

# IATJ 2012 – Munich

## GAAR & Judicial Anti-Avoidance Doctrines

### A Canadian Perspective



**Farcus**

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**“Geez, I hate tax law.”**

- Canada has had a statutory GAAR since 1988
  - Replaced an “undue or artificial reduction” provision
- Canada continues to have judicially developed, non-statutory anti-avoidance principles:
  - Ineffective or incomplete transactions
  - Sham transactions

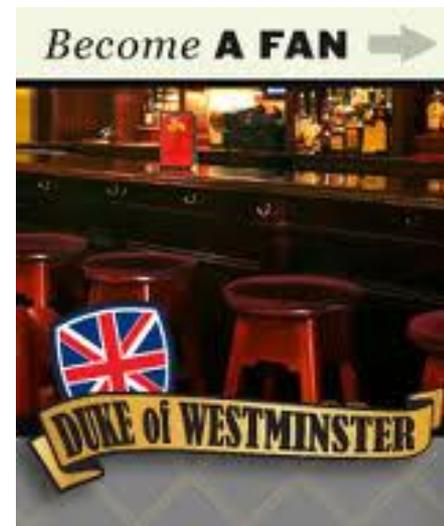
# The *Duke of Westminster* may be alive and well in Canada





*“Every man is entitled if he can to order his affairs so as that the tax attaching under the appropriate Acts is less than it otherwise would be. If he succeeds in ordering them so as to secure this result, then, however unappreciative the Commissioners of Inland Revenue or his fellow taxpayers may be of his ingenuity, he cannot be compelled to pay an increased tax.”*

Per Lord Tomlin









# ***Stuart Investments Ltd***

- Government's 1984 loss in Supreme Court of Canada led to the introduction of GAAR
- Crown was seeking a judicial 'business purpose test' doctrine
- SCC clearly rejected a *bona fide* business purpose test
- SCC says a transaction lacking a *bona fide* business purpose can only be overlooked if its tax result defeats the *object and spirit* of the provision read *in the context of the whole statute* and the provision's *purpose*

# GAAR

- Announced in 1987. Effective 1988
- Requires 3 things:
  - Tax benefit
  - Avoidance transaction
    - Defined as undertaken primarily for *bona fide* non-tax purposes
      - » Not *bona fide* business purposes
  - Misuse or abuse of the provisions of the statute or the statute read as a whole
    - Abusive
- Tax consequences are to be redetermined as is reasonable in the circumstances to deny the tax benefit

# 1. Tax Benefit

- If tax deduction claimed, tax reduction necessarily a tax benefit
- Can also look to other available transactions to see if taxpayer chose one with a tax benefit
- Tax reduction can result from Act, Regulations, treaties
  - (*MIL Investments and RMM Enterprises*)
- Onus or burden on taxpayer

## 2. Avoidance Transaction

- Transaction resulting in tax benefit will be an avoidance transaction unless undertaken primarily for *bona fide* non-tax purpose
- Question of fact. Onus or burden on taxpayer
- Tax purpose or knowledge of tax consequences not necessarily primarily for tax purposes
- Look only at transactions undertaken; not alternatives not chosen by taxpayer
  - Deference to the *Duke*

# Series of Transactions

- A transaction will be an avoidance transaction if any of the steps in the series was not undertaken primarily for *bona fide* non-tax purposes
  - Catches steps needed to position the taxpayer to claim the tax benefit sought
- Series has a common law meaning and an inclusive statutory definition
  - Pre-ordained
  - Any related transaction done in contemplation of series
  - Compare series with and without the step in question to test if that step primarily for tax purposes

# 3. Abuse or Misuse

- Is it abusive?
- SCC in *Canada Trustco* (2005) and in *Cophorne Holdings* (2011)
- Two part analytic approach required:
  1. Determine object, spirit or purpose of provision relied upon
    - using a textual, contextual and purposive approach
  2. Does the avoidance transaction fall within that purpose or defeat or frustrate it?

# Does the avoidance transaction fall within that purpose or defeat or frustrate it?

If so it is abusive:

1. Does it achieve an outcome the provision was intended to prevent?
2. Does it defeat the underlying rationale of the provision? or
3. Does it circumvent the provision in a manner that frustrates its object, spirit or purpose?

# Is it Abusive?

- Transaction specific
  - Looks at avoidance transaction step
  - Not relative to other available transactions to achieve same non-tax result
- Onus is on government, not taxpayer,
- Abuse must be clear –any residual doubt to be resolved in favour of taxpayer
  - in the interest of certainty for taxpayers

# Impact of GAAR 20+ Years On

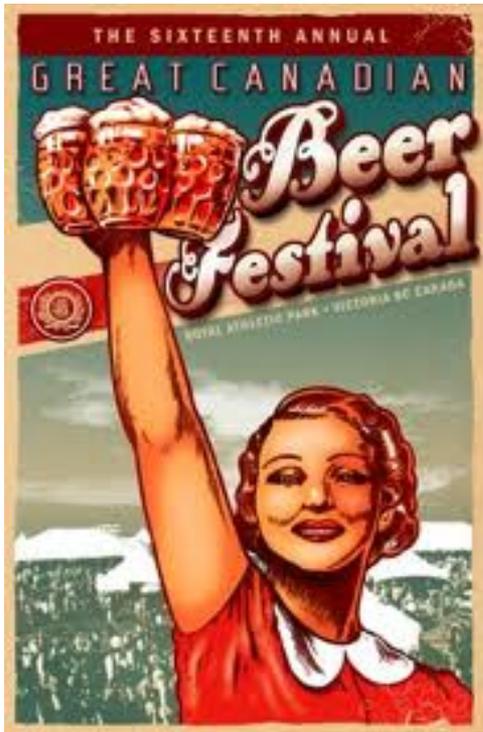
- *Stuart – SCC pre-GAAR:*
  - Does transaction defeat *object and spirit* of the statutory provision
    - *in the context of the whole statute and the provision's purpose*
- SCC on GAAR:
  - identify object, spirit or purpose of provision relied upon
    - using a textual, contextual and purposive approach
  - Does the transaction defeat or frustrate that purpose?
- Plus ça change, plus c'est la même chose?

# Sham Transactions Judicial Doctrine

- Classic UK definition from House of Lords in *Snook v. London West Riding Investments*:
  - *acts done or documents executed by the parties to the “sham” which are intended by them, to give to third parties or the Court, the appearance of creating between the parties, legal rights and obligations different from the actual legal rights and obligations (if any), which the parties intend to create. ...*
- Continues to be applied and evolve in Canada post-GAAR
- Sham is not synonymous with an abuse of the provisions of the Act : FCA in *Faraggi, Langlois et al*
- Tax sham intention to deceive not so high as criminal *mens rea*: FCA in *Antle*

# Ineffective Transaction Judicial Doctrine

- Transactions that are found to be legally invalid and never actually occurred
- All steps not completed, or not completed at the right time or in the right order
- *Antle*



# ENDE

