign bank, further conditions must be met. In paragraph 95(2)(*l*) of the Act, the further condition is the connection to a Canadian regulated bank. This condition does not replace the condition of not conducting business principally with non-arm's length persons: it must mean something different.

[217] Turning, finally, to a purposive approach, why is this non-arm's length provision included to deny a foreign affiliate from taking advantage of the

regulated financial institution exemption? To be clear, at this stage, the search is to interpret the words the drafters have used. The Supreme Court of Canada has indicated in *Copthorne Holdings Ltd v R*[5] that a similar search is necessary to get to the underlying rationale in a GAAR analysis:

> The object, spirit or purpose can be identified by applying the same interpretive approach employed by this Court in all questions of statutory interpretation—a "unified textual, contextual and purposive approach" (Trustco, at para. 47; Lipson v. R., 2009 SCC 1, [2009] 1 S.C.R. 3 (S.C.C.), at para. 26). While the approach is the same as in all statutory interpretation, the analysis seeks to determine a different aspect of the statute than in other cases. In a traditional statutory interpretation approach the court applies the textual, contextual and purposive analysis to determine what the words of the statute mean. In a GAAR analysis the textual, contextual and purposive analysis is employed to determine the object, spirit or purpose of a provision. Here the meaning of the words of the statute may be clear enough. The search is for the rationale that underlies the words that may not be captured by the bare meaning of the words themselves. However, determining the rationale of the relevant provisions of the Act should not be conflated with a value judgment of what is right or wrong nor with theories about what tax law ought to be or ought to do.

[218] So, the Supreme Court of Canada guides us to conduct the same textual, contextual and purposive analysis from two different perspectives: one to get to the meaning of words and the other to get to the underlying rationale. This suggests to me that a purposive search for meaning of words may indeed lead to a different result than a purposive search for an underlying rationale. Does this mean that the latter may override the words while the former should not; that is, that the purpose is constrained by text on the statutory interpretation search, whereas it is not so constrained on the underlying rationale search. It strikes me this is something of a fine, legalistic point.

[219] Although the concept of investment business was first raised in the 1994 federal budget, it is useful to go further back in time to the introduction of the FAPI rules generally in grappling with the purpose behind this provision. In 1969, finance minister Benson introduced a "White Paper" [6] which included a tax to be levied on income that "may easily be diverted" to a controlled non-resident subsidiary while retaining the dividend exemption for those subsidiaries resident in a country with a tax treaty with Canada. Some observers commented this was the

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5 2011 SCC 63.

6 E.J. Benson, Minister of Finance, Proposals for Tax reform (Ottawa: Queen's printer, 1969) at para 6.20 and 6.21 ("White Paper").

genesis of the foreign affiliate regime. These same authors also talk about the notions of capital export neutrality, capital import neutrality and competitiveness as underlying the design of any tax system provisions affecting the taxation of income from foreign direct investment.[7] In the same article, the authors explain that capital import neutrality provides that a parent country not impose additional tax on the foreign subsidiaries' income earned in the source country, thus facilitating competitiveness for foreign subsidiaries in the source country market, as all foreigners would presumably be taxed at the same rate. On the other side, capital export neutrality attempts to curtail the effect of differing tax rates in the different jurisdictions by ensuring the source country income is subject to the same rate as domestic income. This can done by taxing the foreign subsidiary's source country income in the parent's hands on an accrual/current basis, providing foreign tax credits to the affiliate for foreign taxes paid.

[220] How did the White Paper stickhandle these competing neutralities? By concluding that international competitiveness favoured capital import neutrality, retaining the dividend exemption to "permit Canadian corporations to compete abroad without being at a fiscal disadvantage vis-à-vis their competitors, including competing subsidiaries of European corporations."[8] The White Paper recognized the need to support Canadians' ability to compete:

> 6.9 On the other hand, Canadian business is often required to go abroad to seek foreign sources of supply and to develop foreign markets. Going international is frequently necessary to enable Canadian companies to achieve the economies of scale which are otherwise denied them by the relatively small size of the Canadian domestic market. Such companies would find it hard to compete on the international scene if they were subject to more onerous taxes than those which apply to their competitors. …

[221] It still, however, recognized possible abuses:

> 6.20 As noted above, the exemption privilege is susceptible to abuse. Not all foreign corporations carry on bona fide business operations. Some are merely devices of convenience to which income from other sources – dividends, interest, royalties and trans-shipment profits – may easily be diverted. The dividend

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7 J. Scott Wilkie, Robert Raizenne, Heather Kerr and Angelo Nikolakakis. "The Foreign Affiliate System in View and Review" in *Tax Planning for Canada-US and International Transactions* (Toronto: Canadian Tax Foundation, 1994) at 27. See also Sandra Slaats and Penny Woolford, "The Evolution of the International Tax Rules" (2010) 58 (sup.) *Canadian Tax Journal* 225-242 at 228.

8 White paper at para 6.16.

> exemption system would permit such income to be brought back to Canada tax-free. Even the tax-credit system would permit the Canadian tax on such income to be postponed indefinitely.
>
> 6.21 To counter this type of tax-haven abuse, the United States now provides that when such income is channelled to a controlled foreign corporation, the U.S. controlling shareholders shall be taxed on a current basis whether or not the income is distributed to the, U.S. taxes are levied in the year in which the profits are earned rather than postponed until the profits are returned home. The government proposes to introduce provisions patterned generally on those in the United States. This proposal involves complicated and difficult law, but he problem is serious and defies easy solution.

[222] The Canadian Bankers Association had concerns with respect to the White Paper and made submissions to the Government in May 1970 suggesting that in the statutory definition of "passive income" a distinction be drawn between financial institutions and investors. It too stressed the need for Canadians, banks specifically, to be able to compete internationally:

> 54. In developing their international business, the banks have been alert to the growing desire in many countries for some form of location participation. Under the White Paper proposals, planning for the establishment or expansion of local subsidiaries in the present non-treaty countries would become more difficult. Furthermore, in low tax jurisdictions the advantages could be denied to a Canadian bank, whereas a competitor from another country might well continue to profit from them. In fact the White Paper provisions would effectively negate any local tax incentives if a treaty were not eventually negotiates. In our view, the cumulative effect of the proposals, if passed unchanged, would be to place Canada in a non-competitive position compared with other countries.[9]

[223] The FAPI legislation was tabled in June 1971, though not coming into force until a few years later, which, according to the Respondent, subjected Canadian taxpayers to current/accrual basis taxation on FAPI earned by foreign affiliates, retaining the dividend exemption in a restricted form.

[224] In November 1974, John Turner re-tabled revised FAPI legislation, first introduced in an earlier May budget, that defined FAPI to include income from property, businesses other than active businesses and taxable capital gains from disposition of property not used for the purpose of gaining or producing active business income. Mr. Turner stated in his May budget speech:

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[9] Canada, Parliament, House of Commons, Standing Committee on Finance, Trade and Economic Affairs, *Minutes of the Proceedings and Evidence*, 28th Parl, 2d Sess, No 58 (9 June 1970) at 67:170.

> … [T]he passive income rules … were introduced as part of tax reform in 1971 to protect against the diversion of income that would otherwise be taxable in Canada.
>
> … The proposed changes improve our protection against the improper use of tax havens to avoid Canadian tax on passive investment income and income diverted from Canada. At the same time, the changes remove from the scope of these rules the income Canadians derive from their active business operations abroad. In addition, the rules will apply onto to those offshore corporations and trusts that are controlled by Canadian taxpayers, and not, as at present, where there may simply be some equity interest. Canada's fiscal climate must remain hospitable to the Canadian company that competes internationally with the large multinational companies of other countries. The changes proposed in this area of law are designed to ensure that this principle is not compromised.[10]

[225] Fast forward several years to the Auditor General's 1992 Report which expressed concerns with existing legislation regarding foreign affiliates:

> A key concern is the fact that the *Income Tax Act* does not define active or passive income in the context of the FAPI rules…. The meaning of passive income for the FAPI rules may be very narrow.[11]

[226] The Department of Finance responded to this Report with some criticism but also reflected on the competing neutralities, as well as the importance of competitiveness:

> Background. Canada has had to struggle with two conflicting goals. The goal of economic efficiency argues for a system which preserves capital export neutrality. This is achieved when foreign source income is subject to the same effective tax rate as domestic source income, leaving taxpayers indifferent, at least from a tax perspective, as to whether they invest inside or outside of Canada. Conversely, the goal of competitiveness argues for capital import neutrality. This requires that a Canadian investing in a foreign country be subject to tax at the same effective rate as a resident of that country. From a tax perspective, this ensures a level playing field between Canadian and non-Canadian businesses operating internationally.
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> In a world where countries maintain different tax systems, it is impossible to achieve both capital import and capital export neutrality. Accordingly, Canada has opted for a system that ensures capital export neutrality with respect to certain types of income and capital import neutrality with respect to other types of

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10 Canada, House of Commons, *Official Report of Debates House of Commons*, 29th Parl, 2nd Session, Vol 2 (6 May 1974) at 2086.

11 Canada, Report of the Auditor General of Canada to the House of Commons (Ottawa: Supply and Services, 1992) at para 2.52.

> income. Specifically, in the case of passive income (i.e., investment income such as interest, dividends and rent) the tax policy concern is that taxpayers will attempt to shelter income in tax haven countries in order to defer the payment of Canadian tax. As a result of this concern, the *Income Tax Act* contains what are commonly referred to as the Foreign Accrual Property Income (FAPI) rules. The FAPI rules are intended to ensure that passive income earned by certain foreign affiliates is accrued and subject to Canadian tax on a current basis (i.e., annually), thereby eliminating the potential for deferral and hence the tax incentive to shift income offshore.
>
> Conversely, in order to preserve the international competitiveness of Canadian businesses, active business income that is earned offshore by a foreign affiliate is not required to be accrued and is subject to tax only in, the foreign jurisdiction. Furthermore, where such income is earned in a "listed country" (basically counties with which Canada has entered into a tax treaty) it may be repatriated (i.e., paid back as a dividend) to Canada on a tax-free basis. The ability to receive dividends from a foreign affiliate on a tax-free basis is intended, at least in part, as a proxy for the foreign tax credit that would have been available to the Canadian company if it had carried on its business through a foreign branch rather than a subsidiary. It also helps to ensure that there is no tax impediment to corporations re-investing their foreign earnings in their Canadian operations….
>
> While the Auditor General has identified a number of concerns with respect to the operation of the foreign affiliate rules, he has failed to indicate that most of these concerns are the result of conscious policy decisions on the part of the government and reflect a desire to promote the goal of international competitiveness. Moreover, he has also overstated the impact of the rules on revenue collection while understating the degree to which any problems have already been addressed by existing legislation. It would not be prudent to implement a system for the taxation of foreign source income which deviates substantially from internal norms and fails to properly address the issue of competitiveness. In this regard, the economic costs inherent in amending the income tax legislation to accommodate the Auditor General's ostensible concerns would far exceed any marginal revenue gains that might be realized thereby.[12]

[227] The Standing Committee on Public Accounts that ran hearings in 1992 and 1993, notwithstanding concerns, recommended:

> The lack of a precise definition is a matter of concern. The Committee wonders how the General Anti-Avoidance Rule can be applied when the term "active income" has never been defined. The Committee considers that something that is implicitly permitted by the Income Tax Act cannot be prohibited. Amending the Act to clarify what is meant by active income would not weaken the rule of taxing

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[12] Respondent's Written Submissions filed on July 4, 2018.

> income from foreign sources, and it would put an end to the tax avoidance schemes that are eroding the Canadian tax base.
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> Contrary to what some witnesses have said, the Committee also considers that the responsibility for finding the right definition should not be left to the courts. It is time to act. Since there is no question of changing the basic structure of the rules, the Committee thinks that definitions can be developed. Even the Department of Finance agrees on the nature of the problem, since it stated: "the essential problem is one of finding out what the definition should be."[13]

[228] This focus by legislators in these years on this difficult area of international taxation does highlight the conflict between competitiveness and abuse, and the need for some definition.

[229] Thus, we come to the February 22, 1994, budget introducing the concept of "investment business." These amendments were passed into law in June 1995.

[230] In announcing the amendments, the Government indicated in Tax Measures: Supplementary Information distributed on February 22, 1994:

> The rules relating to foreign affiliates are complex. They seek to ensure that Canadian companies carrying on business outside Canada through their foreign affiliates are not placed at a disadvantage under the Canadian tax system vis-à-vis multinational companies based in other countries with which they have to compete. On the other hand, the rules also seek to ensure that foreign affiliates cannot be used to shelter passive income, or income that has been diverted from Canada, from Canadian tax.[14]

[231] Again, a recognition of the conflict between competitiveness and sheltering passive income.

[232] As noted by authors Li, Cockfield and Wilkie in International Taxation in Canada:

> The definition of "investment business" was enacted in 1995 after judicial determinations had attributed a very low threshold for the level of "activity" that would allow income, even from indirect Canadian sources, to be treated as "exempt" foreign business income (see *Canada Trustco Mortgage Co. v. Canada (Minister of National Revenue)*, [1991] T.C.J. No. 906, [1991] 2 C.T.C. 2728, 91

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13 Canada, Parliament, House of Commons, Standing Committee on Public Accounts, *Minutes of the Proceedings and Evidence*, 34th Parl, 3d Sess, No 48 (23 April 1993) at 6.

14 Canada, *Tax Measures: Supplementary Information* (Ottawa: Department of Finance, 1994).

> D.T.C. 1312 (T.C.C.)). In keeping with the neutrality principles that apply to distinguish between how genuinely active, and portfolio or passive, income earned indirectly should be taxed, the "investment business" notion ensures that the return from highly mobile capital deployed to earn a competitive return is taxable even if the return is earned in a businesslike fashion. An "investment business" is a business (other than a business that is defined not to be active in the ITA) carried on principally to earn income from property (interest, dividends, rents, royalties or any similar returns or substitutes for them), income from insuring or reinsuring risks, income from factoring trade accounts receivable and profits from the disposition of investment property, itself a defined term.
>
> Nevertheless, certain exceptions apply. The exceptions have three aspects. First, the business must be a business conducted primarily with arm's length persons. Accordingly, in objective terms, the foreign affiliate must be engaged in a degree of competition with foreign enterprises according to circumstances that are external to the corporate group of which the foreign affiliate is a member. Second, the business must be of a particular type: a regulated financial business, a real estate development business, a money lending business, a business of leasing or licensing property, or an insurance business. Finally, in default of a more reliable qualitative way to explain the degree of activity that the foreign affiliate system requires for gaining access to its exemption aspect, directly or indirectly the business must employ more than five full-time employees, either as employees of the affiliate carrying on the business or indirectly through contractual or other means.[15]

[233] Far more has been written by tax academics on this subject than could ever be exhaustively reviewed in these Reasons, but a brief look at the many articles provided to me on this subject suggest the following summaries, along with the summary just provided, first from this Messrs. Panteleo and Wilkie and second from Wilkie, Raizenne, Kerr and Nikolakakis, catch the flavour of the rules:

> The foreign affiliate rules … control the extent to which any deferral is legitimate by distinguishing between investment income, which has no necessary or unique foreign connection that would justify domestic tax concession in deference to a notion of international competitiveness and whose taxation should therefore be guided by the capital export neutrality principle, and business income that qualitatively may and probably does have a local connection in respect of which

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[15] Jinyan Li, Arthur Cockfield and J. Wilkie, International Taxation in Canada: Principles and Practices, 3d ed (Markham: LexisNexis, 2014) at 322-323.

> an emphasis on capital import neutrality, or international competitiveness, would not be misplaced.[16]
>
> Canada, in effect, acknowledges the desirable primacy of a territorial system [i.e., capital import neutrality] for taxing income from foreign direct investment as long as the affected income is generated by activities, generally outside Canada, that are genuinely "productive" in the national economic and commercial contexts in which they occur, in relation to local enterprises. Canada also addresses the need for limits on territorial primacy for highly mobile income whose connections to any particular jurisdiction are tenuous, and in respect of which there are no compelling reasons to cede or defer tax jurisdiction.[17]

[234] While I do not accept that these authors alone provide the determinative word on government policy, there is certainly a consistency against which I have been presented with nothing from the government materials to suggest anything to the contrary.

[235] The Respondent approaches the purposive analysis without distinguishing between analysis for the purposes of statutory interpretation versus the analysis for the purposes of the GAAR search for the underlying rationale. The Respondent simply concludes in her argument on this front that the regulated financial institution exemption reflects a fundamental principle of the foreign affiliate rules: that foreign affiliates should be able to compete internationally with other foreign businesses at the same tax rate. And, further, that it balances the policy objectives at the heart of the foreign affiliate system. In particular, it is intended to apply the capital export neutrality norm (i.e., the FAPI rules) to activities that produce highly mobile income, while facilitating the competitiveness of Canadian-owned financial institutions operating in the international market by applying the capital import neutrality norm. My take on the government's argument is that only if the affiliate is competing for customers in a foreign market with other players in that market is relief from FAPI provided, as only in that circumstance does the relief enhance competitiveness.

[236] Interestingly, the Appellant does not quarrel with the Respondent's view that competitiveness does indeed partly underlie the definition of "investment

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16 Nick Pantaleo and J. Scott Wilkie, "Taxing Foreign Business Income" in Business Tax Reform, 1998 Corporate Management Tax Conference (Toronto: Canadian Tax Foundation, 1998) at 6-7.

17 J. Scott Wilkie, Robert Raizenne, Heather Kerr and Angelo Nikolakakis, "The Foreign Affiliate System in View and Review" in *Tax Planning for Canada-US and International Transactions* (Toronto: Canadian Tax Foundation, 1994) at 4-5.

business," but maintains the purpose is comprehensively captured by the words themselves, especially if you look at the definition as a whole, including the exemption. The Appellant argues that competitiveness is not the sole driver but, according to Appellant's counsel, the Department of Finance put its mind to the competitiveness thesis and determined that "foreign bank," (something already defined by the Government in the *Bank Act*) could readily define the class of people to benefit from the exemption. What the Appellant's approach does not address, however, is the preliminary requirement that the foreign bank not conduct business primarily with non-arm's length persons. We come full circle. The Appellant seems to be suggesting that the purpose was to relieve regulated foreign banks actively carrying on banking business from the grasp of FAPI, I can only presume on the basis such banks would not carry on banking business with non-arm's length persons, or with just one customer. Then along comes Loblaw putting that understanding to question.

[237] Frankly, both Parties slip too readily into the purposive analysis with their GAAR hats on, rather than addressing the statutory interpretation analysis of the financial institution exemption.

[238] I conclude from a textual, contextual and purposive analysis of the provision at issue, and specifically the term "conducting business principally with non-arm's length persons" that it is grounded in an underlying rationale that does indeed focus on competitiveness. At the GAAR analysis stage, I will have no difficulty being convinced that the Respondent's explanation of the underlying rationale is strongly supported by government materials and third party commentary. I am also convinced at this statutory interpretation stage that in looking at both aspects of a foreign bank's business, the receipt of funds and use of funds, there should be emphasis on the receipt side as that is where one would expect to find the competition element but I do not go as far as the Respondent, whose approach appears to focus exclusively on the receipt side of the banking business. It remains to determine whether GBL, in all aspects of the conduct of business, though with an emphasis on its competitiveness, dealt primarily with non-arm's length persons.

[239] Apart from amounts received from Waterman, which never exceeded more than $18 million in a year, compared to assets under management which ranged from $175 million to $1.2 billion, on the receipt of funds side of the equation it all came from non-arm's length parties. Clearly, the conduct of business in that regard was principally, almost exclusively, with non-arm's length persons. There was no competition.

[240] Likewise, the assets under management were again clearly for non-arm's length persons. However, given the application of paragraph 95(2)(*b*) of the *Act*, this business activity can be carved out as a separate business.

[241] In considering the conduct of business from the "use of funds" perspective, it is my view that to overcome the lack of arm's length conduct on the receipt of funds side of the banking business, GBL must demonstrate on the use of funds side that there was little or no conduct of business with non-arm's length persons. It has been unable to do so for the following reasons.

[242] First, with respect to investment in short term debt securities, how is that to be classified? Taking a non-arm's length person's money and buying this type of security could be viewed as conducting business in either respect. Simply buying these investments does not entail any negotiation or active conduct of business. The Appellant suggests that because those investments are with third parties that GBL is conducting business with those persons. This stretches the term considerably. Research done in determining where the best rate can be obtained is, I would suggest, research done on behalf of the person whose money you are investing, which would be the non-arm's length party's. The evidence suggests considerable time was spent in research and meetings establishing the investment strategy for the non-arm's length persons' money, as one witness put it, to make as much money as possible for Mr. Weston.

[243] With respect to the I/O Loan portfolio, the Appellant argues that from 2001 to 2005 thousands of independent operators received loans from GBL, clearly conducting business with arm's length persons, according to the Appellant. Yet, there was no element of competing to get these borrowers. They were effectively handed over to GBL by Loblaw. There was no evidence from either of the employees who managed the loan portfolio as to how much, if any, business was conducted directly with the borrowers. Indeed, GBL was not even paid by the borrowers but through a related company. I find this aspect of the business was conducted as much with Loblaw as with the borrowers.

[244] From 2005 to 2009, GBL received payments from Glendock for managing the portfolio – clearly non-arm's length.

[245] With respect to intercompany loans and equity forwards, the business was conducted with non-arm's length persons.

[246] Turning finally to the swaps activity, the Appellant identifies the major financial institution counterparties as arm's length persons with whom GBL conducted business. The Respondent suggests that because GBL was a customer of these institutions, and had to provide security it was therefore not carrying on business with the dealer who sold the investment. The test is not the carrying on of business but the conduct of business. Did GBL conduct business with these counterparties? Does contracting with a third party constitute the conduct of business? On its face, it does. However, in the context of developing an elaborate investment strategy to make money for Loblaw, I do not consider this swap activity as constituting the principal portion of GBL's overall conduct of business. It is certainly not sufficient to outweigh all the non-arm's length elements of the conduct of business I have identified.

[247] Further, even the swap activity has a considerable element of conducting business with non-arm's length persons, as the swaps were subject to Loblaw derivative policies. Also, the evidence was that certain ISDA agreements could be terminated if GBL was no longer affiliated with Loblaw. So, even considering the swaps as being business not directly conducted with non-arm's length persons (excuse the double negative but the statutory language demands it), Loblaw influence pervades the conduct of business. This is further brought home in spades by the exhaustive regular reporting requirements imposed on GBL by Loblaw as to how GBL was using the funds. Representatives of Loblaw also regularly attended GBL board meetings.

[248] The Appellant has not satisfied me that even the use of funds side of the conduct of banking business was not principally conducting business with non-arm's length persons. When looking at both sides of GBL's banking business, in the context of the need to emphasize the competitive element of the conduct of business, I conclude GBL's business was principally with non-arm's length persons. It therefore does not qualify for the foreign institution exemption.

[249] As I foretold at the outset, this case is a FAPI case. I have determined Loblaw Financial was incorrect in not identifying GBL's income as FAPI. This is sufficient for disposal of the case. However, due to the time and effort spent on the remaining issues, I intend to address them in *obiter*.

(c) Was GBL regulated under the laws of Barbados?

[250] Yes. The Respondent has conceded that GBL was regulated under the laws of Barbados. I need delve into this issue no further, notwithstanding the considerable evidence produced at trial on this matter.

(d) Did GBL employ more than five full time employees or the equivalent thereof in the active conduct of the business?

[251] This requirement is found in paragraph (c) of the definition of "investment business." One might think that this would be a relatively straightforward question that requires simply stepping back and taking a bird's eye view of the employees' work at GBL to reach a practical, comprehensible decision. Not so. Counsel have converted such an analysis into a scientific, statistical endeavour worthy of software algorithms. In reviewing their respective positions outlined in several appendices, I was left with the overriding impression that one can make stats do whatever you want. Appellant's counsel painted the Respondent's methodology as "contrived with a view to slicing and dicing the number of employees," and then responded by slicing and dicing the number of employees. This is perhaps inevitable when addressing the equivalency element of the test, and I too intend to slice and dice.

[252] At the outset, the Respondent concedes there is a basis for GBL meeting the equivalency test in 2000, 2001 and 2002 taxation years. This is due to the carve-out in paragraph 95(2)(*b*) of the *Act*, arising after 2002, of a separate business that would include GBL's managing assets of non-arm's length persons (although there is an issue as to whether all related parties to whom they provided services are caught under this provision – more later). So, I need only address taxations years 2003, 2004, 2005, 2008 and 2010.

[253] Notwithstanding I intend to answer this issue based on the equivalency test, I start by addressing what is meant by full time. The Respondent takes a textual, contextual and purposive approach, concluding:

1. From a textual perspective, full time excludes the concept that employees could work part time in the active conduct of the business, business meaning the investment business of earning certain types of income.

2. Contextually, interpreting full time to mean anything less than full time in the subject business would replicate the equivalency test. Guidance can be found in the interpretation of subsection 125(7) of the *Act* which deals with specified investment business. In the case of *Huntly Investments Limited v*

R,[18] the full time test in subsection 125(7) requires examining whether "employees work normal working hours each day, week and month."

3. From a purposive view, the Respondent notes original section 94 amendments did not include an equivalency test but just the full time test, which was to be applied on a business by business basis. Recognizing employees may be used in separate income earning activities (specifically, a separate business pursuant to subsection 95(2)) the equivalency test was added.

[254] The Respondent concludes that allowing work done by employees in respect of other income earning activities to count towards the full time test would violate the legislative framework: qualifying work of such employees in respect of GBL's investment business should only be addressed or counted under the equivalency test.

[255] The Appellant takes a slightly different view of these tests suggesting they be interpreted in a commercially reasonable manner that taxpayers can understand and apply, relying on an ordinary meaning of the term full time, which would permit of some de minimis work on other matters. Further, the Appellant disagrees that employees in a separate business pursuant to paragraph 95(2)(*b*) of the *Act* are also deemed to be excluded in determining the number of full time employees engaged in active conduct of the business for purposes of the full time test. The Appellant raises three arguments as to why the deeming provision in 95(2)(*b*) does not operate to exclude GBL employees' asset management services to related companies from being considered as engaged in active conduct of the one GBL business:

1. Although the provision by GBL of management services to certain foreign affiliates is deemed under paragraph 95(2)(*b*) to be a separate business other than an active business, it is not expressly required they be excluded in determining the number of employees factually engaged in the active conduct of GBL's business. Deeming provisions, as indicated by the Federal Court of Appeal in the *Survivance v R*,[19] "effectively alter reality: its meaning should be limited to what is clearly expressed: a deeming provision cannot otherwise modify the actual situation that obtains."

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[18] 2017 TCC 255 at para 64.

[19] 2006 FCA 129.

2. Most of the asset management activity would have been performed regardless whether GBL was also managing the related affiliates' assets.

3. The incremental time to manage the related affiliates' assets was insignificant.

[256] Turning first to the interplay between the definition of "investment business" and paragraph 95(2)(*b*) of the *Act*, I agree with the Respondent that the words are clear, and the intention was to allocate employees to each business. Paragraph 95(2)(*b*) is express in identifying the asset management service to non-arm's length persons is indeed a separate business. This carve-out is then incorporated into the definition of "investment business" as a specific exclusion. It simply does not fall into the "business" to which the full time and equivalency tests apply.

[257] Does any amount of work by employees for this separate business disqualify them from being considered full time in the active conduct of the remaining business? The Appellant says no: this is what the Appellant is getting at in suggesting the work would have been done in any event and that any incremental work by employees is so insignificant that even if excepted out does not alter their full time status. The Respondent argues that the work done by the employees on the paragraph 95(2)(*b*) business is such that it does disqualify those employees who worked in this regard from full time status, and their work can only be factored into the equivalency test.

[258] Apart from the paragraph 95(2)(*b*) of the *Act* work, there is a second element that may impact on the full time test, and that is the work for non-arm's length persons such as receptionist duties, financial statement preparation, board meeting preparation, directorships and executive positions held, which I will refer to collectively as the "ancillary work."

[259] I had initially intended to look at the impact these two elements of work have on "full time" on the basis of time spent, examining whether the employees work normal working hours each day, week and month on GBL's investment business. I have, however, concluded that the answer on this employee issue generally rests more with the application of the equivalency test, without having to concoct any sort of bright line test as to what is de minimis work in determining full time.

[260] I agree with the Appellant that there must be a reasonable commercial approach. And, given that full time equivalency is a test by its nature involving

time, it is time that I turn to in determining the equivalency. Employees did not log their time so this makes analysis somewhat rough, but there was sufficient evidence from several employees to draw certain general conclusions, without the need for the detailed statistical analysis provided by counsel.

[261] As already indicated, given the concession for the 2001 and 2002 taxation years by the Respondent, it remains to simply address 2003, 2004, 2005, 2008 and 2010. In those years, there were 11, 12, 10, 11 and 9 employees employed by GBL throughout the year. For GBL to qualify, I need to find that the equivalent of just over half of these employees were engaged in the active conduct of GBL's investment business. Based on the evidence, this is not an onerous hurdle to overcome.

[262] A review of the evidence of the employees' work in those years leads me to the following conclusions.

[263] First, with respect to the ancillary work, such work was provided by many of the employees, but the volume of such work paled in comparison to work performed by them for GBL on its own activities. Receptionist duties and serving as a director or in a titular executive role with little responsibility attached to it involved little time. Preparation of materials for annual meetings or annual financial statements for related companies was not an ongoing daily activity but more of an one-off type of activity. Payroll support for GRCL was limited to one employee (Ms. Cummins). Occasional assistance with wire transfers or routine banking matters to those companies who shared space was sporadic. There was no evidence from any of the employees who testified that any significant time was spent on the ancillary work. Indeed, overall, I took from the evidence that the regular day-to-day work involved very little ancillary work.

[264] By way of another example, the Respondent raised the fact that the receptionist would have to cover for the related entities who shared space, yet the evidence was there was little to no traffic in that regard. So, presuming yearly hours of an employee were between 1500 and 1800, allowing even 5% for such work, or 75 to 90 hours of an employee's time would be a generous allocation.

[265] Another example raised by the Respondent is the work done by the employees, primarily Mr. Berry, for GGMI in dealing with Waterman and Moidart. Mr. Berry, however, testified that GGMI was intended simply to be a marketing tool for GBL but never really took off. Again, the evidence suggests an

insignificant percentage of time spent on that. In any event, it was dissolved in early 2003 so what little work was involved relates only to that one year.

[266] Next, with respect to the management of portfolios (GBL's own versus those for related entities), the Respondent argues that it takes an appropriate evidence based approach to divide up the workers taking into account the following:

> a. the portfolio management work done by employees on the Investment Desk was done on a per portfolio basis. They would verify that each separate portfolio was in compliance with its SIPG, conduct research that benefited all the portfolios, and buy specific securities for each individual portfolio;
>
> b. the portfolio management work done by employees in the Back Office was to process and settle the individual trades for each individual portfolio; and
>
> c. if securities were bought as a "block" they would have to be sub-allocated between the different portfolios and each individual purchase for each portfolio would have its own trade ticket. The difference in term of time spent in such a black traded related to dealing with the individual trade tickets.[20]

The Respondent then goes on to argue:

> 394. As such, the respondent proposes to divide the time spent managing portfolios by considering the number of individual trade tickets generated as a result of these activities.
>
> 395. This can be calculated, on a per portfolio basis, by counting the individual securities held in each individual portfolio as each of those would have had its own unique trade ticket prepared when the security was purchased.[21]

[267] I weigh this approach against the Appellant's view that this contrived calculation ignores two factors. First, most of the work on the investment side was necessary to manage GBL's portfolio in any event, and second, the revenue generated by the asset management fees was a small fraction of the revenue derived from GBL's portfolio. I would add that the Appellant's approach does not weigh time differently between the front office and back office.

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[20] See Evidence: Bayley, pp. 1742 and 1743

[21] See Evidence: Bayley, pp. 1738 and 1739

[268] On balance, I conclude there is a commercial view that, while lacking the science perhaps of the Respondent's approach, accords with commercial realities based on the employees' evidence as to how they and their colleagues indeed spent their time generally. On this basis, I distribute time as follows:

1. For Mr. Berry, in all five years (2003, 2004, 2005, 2008 and 2010), taking into account his overall managerial responsibilities, I find that time on the investment side for related entities plus his ancillary work, accounted for approximately 40%, leaving 60% on GBL business.

2. For Ms. Patel, in all five years, taking into account her primary responsibility for swaps, I find time on the investment side for related entities plus ancillary work accounted for less than 10%, leaving 90% of her time on GBL business.

3. For Ms. Taylor and Ms. Medford, for 2003, 2004, 2005 and 2008 years, I find very little was on anything other than the I/O Loans – less than 10% each leaving 90% on GBL business.

4. For Ms. Blackman and Ms. Holder, in all five years, they both served in general administrative capacities for GBL, though Ms. Blackman also provided some minimal ancillary work (financial statements for Glenhuron Holdings) and had some involvement on the accounting side. I would attribute 95% of Ms. Holder's time to GBL business and 90% of Ms. Blackman's time to GBL business.

[269] Just on the basis of these six employees alone, I readily find GBL meets the equivalency test of greater than five full time employees for the first four of the five years in issue. And it still leaves, for all five years, consideration of Ms. Rogers, working on the investment side, to which I attribute 50% to GBL alone; Mr. Welch, in charge of the accounting side focused primarily, if not entirely, on GBL business, to which I attribute 90% to GBL; and Mr. Mason, working in both the front office and back office in different years to which I attribute 50% of his time in the investment years to GBL and 90% in his accounting years to GBL. This adequately covers the 2010 taxation year. These results do not even factor in the remaining employees, Mr. Drayton, Ms. Robinson, Ms. McKenzie, Mr. Bayley and Mr. Whittaker, who worked at different times during the five years at issue.

[270] I find commercial support in this conclusion, based on my estimate of time spent by employees, by also looking at revenues derived from GBL's business compared to revenues arising from the other sources, being primarily the fees from the management of related entities' assets. The latter represent a very small percentage of the former. The overall impression is that employees were dedicated to making money from GBL's portfolio in an elaborate investment strategy. GBL has met the equivalent to five full time employees test.

C. If Loblaw Financial received FAPI from GBL has it been correctly calculated?

[271] There are two relatively minor issues to address in the determination of the correct calculation of FAPI:

(1) Were the foreign exchange gains/losses arising on GBL's investments in short term securities on income or capital account?

(2) Whether the inclusion in FAPI pursuant to paragraph 95(2)(*b*) of the *Act* which deems the management of non-arm's length parties assets to be a separate business other than an active business includes fees from the Disputed Entities?

(1) Foreign exchange gains/losses – income or capital account

[272] The Respondent concluded that some or all of GBL's foreign gains/losses on the investment in short term securities was on account of capital, as the securities were not held as inventory. The Appellant argues that such gains/losses were incurred in the course of carrying on an active business and therefore are on income account.

[273] To calculate the amount of FAPI paragraph 95(2)(*f*) of the *Act* deems a foreign affiliate to be resident in Canada and required to determine capital gains or losses using Canadian currency. The Respondent maintains the short term securities were held to earn income from property and not as inventory of an active business, pointing out the vast majority were held to maturity.

[274] The Respondent's argument centers on the definition of "inventory," concluding that the short term securities are not captured by subsection 248(1) of the *Act* definition, which describes inventory as property the cost or value of which is relevant in computing income from a business. This emphasis is misplaced and does not take into account the active nature of GBL's business. Yes, it is an

investment business for the FAPI determination, but its purpose was to derive income from carrying out an elaborate investment strategy in which the income from the short term securities was used to fund the derivative program.

[275] In *CCLI (1994) Inc v R*,[22] the Federal Court of Appeal set out the basis upon which foreign gains/losses are to be characterized:

> 13. For income tax purposes, the classification of a foreign exchange gain or loss as income or capital depends on the nature of the transaction in relation to which the gain or loss occurred. In this case, the transactions are the loans from Citibank Canada to CCLI. The question is whether, to CCLI, those loans are capital transactions or income transactions.

[276] The acquisition of the short term securities, taking their yield and funding a derivatives program to produce a greater yield is, I would respectfully suggest, using these short term securities in a manner akin to inventory in an income producing scheme. The Appellant cited to me the following passage from the Supreme Court of Canada in *Sutton Lumber & Trading Co. v Minister of National Revenue*:[23]

> 33. In Commissioner of Taxes v. The Melbourne Trust Limited 7, Lord Dunedin, in delivering the judgment of the Judicial Committee, quoted with approval the following passage from the judgment in California Copper Syndicate v. Harris 8:
>
> > It is quite a well settled principle in dealing with questions of income tax that where the owner of an ordinary investment chooses to realize it, and obtains a greater price for it than he originally acquired it at, the enhanced price is not profit in the sense of Schedule D of the Income Tax Act of 1842 assessable to income tax. But it is equally well established that enhanced values obtained from realization or conversion of securities may be so assessable where what is done is not merely a realization or change of investment, but an act done in what is truly the carrying on, or carrying out, of a business.

[277] This captures the essence of what GBL was doing. I find the foreign exchange gains/losses associate more closely with this income activity than with a traditional view that such short term securities are capital, passing that classification on to the foreign exchange gains/losses attaching to them.

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22 2007 FCA 185.

23 [1953] 2 SCR 77.

(2) Paragraph 95(2)(*b*) of the *Act*

[278] The Appellant conceded that paragraph 95(2)(*b*) of the *Act* does apply to the management fees derived from managing the assets of non-arm's length persons, but disputed this application to the fees in connection with the Disputed Entities. The amount of income in dispute from the Disputed Entities is insignificant in the scheme of things, being approximately $220,000 over the years in issue. This issue strikes me as moot at this point, as if I find the Disputed Entities' fees are not caught under paragraph 95(2)(*b*) of the *Act*, then they would simply fall into GBL's business, which I have found is an investment business and subject to FAPI inclusion.

D. If GBL was not carrying on an investment business, is Loblaw Financial caught by the application of the GAAR?

Again, to be clear, the following is *obiter* as I do not need to decide the GAAR issue.

(1) Do the waivers for the taxation years 2001 to 2005 preclude the Respondent from relying on the GAAR for those years.

[279] The Minister may assess beyond the normal reassessment period if the taxpayer has filed a waiver (subparagraph 152(4)(*a*)(ii) of the *Act*). Subsection 152(4.01) then goes on to provide:

> (4.01) Notwithstanding subsections (4) and (5), an assessment, reassessment or additional assessment to which paragraph (4)(a), (b), (b.1), (b.3) or (c) applies in respect of a taxpayer for a taxation year may be made after the taxpayer's normal reassessment period in respect of the year to the extent that, but only to the extent that, it can reasonably be regarded as relating to,
>
> (*a*) where paragraph 152(4)(a) applies to the assessment, reassessment or additional assessment, …
>
> (ii) a matter specified in a waiver filed with the Minister in respect of the year;

[280] I am satisfied that neither Loblaw Financial nor the CRA had GAAR in mind when the 2001-2005 waivers were prepared by the CRA and signed by officers of Loblaw Financial. Those waivers made no specific mention of GAAR,

but referred only to the inclusion of FAPI of GBL and a deduction in respect of foreign taxes (the first two years specifically identifying subsections 91(1) and 91(4) of the *Act*). The waivers with respect to the 2005 taxation year added reference to a deduction under section 113 of the *Act*.

[281] It was not until August 1, 2012 that Loblaw Financial was given any indication that the CRA's ongoing review that commenced in 2005 was considering anything other than the technical application of the FAPI regime, as this letter, for the first time, mentioned the matter had been referred to Aggressive Tax Planning. Indeed, in June 2011, the CRA confirmed that for the 2001 to 2006 taxation years, GBL's income was FAPI, with no suggestion this arose due to the application of GAAR.

[282] The key determination is whether or not the GAAR assessment can reasonably be regarded as relating to these matters specified in the first five years' waivers. It is certainly not lost on me that the CRA only added GAAR wording for the 2007 and subsequent years on the recommendation of Aggressive Tax Planning, first received in August 2012. Clearly, CRA had a concern as to the breadth of the prior waivers and with adding reference to GAAR presumably removed any doubt.

[283] In *Honeywell Ltd. v R*,[24] Chief Justice Bowman said the following:

> 21. …
>
> (*c*) I do not interpret the words "matter specified in an election" ("question précisée dans une renonciation") as meaning simply an amount of money, nor do I read the waiver as saying "anything arising generally out of your relations with your subsidiary Honeywell NV". Some effect must be given to the words "reasonably" and "to the extent that but only to the extent that..." I think a "matter" in subsection 152(4.01) means a separate subject matter or a discrete head of taxation. An obvious example would be where a taxpayer signed a waiver specifying that the Minister could reassess to treat a disposition of property as being on revenue as opposed to capital account. Could the Minister then, after assessing in the manner specified in the waiver, argue that the net amount of tax assessed could be justified on the basis that even if the disposition was on capital account the taxpayer had claimed expenses in an unrelated matter that were not allowable? I think

[24] 2006 TCC 325, *aff'd* 2007 FCA 22.

> not. The matters are different. By the same token, I think a GAAR recharacterization of a foreign affiliate's income as interest received by a parent is a fundamentally different subject matter or head of taxation, and therefore a different matter, from a FAPI assessment.

[284] The Federal Court of Appeal upheld Chief Justice Bowman's decision, describing a waiver as follows:

> 32. A waiver when given by a taxpayer and accepted by the Minister gives rise to a bargain of sorts. The taxpayer foregoes the benefit of the normal assessment period for the particular year with respect to the matter specified in the waiver, and the Minister, relying on the waiver, acquires the right to reassess outside the normal assessment period, but only with respect to the matter specified in the waiver. Just as the taxpayer cannot alter the waiver once given, the Minister cannot issue a reassessment that does not reasonably relate to the matter specified in the waiver. As pointed out by Bowman C.J., this is made clear by the language of subparagraph 152(4.01)(a)(ii) which provides that when relying on a waiver the Minister may reassess, "but only to the extent that, [the reassessment] can reasonably be regarded as relating to, … a matter specified in a waiver filed with the Minister in respect of the year, …". Accordingly, where a reassessment has been issued pursuant to a waiver, the reference to a "reassessment" in subsection 152(4) can only mean a reassessment as permitted by the waiver.

[285] For an assessment to reasonably relate to a matter in a waiver, it is my view that means it must reasonably relate to the bargain, as Justice Noël put it. There was no bargain between the parties at the time of signing the 2001 to 2005 waivers that related in any way, reasonably or otherwise, to a GAAR application.

[286] To accept the Respondent's position that a GAAR assessment is reasonably related to the technical application of the FAPI rules, or frankly to any technical application of a substantive taxing provision, simply because the assessment of tax would be the same under either approach, means that GAAR would always be subsumed into any and every matter raised in a waiver, without any need to explicitly raise it. I am not prepared to go that far. The GAAR is a powerful tool in the government's toolbox which should only normally be viewed as a separate matter, requiring specific mention in a waiver. There may be circumstances where in an ongoing audit both parties are clearly aware GAAR is on the table, and the bargain reached, evidenced in a waiver, may indeed contemplate GAAR without specific mention. In such rare or limited circumstances a GAAR assessment may reasonably relate to the waiver bargain. That is not the case before me – quite the

opposite. GAAR, not having been on either sides' radar screen, cannot now be imposed as reasonably being regarded as relating to the technical application of FAPI.

[287] I conclude that Aggressive Tax Planning recognized the need to add specific reference to GAAR to ensure the years going forward could be subjected to GAAR. They could not, however, salvage the prior years. I limit consideration of GAAR to 2008 and 2010. This limitation may explain Appellant's counsel's view this case should be viewed as a GAAR case.

(2) Was there a tax benefit?

[288] Before addressing the three elements of a GAAR analysis, tax benefit, avoidance transaction and misuse or abuse of provisions of the *Act*, I have some preliminary observations. Often the GAAR analysis comes down to the third element. This switches the onus over to the Respondent to establish an underlying rationale of the provisions in issue so that the judge can then make a determination as whether they have been misused. On fewer occasions is the answer determined at either the tax benefit or avoidance transaction level. In this case, I find no difficulty in finding a tax benefit or indeed a misuse, but does the misuse arise from an avoidance transaction? Normally, I would not get to the third question if I find there is no avoidance transaction. But in this case, given my analysis of the purpose underlying the wording of the investment business definition, and specifically the non-arm's length proviso, I have had to already review purpose or underlying rationale in the statutory interpretation context. So, I find a somewhat unusual situation where I can conclude a tax benefit has been achieved through the misuse of provisions of the *Act*, yet GAAR may not apply if there has been no avoidance transaction. Though it is a close call, I have not been persuaded that Loblaw Financial entered any of the transactions other than for the principal commercial purpose of making money from an elaborate investment strategy in a low tax jurisdiction.

[289] I do start, however, with the question of whether there has been a tax benefit. The Appellant suggests there can no tax benefit, that is, no reduction, avoidance or deferral of tax, because at no point was any tax payable. The Appellant refutes comparisons by the Respondent to possible alternative arrangements. It is unnecessary to go through these. A tax benefit does not always have to arise by means of comparison to some normative transactions. Loblaw Financial had a controlled foreign affiliate. It filed on the basis the controlled foreign affiliate was not carrying on an investment business, relying on the financial institution

exemption. This was an avoidance of tax on FAPI. It needs be no more complicated than that. There is a tax benefit.

(3) Were there avoidance transactions?

[290] Subsection 245(3) of the *Act* defines avoidance transaction as follows:

> 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.

[291] Keep in mind, had I needed to go down the GAAR path, I would have limited the issue of the application of GAAR to the 2008 and 2010 taxation years. The only transaction in those years that could be considered an avoidance transaction (that is, according to section 245(3) of the *Act*, a transaction resulting in a tax benefit unless it may reasonably be considered to have been undertaken or arranged primarily for *bona fide* purposes other than to obtain the tax benefit), would be the renewal of the *IFSA* licence.

[292] A review of the licence renewal can be undertaken from the perspective of a standalone avoidance transaction or, as the Respondent argues, as part of a series that goes back to the very incorporation of GBL and its initial application for an *OSBA* licence. While I recognize the legislative amendments to FAPI introducing the foreign bank exemption had long been in place by 2008, I am of the view that if the initial licence was sought for a purpose other than to obtain a tax benefit, then subsequent renewals maintaining the *status quo* should be painted with the same brush. So let us go back to 1993 and the initial licence application.

[293] The definition of offshore banking business is found in section 4 of *OSBA* (see paragraph 153 of these Reasons). It is broadly worded. It is hard to dispute that GBL did not receive foreign funds in the manner indicated and used the foreign funds so acquired likewise in the manner indicated. Ms. Jones was clear in her written opinion:

> during the *OSBA* years, the activities of GBL met the criteria for "offshore banking" under section 4 of the *OSBA*. GBL was therefore conducting offshore banking and required a licence in order lawfully do so.

She gave a similar opinion for the *IFSA* years in relation to conducting international banking business.

[294] As previously mentioned, there are two elements to the definition of banking or banking business: the receipt of funds and the use of funds. On the receipt side, after licensing, GBL received foreign funds from short term debt security yields, shareholder capital injections, swaps, the sale of the I/O Loan portfolio and indirectly from the sale of NHI. Ms. Jones opines that these activities fit within the definition of activities under *OSBA* and *IFSA*.

[295] Similarly, Ms. Jones opines GBL used the funds once licensed in a manner described in the legislation as it invested and managed its US dollar portfolio, entered swaps, loaned to an affiliate and provided standby credit.

[296] The Respondent rejects Ms. Jones conclusion on the basis it is overly broad and would mean that every international business company (recall this was GBL's status before being licenced under *OSBA*) would be conducting international banking, rendering *OSBA* and *IFSA* purposeless. The Respondent goes on to argue that obtaining the first licence in late 1993, and the subsequent renewals of the licence, were not primarily for the purpose of enabling GBL to comply with Barbados law, as an international business company licence could achieve the same purpose.

[297] Ms. Jones did also point out that being licensed under *OSBA* or *IFSA* would lend some reassurance to those with whom a licensed international bank would interact that it was dealing with a regulated financial institution.

[298] The factors that suggest the licence was initially sought for tax avoidance purposes are:

- GBL was conducting the same business before the licence as an international business company as after, including the swap business.
- Mr. King advised at the November 12, 1992 first organizational meeting of GBL that the international business company licence would allow for the transaction of international business.

- When Mr. King wrote to the CBB on November 12, 1993 seeking an *OSBA* licence, he referred to "financial activities which they proposed to engage in," and its attached schedule described investment banking activities already engaged in and adding commercial banking activities such as secured mortgage lending that GBL ultimately did not engage in.

- At the November 18, 1993 GBL board meeting, no mention was made that GBL may have been doing business that required a licence.

[299] The Respondent also raises the reference in the GOBV board minutes of November 18, 1993 that "there is no follow up on the Auditor General's Report concerning the loopholes in Canadian tax law with respect to international activities of Canadian multinationals." This, however, can also be viewed as confirming that there is no knowledge of any exact new law with an investment business definition. Mr. Mavrinac was aware that an active business would be necessary but denied acting on any unknown detail of future FAPI legislation.

[300] The factors that suggest the licence was sought for *bona fide* commercial purposes (legally required or otherwise) are:

- Ms. Jones opinion.

- The swaps already entered into by GBL were only in October 1993, just before the board meeting at which Mr. King recommended a licence.

- Mr. Zoetmulder's evidence was that GBL needed a licence.

- Mr. DiFilippo's evidence was the licence made it easier for counterparties to know they were dealing with a regulated institution.

- The November 18, 1993 GBL board meeting minutes indicate:

  > After discussion it was agreed that the nature of the company's actual business was more in keeping with that of a bank.

- CBB did review the application and grant a licence and continued to review and annually renew the licence.

[301] No question the licence was obtained to be an offshore bank and renewed in the years in issue to be an international bank. There is evidence that the Canadian FAPI laws were under review in 1993, but at the time there was no clarity as to what those laws would look like, whether indeed there would be any foreign bank

exemption. While the factors going both ways are, frankly, evenly divided, I conclude the timing of impending but unknown legislative amendments could not have been the reason for seeking the licence in November 1993.

[302] The issue then shifts to whether the licence renewal in 2008 and 2010, after the FAPI amendments were in place, alters the purpose. I would have to conclude that, at renewal time, GBL made a conscious decision to renew for a reason other than why it got the licence in the first place. I have no evidence surrounding the renewals to suggest that. I only know the legislation had changed and I am being asked to therefore presume the reasons for the licence changed. It does not so automatically follow.

[303] If the licence renewal is not an avoidance transaction on its own account, the Respondent argues, relying on subsection 248(10) of the *Act*, and the common law concept of "series," that it is part of a series that constitutes an avoidance transaction. The Respondent describes the series to include steps to create the initial structure, as well as those adapted to the FAPI amendments which would have made its income taxable in Canada, unless it was a regulated foreign bank with more than five employees.

[304] The specific transactions in the series relied upon by the Respondent are:

1. The incorporation of GBL as a treasury centre in 1992.

2. Capitalization by Loblaw Financial and GBOV.

3. The name change, articles of amendment and application for licence in 1993.

4. Licence renewals every year thereafter to and including 2008 and 2010.

5. Hiring three additional employees in 1994.

6. The transfer of US $291 million from NHI to GBL in 2000.

[305] The Respondent did not propose that all the transactions were predetermined in 1992 or 1993, claiming predetermination is only required to establish a common law series, which can then be expanded by the application of subsection 248(10) of the *Act* which reads:

> For the purposes of this Act, where there is a reference to a series of transactions or events, the series shall be deemed to include any related transactions or events completed in contemplation of the series.

[306] The Appellant views this approach as a far too broad reading of subsection 248(10) of the *Act* which would have the unreasonable effect of capturing all transactions over GBL's life simply because they relate to the incorporation and licence, absence any nexus or temporal connection.

[307] To put this avoidance transaction debate in perspective, the Respondent's position is the series' only purpose was to obtain the tax benefit of avoiding FAPI, versus the Appellant's position which is that avoiding FAPI was not a purpose at all. I have concluded that the reality is found between these two opposing viewpoints. Overall, I take from the evidence that the transactions were entered into for three purposes:

1. To make money for Loblaw Financial through an elaborate investment strategy using offshore money.

2. To do so in a low tax jurisdiction with a recognized international financial infrastructure.

3. To avoid FAPI.

[308] I further conclude that the first two objectives were *bona fide* commercial purposes and outweighed the third objective, which I would categorize more as an advantageous fallout from the first two. I do not conclude that it was the driving force behind these transactions, though I also do not accept that it was irrelevant or not a factor. It would belie credulity to suppose a major Canadian organization with its own tax department and dozens of foreign affiliates would not be fully cognizant of the tax implications of FAPI, and being so aware, would not have its avoidance as an objective. Indeed, Mr. Mavrinac testified the business needed to be an active business, yet it was the development of the business that drove this, not FAPI. Also, the fact one objective was to find a low tax jurisdiction does not go to the tax benefit, which relates only to FAPI avoidance. The choice of Barbados due to its low tax regime may have been a tax objective but it was not a tax benefit avoidance objective as contemplated by the GAAR.

[309] Returning to the series, I am guided by the Supreme Court of Canada's approach in *Copthorne*:

> 40. Where, as here, the Minister assumes that the tax benefit resulted from a series of transactions rather than a single transaction, it is necessary to determine if there was a series, which transactions make up the series, and whether the tax benefit resulted from the series. If there is a series that results, directly or indirectly, in a tax benefit, it will be caught by s. 245(3) unless each transaction within the series could "reasonably be considered to have been undertaken or arranged primarily for bona fide purposes other than to obtain [a] tax benefit". If any transaction within the series is not undertaken primarily for a *bona fide* non-tax purpose that transaction will be an avoidance transaction.
>
> 41. The first consideration is whether there was a series that resulted in a tax benefit. As I will explain below, it will be necessary to consider when a transaction which is related to a common law series of transactions is part of a series of transactions as defined in s. 248(10) of the *Income Tax Act*. The second consideration is whether any of the transactions within the purported series is an avoidance transaction.[25]

[310] Looking at this analysis with an eye to 2008 and 2010, the only transaction in those years that the Respondent argues forms part of any series is the licence renewal. So, is it part of a series, and if so, is there any transaction within that series that is an avoidance transaction that taints the series as such?

[311] The Respondent does not argue that the licence renewals were part of the predetermined common law series but rather maintains the licence renewals are captured in the series by the application of subsection 248(10) of the *Act*.

[312] The Supreme Court of Canada had much to say about this provision in *Copthorne*, taking an expansive approach to its interpretation, which did not require any strong nexus to meet the test. In *Copthorne* though the Parties had agreed that there was a series but not on whether the final transaction (redemption of shares), was part of that series. The Supreme Court of Canada also noted that time may be a relevant consideration, as would intervening events.

[313] In 2008 and 2010 the tax benefit (FAPI avoidance) arises because GBL is a controlled foreign affiliate of Loblaw Financial claiming the foreign bank exemption in the definition of "investment business." Notwithstanding this is many years after the incorporation and initial licence, the renewal of the licence was an annual event and did not simply pop-up for the first time 15 years on: it was continual, so I do not see a temporal issue. The licence renewal, on an expansive

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[25] *Supra*, note 5.

approach, can relate to the initial licence and in turn relate to the incorporation. It is not as farfetched as the Appellant supposes.

[314] It is my view that it is not so much whether or not there is a series that focuses the analysis but whether any transaction within the series is an avoidance transaction. I find, while a tax benefit arises from the incorporation, the licencing and the investment of funds into GBL, there were *bona fide* commercial purposes that outweighed the FAPI avoidance purpose at each step.

[315] Examining this further, once I conclude the initial licence is not an avoidance transaction, as I have, I can readily treat the contemporaneous transactions of name change and articles of amendment in the same light. With respect to the incorporation itself, I likewise find that, though on Loblaw's radar, FAPI avoidance simply was not the primary purpose for incorporating GBL, but the other two objectives I have already identified were.

[316] The Respondent emphasized the injection of the $291 million of funds from the NHI sale as having no *bona fide* commercial purpose and was only undertaken to avoid FAPI, as there would have been FAPI but for diverting these funds into GBL. The Respondent also pointed out that there was no evidence that GBL employees sought these funds or required them in their business. This is curious to me, as GBL's business was making money from money: to do so required money. Loblaw Financial was well aware it had this profitable Barbadian financial institution in which funds could be deposited and, yes, it would avoid FAPI. But to follow the Respondent's logic would be to conclude that a business' objective of growth is not a legitimate business objective but that the tax tail alone wags the dog. I just do not buy it.

[317] I further question the Respondent's view, given Mr. Holland was clear that the primary driver was to put the cash that was in the US into GBL for use in its business. He also testified that had the funds been left in the US, the Canadian tax would have been a tenth of the US tax and, in some years, there likely would have been no FAPI reported at all. I accept that Mr. Holland was not an expert, but I do not view this as expert evidence nor do I look on this evidence as putting forth some different US tax purpose that overrides the Respondent's position this was done solely for a FAPI avoidance purpose. I see the evidence simply as supportive of a business decision to put the money in Loblaw Financial's successful moneymaking venture in Barbados. Again, I do not accept the Appellant's view there was no FAPI consideration. It remains my view, however, that this was not the predominant purpose.

[318] The final transaction that I wish to review which the Respondent argues is an avoidance transaction that is part of a series that extends to the licence renewal transactions in 2008 and 2010 is the hiring of three employees in 1994. Mr. King's letter of May 5, 1994 (see paragraph 24) is clear that hiring more employees is motivated by the legislative change requiring "subsidiaries of Canadian companies doing investment business in Barbados to increase employment to more than five persons." The Appellant argues that even if I were to find the hiring of three employees was an avoidance transaction, its impact from a GAAR perspective must be limited to 1994: it is not a continuing attribute, as Mr. Meghji put it, unlike PUC say, which created in year one could still be relevant in year 10 in a GAAR analysis.

[319] The hiring of the three employees, 14 years before the first year in issue, is, according to the Appellant, simply irrelevant to the analysis. Though not saying it directly, I take from these comments the Appellant's position is that the 2008 and 2010 licence renewals are not part of a series that includes the hiring of three employees in 1994. I agree. It is one thing to claim the incorporation of a company has an ongoing role in defining a series to which it might attach, but that is quite distinct from a one-off transaction that has no bearing beyond the year in which it occurred. Put another way, the hiring of three employees in 1994 may well be part of a series that includes the incorporation of GBL but that series ends in 1994. The question of employees in 2008 and 2010 is just not connected to those hirings. Any series that extends to 2008 and 2010 just does not include the 1994 hirings.

[320] I conclude that, on balance, the transactions entered into by Loblaw Financial that the Respondent claims are a series, albeit resulting in a tax benefit, were entered primarily for purposes other than to obtain the tax benefit and consequently were not avoidance transactions.

(4) Was there an abuse of the FAPI provisions, specifically subsection 95(1) of the *Act*?

[321] While there is no need to delve into this question given my finding there were no avoidance transactions, I intend to address it in summary fashion, as it goes to the heart of what the case is all about, albeit from a different perspective than the statutory interpretation of the provisions themselves. To be clear, the guts of this case is not a question of any overriding intention or plan to avoid tax, as the Parties have portrayed it. No, as I have indicated, this is a FAPI case not a GAAR case. I agree with the Respondent that the essential question is "at what point has

Parliament determined that Canada will – and will not – tax foreign source income earned by a Canadian taxpayer through a foreign affiliate?"

[322] I need not repeat my review of a purposive analysis of the financial institution exemption. It is clear the Government, well aware of the need to balance the competing concepts of capital import neutrality and capital export neutrality, chose a course of capturing the business principally earning income from property while exempting income from the financial institution regulated in a foreign country, that competes with other such institutions in international markets. The policy, or underlying rationale, of the exemption is not vague as suggested by the Appellant: it is to promote competition of affiliates operating in international markets. It is not, as the Appellant argues, a complete answer that the Government's identification of "foreign banks," in and of itself reflects a Government policy with no reference to the element of competition. As indicated, this ignores the non-arm's length element of the exemption.

[323] Having concluded the rationale for the financial institution exemption is grounded in "competition," it follows that Loblaw Financial was misusing this exemption as it was not competing in any manner in any international market. It basically managed an investment portfolio for Loblaw. Yes, this took many employees and yes, GBL was regulated as a foreign bank, but look at what it did, and more specifically what it did not do. Loblaw Financial took great umbrage at the Respondent's reference to it as simply playing with its own money. Yet, that is exactly the picture the witnesses have painted for me. The only scintilla of evidence that had GBL vying for business was in obtaining the Waterman contract, but that is minor to the point of insignificance. It was no surprise to hear from Mr. Berry that the so-called marketing arm (GGMI) never amounted to much – there was no need to market. This is not the business the policy was designed to relieve from the application of FAPI – just the opposite. The difference though between the Respondent's approach to this view and mine is that the Respondent infers an intentional overriding avoidance plan and thus casts the term "playing with its own money" in an implicit derogatory manner. I do not read it that way. There is nothing wrong with playing with your own money, even when there is a lot of it, with an objective that one result may be a favourable tax consequence. Where this objective is not the driving force, GAAR should not come into play. I have concluded, however, the objective in this case was misconceived: a difference of interpretation of the financial institution exemption.

[324] I would also like to address the Appellant's position that by seeking to apply the GAAR, the Respondent is inviting me to extend the scope of paragraph 95(2)(*l*)

of the *Act*, which would specifically relieve Loblaw Financial from FAPI inclusion due to its connection with PC Bank (see paragraphs 215 and 216). The Appellant argues that this specific anti-avoidance rule makes clear that Parliament made an explicit policy choice to exclude foreign subsidiaries of Canadian regulated financial institutions. It is not as all-encompassing as that, I would suggest. A letter from the Joint Committee on Taxation of the Canadian Bar Association and Canadian Institution of Chartered Accountants in October 1994 gives some insight as to why this particular provision was introduced to accommodate *bona fide* financial institutions concerned about the proposed draft legislation in June 1994, that denied any exemption from FAPI with respect to a foreign affiliates business of trading in debt obligations on its own account or on the account of non-arm's length persons, even if it was a regulated financial institution:

> We consider that the scope of this exclusion is too broad, and may exclude from active business treatment under the FA rules many FAs that provide financial services to third parties. We are aware of at least one financial institution whose U.S. subsidiary employs thousands of persons and has hundreds of retail outlets. Nevertheless, this FA will likely be considered to have an investment business because it trades in mortgages which is not uncommon for U.S. financial institutions. Stock brokers who operate abroad through subsidiaries would also very likely encounter this problem.

[325] This again emphasizes the requirement for third party business, not just trading for proprietary purposes. It goes hand in hand with the financial institution exemption from investment business, rather than supplant it. I do not see any extending the scope of paragraph 95(2)(*l*) of the *Act*. No, had there been any avoidance transactions the Appellant would not be saved by the fact it is not caught by a specific anti-avoidance provision.

IV. CONCLUSION

[326] The FAPI rules are complicated, or convoluted as counsel on both sides reminded me, though I needed no reminding. GAAR can be complicated. Taken together they weave a web of intricacy worthy of the 400 pages of written argument presented to me by the Parties. It has not been necessary for me to cover in exhaustive detail every strand of the web. Once I determined how to interpret the financial institution exemption, the complexity disappeared and the case could be readily resolved on the simple basis that Loblaw Financial's foreign affiliate, a regulated foreign bank with more than the equivalent of five full time employees was conducting business principally with Loblaw and therefore could not avail itself of the financial institution exemption from investment business.

[327] With respect to the calculation of the FAPI that arises from my determination, I agree with Loblaw Financial that the financial exchange gains/losses should not be treated on capital account but on income account. It does not matter whether the management fees from the Disputed Entities fall within paragraph 95(2)(*b*) of the *Act* as they would be part of GBL's investment business caught by FAPI in any event.

[328] The Parties made no representations with respect to costs, which I have no doubt would be substantial on both sides. The Respondent has been successful in the final result though she lost many battles notwithstanding winning the war. My inclination would be to make no award of costs, sending each side home licking their wounds, absorbing their own costs. Given the time, energy and resources consumed by both sides on this matter, and their inability to reach a compromise that could easily have saved a considerable amount of such time, energy and resources, it will be no surprise to me if they would prefer making submissions on costs. I will not deny them the opportunity, especially if there had been a settlement offer of which, of course, I would not be aware. I give the Parties a head's up that it will have to be that sort of compelling argument to satisfy me my initial inclination is misplaced. I see no need for the Parties to re-attend to make oral argument: written argument will suffice. To that end, I limit the Parties to a maximum of 15 pages for their costs' argument. They shall advise me within one week of this decision whether they wish to avail themselves of the opportunity to make such written submissions. If they do not, then I make no costs award. If they do, then they shall have 60 days to submit their written arguments.

[329] I would like to conclude by thanking counsel for their professionalism, diligence and their quality of argument, but I cannot resist also expressing some regret that such competent representation could not have found a way to resolve these matters without the need for this trial and all that it entailed. From my perspective there were many possible principled bases for compromise. Pity.

Signed at Ottawa, Canada, this 7th day of September 2018.

"Campbell J. Miller"

C. Miller J.

APPENDIX A

LIST OF PERSONS INVOLVED

A. CORPORATE ENTITIES

Name	Description
George Weston Bakeries Inc.	A Delaware company whose goods were distributed by the Independent Operators.
George Weston International BV ("GWIBV")	A Dutch subsidiary of GWL involved in financing GWL's US operations.
George Weston Limited ("GWL")	A public corporation whose shares traded on the Toronto Stock Exchange, resident in Canada and controlling shareholder of LCL.
Glendock Finance Company ("Glendock")	An Irish company that acquired the independent operator loan portfolio from GBL in 2005.
Glenhuron Bank Limited	A Barbadian company licenced initially under *OSBA*, subsequently *IFSA*.
Glenhuron Global Management Inc. ("GGMI")	A subsidiary of GBL, identified by Mr. Berry as a marketing tool, dissolved in March 2003.
Glenhuron Finance	An LCL subsidiary.
Glenhuron Holdings Inc.	A subsidiary of Loblaw Financial.
Glenmaple Overseas BV ("GOBV")	A Dutch subsidiary of Loblaw Financial and preferred shareholder of GBL and NHI.
Glenmaple Reinsurance Company Limited ("GRCL")	A Barbadian company licenced under the *Exempt Insurance Act* of Barbados wholly owned by Dicoa Holdings Limited: its ultimate parent company is GWL.
Grupo Bimbo, SAB de CV	A corporation which acquired the US bakery operation and accompanying distributor loans in January 2009.
Loblaw Companies Limited ("LCL")	A Canadian public company whose shares traded on the Toronto Stock

	Exchange which wholly owned LINC which in turn wholly owned Loblaw Financial.
Loblaw Financial Holdings Inc. (the "Appellant" or "Loblaw Financial")	A wholly owned subsidiary of LINC and a controlled foreign affiliate of LCL. This entity was previously called Loblaw International Holding Inc. ("LIHI").
Loblaw Inc. ("LINC")	A Canadian resident corporation and wholly owned subsidiary of LCL.
National Holdings Inc. ("NHI")	A subsidiary of Loblaw Financial which held all common shares. Preferred shares of NHI were held by GOBV. NHI owned National TEA Company.
National TEA Company	A US company operating a grocery business in the US.
Pencarrek Limited	A Barbados International Business Company owned by Michael Berry.
President's Choice Bank ("PC Bank")	A wholly owned subsidiary of Loblaw Financial. A Schedule I Bank in Canada.
Provigo Distribution Inc.	An indirectly wholly-owned subsidiary of LCL
Provigo Holdings Inc.	
Weston Foods Canada Inc.	A Canadian resident corporation owned directly or indirectly by GWL
Weston Foods, Inc.	A US foreign affiliate of Loblaw Financial.
WFRG Investments Limited ("WFRG")	A subsidiary of Wittington Investments.
Wilmington Trust Company	A Delaware corporation, subsidiary of Citibank North America which managed the $440 million arising from the sale of National TEA as well as GBL's assets before the in-house investment team.
Wittington Investments Limited	A private company owned by Galen Weston.
Bank of America Corporation and SunTrust bank Inc.	The two corporate entities which sold the IO loan portfolio to GBL.
Best Foods Baking Company	Bought in 2001 by GWL

PGV Acquisition Inc.	

B. CORPORATIONS WITH ASSETS UNDER MANAGEMENT BY GBL

Name	Description
Dicoa Holdings Limited	A subsidiary of GWL incorporated in Gibraltar and sole owner of GRCL.
Dicoa Investment Limited	
Dunedin a Islandia sf, Swiss Branch	GWL subsidiary
Dunedin Holding Sarl	GWL subsidiary
Dunedin Holding Sarl, Swiss Branch	GWL subsidiary
Dunedin Servicing Co Rt., Swiss Branch	GWL subsidiary
Dunedin Finance a Islandi ehf	GWL subsidiary
Glendel Inc.	A Delaware company wholly owned by NHI.
GRCL	
JFS Inc.	
Megargy Kft.	
Megargy Kft, Luxembourg Branch	
Megargy Rt, Swiss Branch	
Moidart Finance Company	
Moidart Financial Services Company Limited	
Moidart Holdings LLC.	
PVO Assurance Inc.	A subsidiary of LCL through LCL's purchase of Provigo.
Sunfresh LLC	A US subsidiary of LCL and carried on the US grocery business not sold as part of the National TEA transaction.
Waterman Insurance Inc.	A reinsurance company being the only corporation with assets under management by GBL that was unrelated to GBL.
Weston Foods, Inc.	
Weston Foods U.S. Inc.	
Weston Acquisition Inc.	

C. GBL DIRECTORS AND EMPLOYEES

Name	Start date	End date	Role
Michael Berry	January 1, 1997	2013/ Liquidation	Originally he was Vice-President and Chief Investment Officer of GBL. On January 1, 2002 he became the President of GBL. On January 1, 2002 he became the President of GRCL. Subsequently, Mr. Berry also became President of PVO Assurance, WFRG Investments and Glenhuron Holdings. None of these entities paid him employment income, though WFRG paid him a director's fee. He was a Director of these companies.
Manny DiFilippo	Mid-1998	February 2002	For his first four months at GBL he was VP of Finance Administration. Then he replaced Mr. Walker as President of GBL. Upon leaving GBL, he "rejoined the corporate office at Loblaw George Weston" (at this point LCL and GWL had a combined corporate office).
Trevor Welch	August 1, 2001	Sometime after the end of 2010	In 2001 he joined GBL as VP Finance and Administration. He served as a director of GGMI in 2003. He previously worked at GBL from November 1993 to May 1998.
Wendel Mason	April 1, 1994	2013/ Liquidation	Originally he was an assistant accountant. He worked up to the accounting manager position. Then from 2002 to June 2005 he worked on the investment desk. The GBL organization charts found in Appendix C were incorrect regarding his position. Upon rejoining the back-office, he was "financial controller".
Jason Bayley	September 2007	April 2012	Originally he was an "Investment analyst". In 2011 he became an "Investment manager".

Donna Rogers	1994	2013/ Liquidation	She was always assistant to president to the bank [GBL]. In 2002 she became Treasury Assistant. She also assisted Mr. Berry with administrative tasks for the board meetings of GRCL, PVO Assurance, Glenhuron Holdings and WFRG.
Antoinette Patel	March 9, 1994	2010 or later	She was "initially assistant treasurer". She was "promoted to treasury manager" in 1998. She served as a director of GGMI in 2003.
Brenda Blackman	April 1, 1996	Definitely after 2010 and probably until 2013/ liquidation.	She was initially a receptionist. In the early 2000s she became an accountant/office manager. She prepared the financial statements for Glenhuron Holdings.
Carl Drayton	May 6, 1997	May 2005	He was an accounting officer and network supervisor.
Julia Robinson	February 15, 1999	Around June 30, 2005	She was hired as an accountant. Starting on the 2001 organization chart she is listed as "Accounting Manager". She prepared trial balances for affiliated companies.
Kirk Odle	March 22, 1999	February 28, 2001	He was an "assistant portfolio manager".
Beverly Holder	November 27, 2001	2013/ Liquidation	She was hired as a temporary employee, but became a permanent employee on February 1, 2002. She held various positions … reception, filing and … general administrative duties.
Francine Taylor	February 1, 2002	October 2009	She was a "Loans Administrator" for the IO loan portfolio.
Michelle Medford	January 1, 2002	March 2010	She was the loans accountant for the IO loan portfolio and IT supervisor.
Amanda McKenzie	March 1, 2003	2007	She worked "on the investment side" of GBL.

Shane Whittaker	September 1, 2005	2013/ liquidation	His contract listed his position as "financial analyst"; however, Mr. Berry testified that he also did IT.

Name	**Job Position(s)**
Jurriaan Zoetmulder	Around 1980 he became a director and tax advisor for GOBV and George Weston International BV. He was a director of GBL from 1992 until 2007.
Neil Walker	First president of GBL. Terminated as President in 1998.
Hugo Mann	Director of GBL and GOBV
Sheldon Durtsche	Director of GBL and GOBV
David King	Director of GBL from 1992 until 2007.

D. LOBLAW OFFICERS

Name	Description
Richard Mavrinac	Joined LCL as a tax officer in 1982. In 1991 or 1992 he became VP taxation for LCL. In the mid-90s he became VP finance. In the fall of 1996, LCL and GWL combined corporate offices, so he was/became VP finance for both LCL and GWL. Subsequently he became Senior VP finance (presumably for both LCL and GWL) and in 2002 he became CFO of GWL and Executive VP of LCL.
Bradley Holland	Joined GWL as director of taxation in 1993. In 1995 became VP of tax for GWL. In the fall of 1996 he became VP tax for both GWL and LCL. In that role he reported to VP finance for GWL and LCL, Rick Mavrinac. In 2007 he became Senior VP tax.
John Thompson	Executive VP Loblaw and Director of GOBV.
Don Reid	CFO Loblaw
Louise Lacchin	LCL Treasurer, then Senior VP Finance

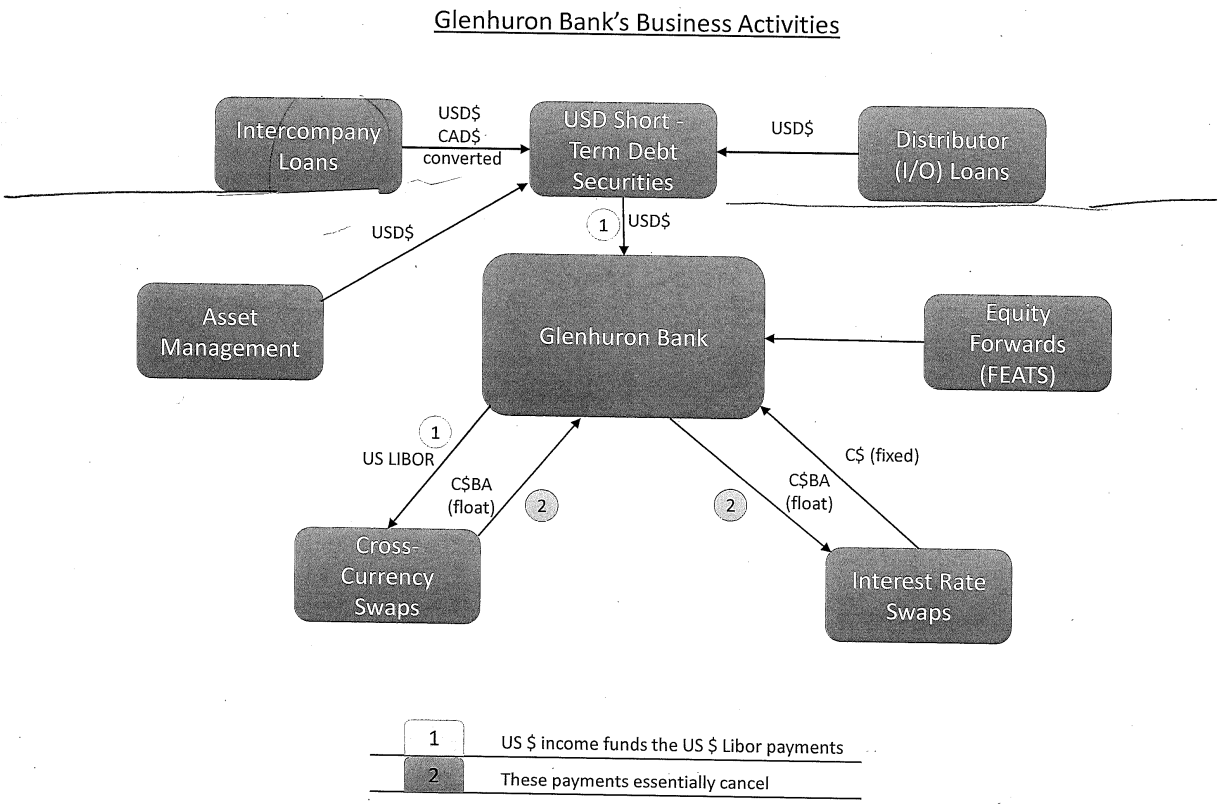
E. EXPERTS

Name	Description
Melanie Jones	Practitioner in Barbados
Rose-Marie Belle	Dean of Law School of West Indies
Antoine	
Mary Mahebir	Practitioner in Barbados

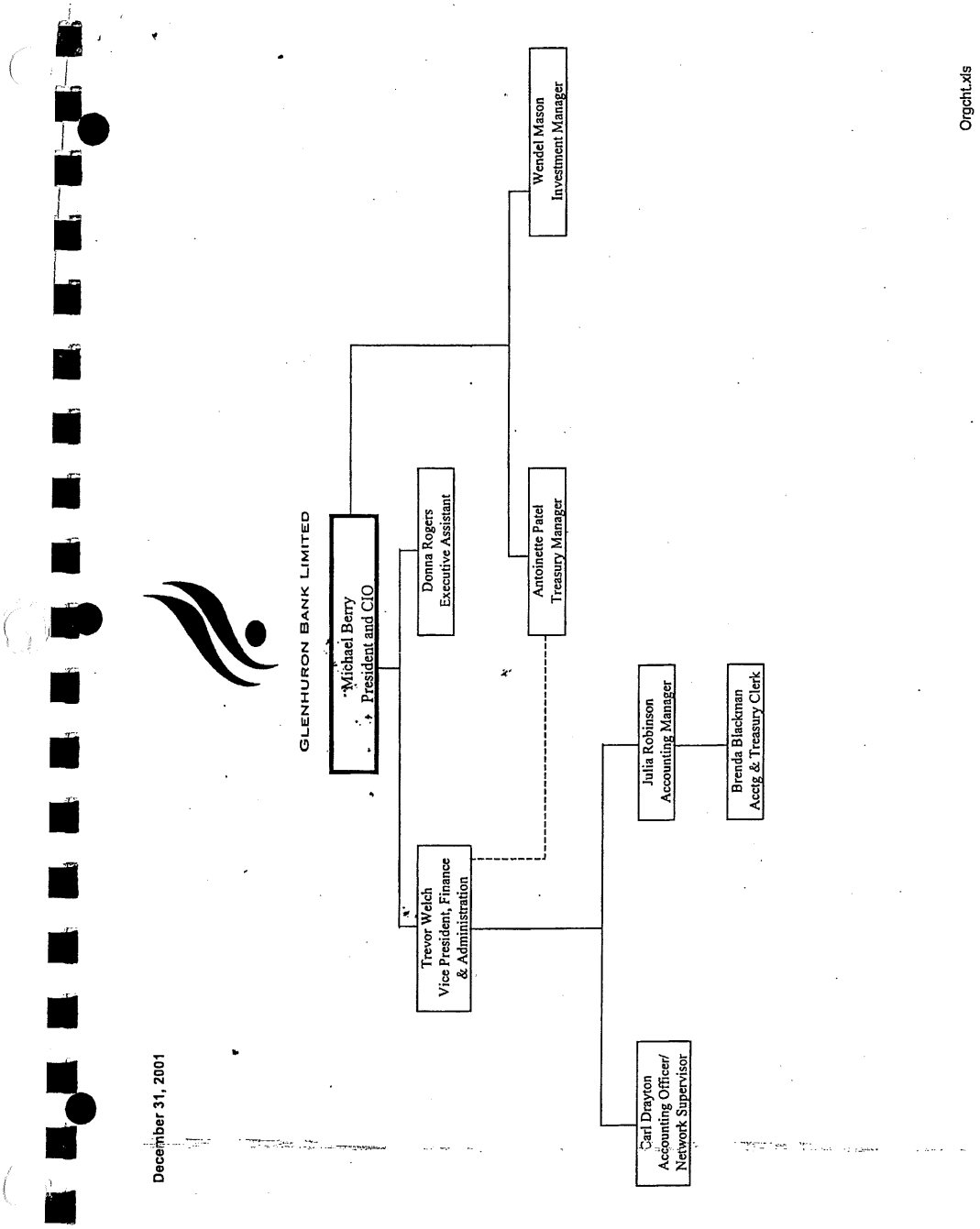
F. OTHERS

Name	Description
Carmen Lau	Revenue Canada employee being the large case manager involved in the audit of Loblaw Financial.

APPENDIX B


Glenhuron Bank's Business Activities
Intercompany Loans
USD$
CAD$
converted
USD Short - Term Debt Securities
USD$
Distributor (I/O) Loans
1
USD$
USD$
Asset Management
Glenhuron Bank
Equity Forwards (FEATS)
1
US LIBOR
C$BA (float)
2
2
C$BA (float)
C$ (fixed)
Cross-Currency Swaps
Interest Rate Swaps
1
US $ income funds the US $ Libor payments
2
These payments essentially cancel

APPENDIX C


GLENHURON BANK LIMITED
Michael Berry
President and CIO
Donna Rogers
Executive Assistant
Wendel Mason
Investment Manager
Antoinette Patel
Treasury Manager
Trevor Welch
Vice President, Finance
& Administration
Julia Robinson
Accounting Manager
Brenda Blackman
Acctg & Treasury Clerk
Carl Drayton
Accounting Officer/
Network Supervisor
December 31, 2001
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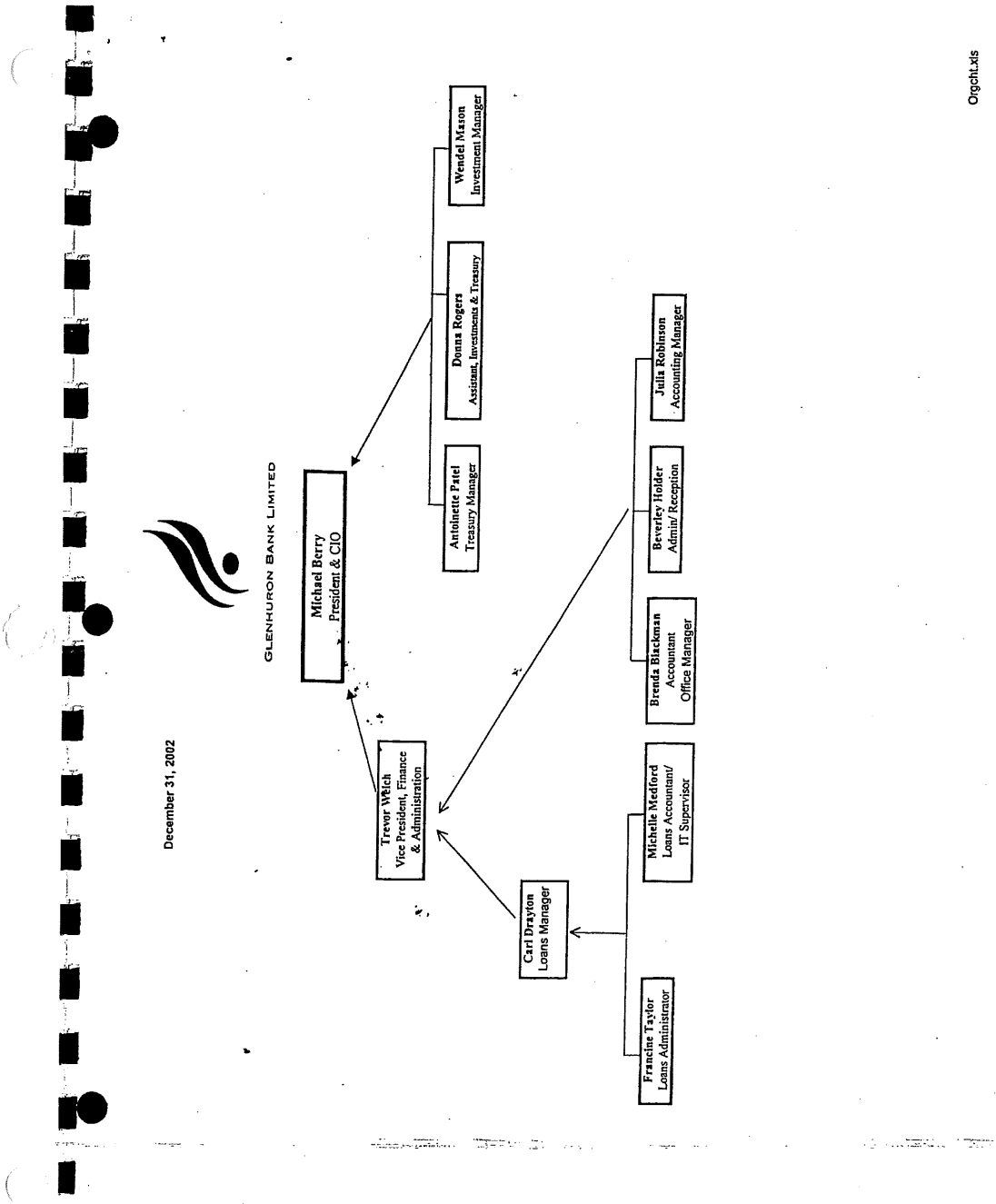
GLENHURON BANK LIMITED
December 31, 2002
Michael Berry
President & CIO
Trevor Welch
Vice President, Finance
& Administration
Antoinette Patel
Treasury Manager
Donna Rogers
Assistant, Investments & Treasury
Wendel Mason
Investment Manager
Julia Robinson
Accounting Manager
Beverley Holder
Admin/ Reception
Brenda Blackman
Accountant
Office Manager
Carl Drayton
Loans Manager
Michelle Medford
Loans Accountant/
IT Supervisor
Francine Taylor
Loans Administrator
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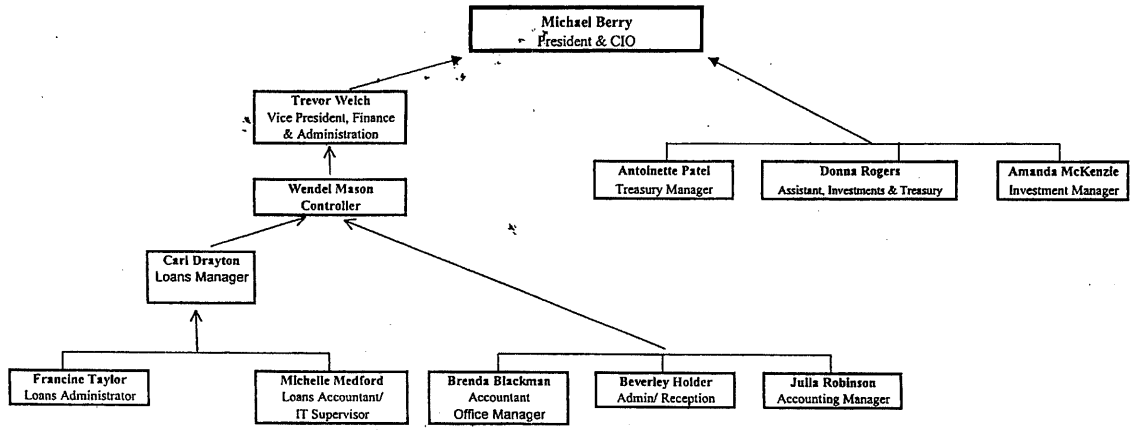
December 31, 2003

GLENHURON BANK LIMITED



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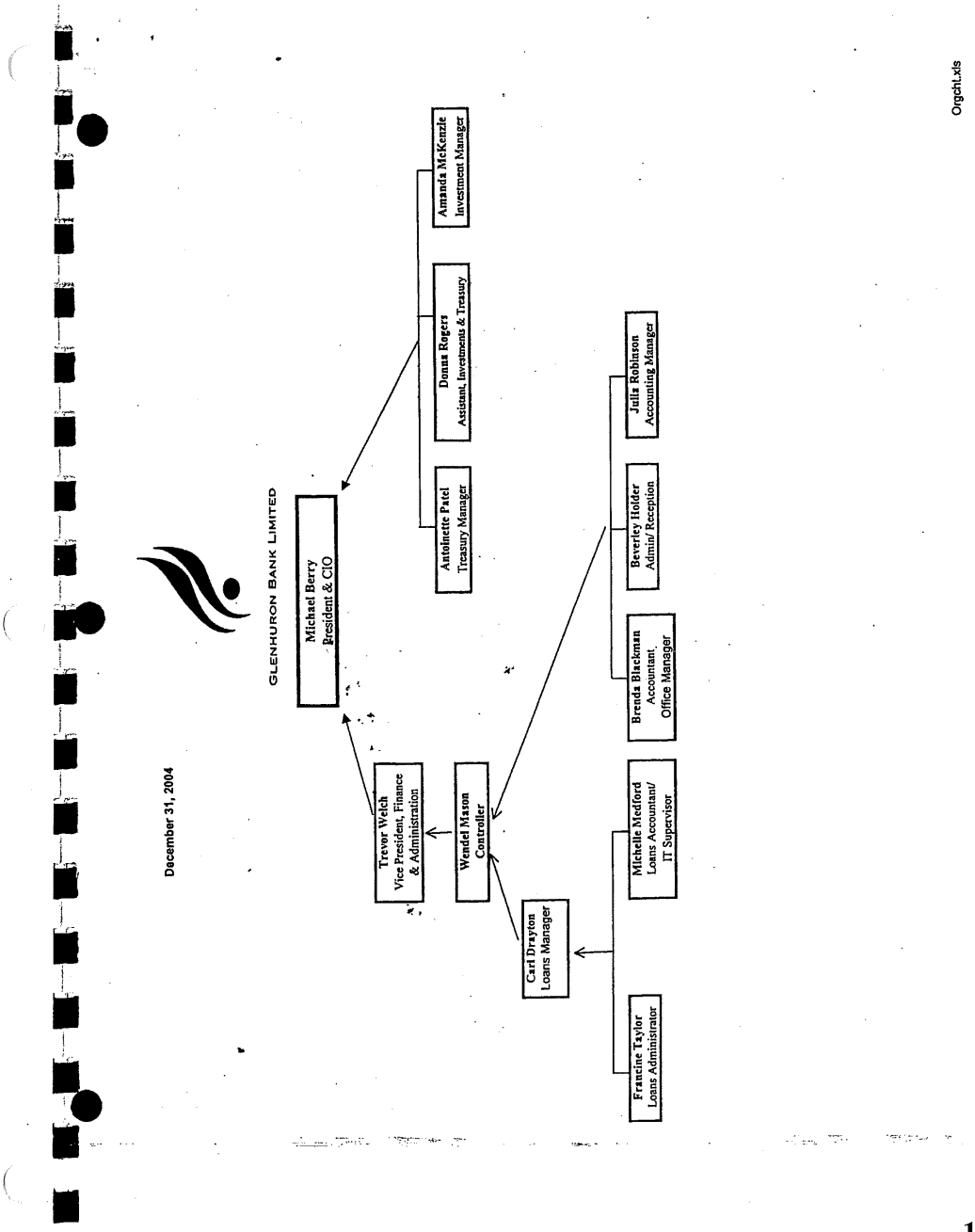
GLENHURON BANK LIMITED
December 31, 2004
Michael Berry
President & CIO
Trevor Welch
Vice President, Finance & Administration
Wendel Mason
Controller
Carl Drayton
Loans Manager
Francine Taylor
Loans Administrator
Michelle Medford
Loans Accountant/ IT Supervisor
Brenda Blackman
Accountant, Office Manager
Beverley Holder
Admin/ Reception
Julia Robinson
Accounting Manager
Antoinette Patel
Treasury Manager
Donna Rogers
Assistant, Investments & Treasury
Amanda McKenzie
Investment Manager
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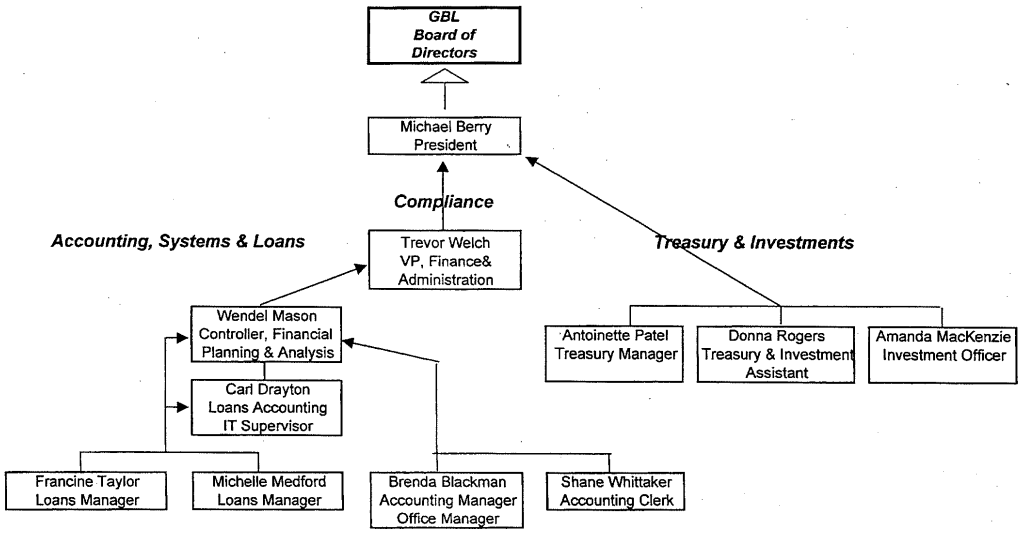
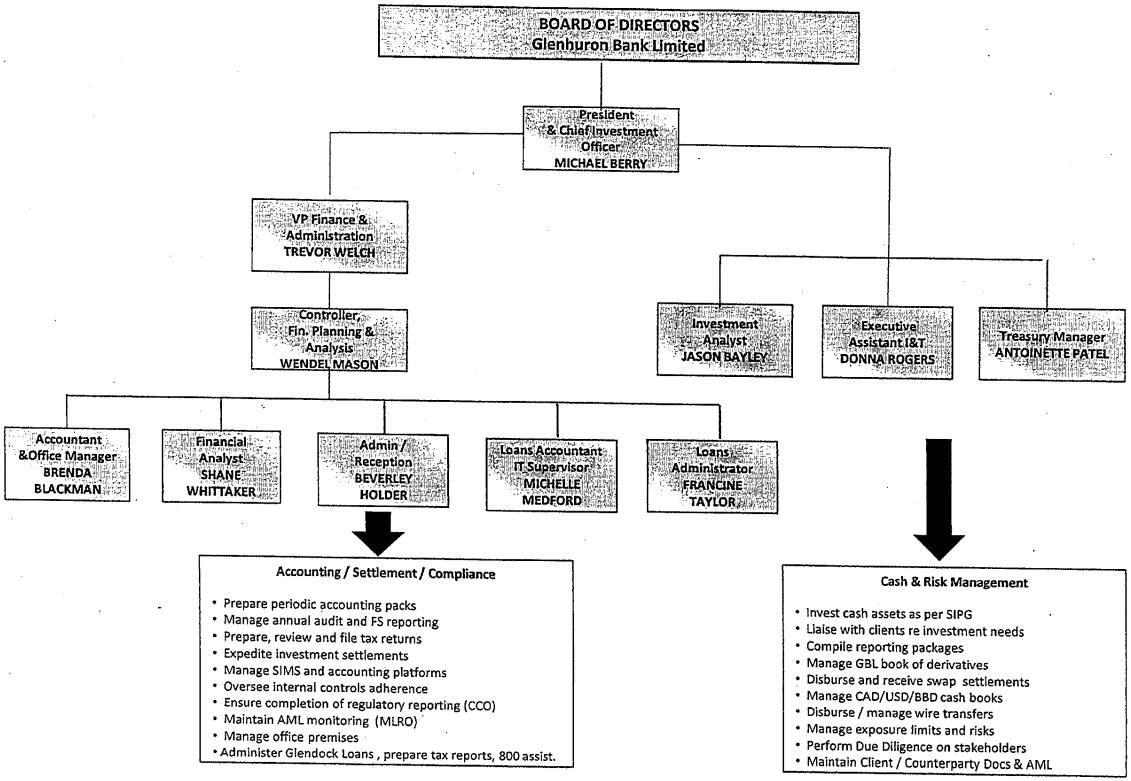
GLENHURON BANK LIMITED

Organization Chart
January 1, 2005.



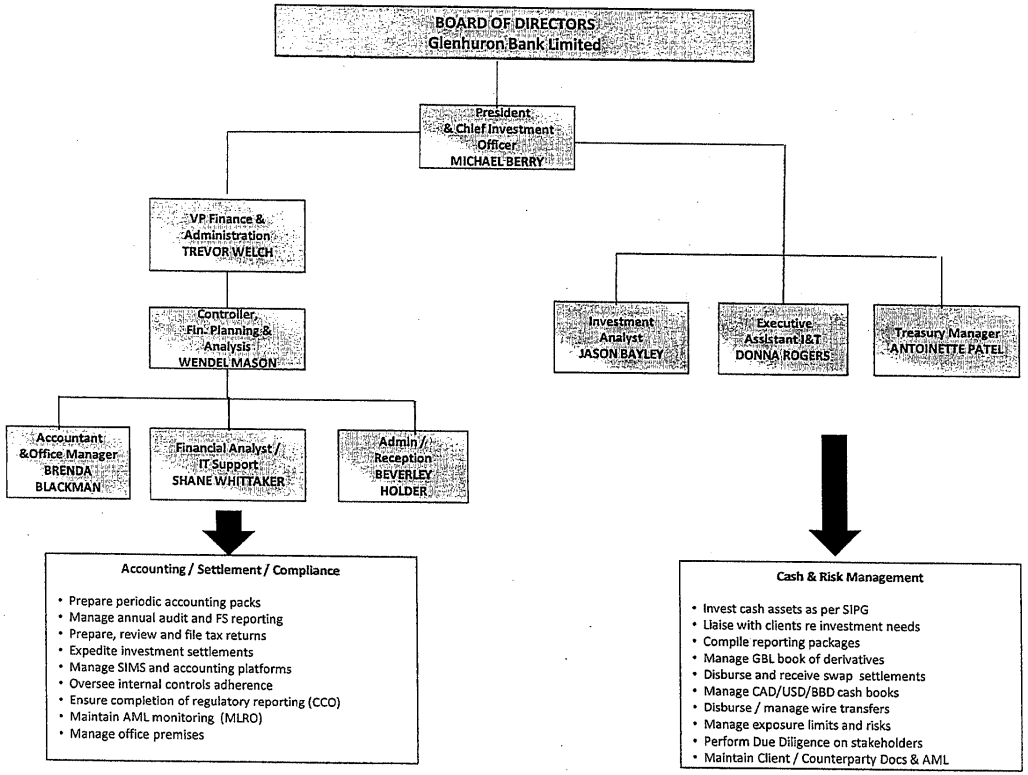
GLENHURON BANK LIMITED

Year End 2007



GLENHURON BANK LIMITED

Year End 2010



APPENDIX D

Legislation Name	Enactment Date	Repealment Date
Banking Act, Cap. 322	April 1, 1964	1992
Interpretation Act, Cap. 1	June 16, 1966	
Exchange Control Act, Cap 71	November 21, 1967	
Income Tax Act, Cap. 73	January 2, 1969	
Central Bank Act, Cap. 323C	May 2, 1972	
Off-shore Banking Act, Cap. 325 ("*OSBA*")	August 7, 1980	2002
Exempt Insurance Act, Cap. 308A	October 4, 1983	
Companies Act, Cap. 308	January 1, 1985	
International Business Companies Act, Cap. 77	March 1, 1992	
Financial Intermediaries Regulatory Act, Cap. 324A	June 9, 1992	1996
International Trusts Act, Cap. 245	December 7, 1995	
Insurance Act, Cap. 310	February 17, 1997	
Financial Institutions Act, Cap. 324A ("*FIA*")	July 1, 1997	
Securities Act, Cap. 318A	August 2, 2001	
International Financial Services Act, Cap. 325 ("*IFSA*")	June 10, 2002	

CITATION:	2018 TCC 182
COURT FILE NO.:	2015-2998(IT)G
STYLE OF CAUSE:	LOBLAW FINANCIAL HOLDINGS INC. AND HER MAJESTY THE QUEEN
PLACE OF HEARING:	Toronto, Ontario
DATE OF HEARING:	April 23 to May 15, July 17 and 18, 2018
REASONS FOR JUDGMENT BY:	The Honourable Justice Campbell J. Miller
DATE OF JUDGMENT:	September 7, 2018

APPEARANCES:

Counsel for the Appellant:	Mary Paterson, Mark Sheeley, Pooja Mihailovich, Al Meghji, Lipi Mishra
Counsel for the Respondent:	Elizabeth Chasson, Isida Ranxi, Aleksandrs Zemdegs, Gary Edwards, Laurent Bartleman, Cherylyn Dickson

COUNSEL OF RECORD:

For the Appellant:

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Firm:	Osler, Hoskin and Harcourt LLP

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