File No. 39869

IN THE SUPREME COURT OF CANADA
(ON APPEAL FROM THE FEDERAL COURT OF APPEAL)

BETWEEN:

DEANS KNIGHT INCOME CORPORATION

Appellant
(Respondent in the
Federal Court of Appeal)

- and -

HER MAJESTY THE QUEEN

Respondent
(Appellant in the
Federal Court of Appeal)

FACTUM OF THE APPELLANT

DEANS KNIGHT INCOME CORPORATION (APPELLANT)

(Pursuant to Section 60 of the *Supreme Court Act*, R.S.C. 1985, c. S-26
and Rules 35, 36, 37, 42 and 43 of the *Rules of the Supreme Court of Canada*, ,SOR/2002-156)

Counsel for the Appellant

Burnet, Duckworth & Palmer LLP
2400, 525 – 8th Avenue SW
Calgary, AB T2P 1G1
Attention: Barry Crump / Heather DiGregorio/
Robert Martz
Email: brc@bdplaw.com / hrd@bdplaw.com /
rmartz@bdplaw.com
Phone: (403) 260-0352 / (403) 260-0341

Counsel for the Respondent

Attorney General of Canada
Department of Justice Canada
British Columbia Regional Office
900 - 840 Howe Street
Vancouver, British Columbia V6Z 2S9
Attention: Michael Taylor / Perry Derksen
Email: michael.taylor@justice.gc.ca /
perry.derksen@justice.gc.ca
Phone: (604) 318-0118 / (604) 775-6017

Agent for the Respondent

Deputy Attorney General of Canada
Department of Justice
National Litigation Sector
50 O'Connor Street, 5th Floor
Ottawa, Ontario K1A 0H8
Attention: Christopher Rupar
Email: christopher.rupar@justice.gc.ca
Phone: (613) 670-6290

TABLE OF CONTENTS

PART I - OVERVIEW AND FACTS

A. Overview

1. Predictability, certainty, and fairness are bedrock principles of Canadian tax law.[1] Over two decades ago in *Duha Printers*, this Court found that "control" in the *Income Tax Act*[2] is *de jure* control, which this Court defined as the "effective control of the affairs and fortunes of the corporation." The test for *de jure* control, accordingly, is the determination of whether a person enjoys the ability to elect the majority of the board of directors by virtue of its shareholdings.[3]

2. In *Duha*, this Court established *de jure* control as the "Canadian standard", expressly telling taxpayers that where a provision of the *Act* uses the term "control", that provision employs the *de jure* control test. Alternatively, where Parliament uses the term "controlled, directly or indirectly in any manner whatever", it signals the *de facto* control test, which allows for the consideration of a broad range of facts and circumstances in addition to *de jure* control.[4]

3. What has emerged since *Duha* under the *Act* is a predictable and complete framework that clearly distinguishes those provisions that require the *de jure* control test from those that apply the *de facto* control test. The two control tests are used extensively throughout the *Act*, with *de jure* control applying in over 90 provisions and *de facto* control applying in at least 18.

4. This appeal raises the question of what Parliament intended when it chose the *de jure* control test as the trigger for the loss restrictions[5] in ss. 37(6.1), 111(5) and 127(9.1) of the *Act*. These sections operate to restrict certain loss deductions and tax credits of a corporation where a new person or group of persons acquires control of the corporation. Under the *Duha* framework, control in these sections has been understood for decades to mean *de jure* control.

---

[1] *R. v. Alta Energy Luxembourg S.A.R.L.*, 2021 SCC 49 ("**Alta Energy**") at para 1.
[2] *Income Tax Act*, R.S.C., 1985, c. 1 (5th Supp.) (en | fn) (the "***Act***").
[3] *Duha Printers (Western) Ltd. v. R.* [1998] 1 S.C.R. 795 ("***Duha***") at para 36.
[4] *Duha* at paras 36 and 52.
[5] In this appeal, the phrase "loss restrictions" is used interchangeably to describe restrictions on claims for non-capital losses, scientific research and experimental development expenditures and investment tax credits, given the similarity of the restrictions to each.

5. The Federal Court of Appeal's (the "**FCA**") decision in this case upends decades of certainty and predictability. Relying on the general anti-avoidance rule (the "**GAAR**"),[6] the FCA created a third category of control that it called "actual control"—a term found nowhere in the *Act*. The FCA asserts that "actual control" includes forms of *de jure* and *de facto* control,[7] while ignoring the fact that in *Duha*, this court equated actual control with *de facto* control.[8] Ultimately, actual control appears to simply be a renaming of the *de facto* control test.

6. The FCA erred by ignoring this Court's decision in *Duha* and using the GAAR to eliminate the clear line that Parliament has drawn between *de jure* and *de facto* control. The FCA's decision has far-reaching consequences, and this recharacterization of Parliament's intent through the creation of an undefined category of "actual control" will affect taxpayers across Canada.

7. In reading this new test of actual control into the object, spirit and purpose of ss. 37(6.1), 111(5) and 127(9.1), the FCA usurps Parliament's role. This Court stated in *Duha* that if the distinction between *de jure* and *de facto* control is to be eliminated, this should be left to Parliament.[9]

8. This invitation has been open for over 24 years; Parliament has not elected to accept it, despite amending the *Act* every year. To the contrary, all amendments to the *Act* have directly and expressly demonstrated that Parliament understands, accepts, and intends to maintain the distinction between *de jure* and *de facto* control. By choosing the *de jure* control test in ss. 37(6.1), 111(5) and 127(9.1), Parliament has balanced its intent to restrict loss trading with its goal of supporting and promoting economic activity in Canada.[10]

9. Rather than accept *Duha's* findings on Parliament's intent, the FCA relied on general policy statements of government officials from 1963 and 1988 (both of which predate *Duha*) to overrule Justice Paris of the Tax Court of Canada (the "**Tax Court**") in this case and introduce its new test

---

[6] Section 245 of the *Act*, (en | fn) (the "***Act***").
[7] Federal Court of Appeal Reasons for Judgment, dated August 4, 2021 at para 83 (**Appellant's Record, Tab 4**) ("**FCA Reasons**").
[8] *Duha* at para 49.
[9] *Duha* at para 52.
[10] John Burghardt and Sarah Chiu, "'Loss' Is Just a Four-Letter Word: Policy, Practice, and Proposals," *Report of Proceedings of the Sixty-Fifth Tax Conference*, 2013 Conference Report (Toronto: Canadian Tax Foundation, 2014) at 14:5-8 (**Appellant's Book of Authorities "ABoA," Tab 17**).

for control. This is directly contrary to this Court's admonition in *Canada Trustco*, repeated in *Copthorne* and *Alta Energy*, that courts cannot search for an overriding policy that is not based on a unified textual, contextual, and purposive interpretation of the specific provisions at issue.[11]

10. The Tax Court's GAAR analysis and application were correct. The Tax Court conducted an in-depth analysis of the legislative history of the provisions at issue, considered the findings in *Duha*, and concluded that the object, spirit and purpose of s. 111(5) (and therefore ss. 37(6.1) and 127(9.1)) was to "target manipulation of losses of a corporation by a new person or group of persons, through effective control over the corporation's actions".[12] This led the Tax Court to find that Matco did not acquire *de jure* control of the Appellant and the series of transactions to recapitalize and restart the Appellant's business was not abusive. In contrast, the FCA largely disregarded the transactions actually undertaken by the Appellant. This Court should set aside the decision of the FCA and reinstate the decision of the Tax Court.

B. Facts

11. The Appellant was incorporated in 1985 and originally engaged in mineral exploration in British Columbia. In 1992, it changed its business entirely and began a drug research and nutritional food additive business. While it was in this business, the Appellant raised over $100 million from investors and spent those funds on its business, incurring significant non-capital losses ("**losses**"), scientific research and experimental development expenditures ("**SR&ED**"), and obtaining investment tax credits ("**ITCs**") (collectively, the "**tax attributes**").[13]

12. The Appellant's business was not profitable, and in 2007, it faced insolvency and a potential delisting of its shares from the NASDAQ stock exchange. Throughout 2007, the Appellant sought new financing and new business opportunities, including potential merger and acquisition opportunities with at least eight other pharmaceutical and research companies.[14]

---

[11] *Copthorne Holdings Ltd. v. R.*, 2011 SCC 63 ("***Copthorne***") at para 118; *Canada Trustco Mortgage Co. v. R.*, 2005 SCC 54 ("***Canada Trustco***") at paras 41–42; *Alta Energy* at para 49.
[12] Reasons for Judgment of the Tax Court of Canada dated April 5, 2019 ("**TCC Reasons**") at para 134 (**Appellant's Record, Tab 2**).
[13] TCC Reasons at paras 1 and 6–8 (**Appellant's Record, Tab 2**); Partial Agreed Statement of Facts ("**Agreed Facts**") at paras 6–22 (**Appellant's Record, Tab 8**).
[14] TCC Reasons at para 7 (**Appellant's Record, Tab 2**); Agreed Facts paras 26–27 and 36 (**Appellant's Record, Tab 8**).

13. In early 2008, the Appellant reorganized and restructured itself by implementing a Plan of Arrangement (the "**Plan**") to effect an eight-to-one exchange of shares and warrants between the Appellant and a new company, 0813361 BC Ltd. ("**Newco**"). Under the Plan, Newco became the parent of the Appellant (*i.e.*, Newco became the owner of 100% of the Appellant's shares) and Newco's shares began to be traded on the NASDAQ in substitution for the shares of the Appellant. This new structure resolved the delisting risk on the NASDAQ and at the same time prepared for the potential to capitalize on financing opportunities that might arise in the future.[15]

14. On March 19, 2008, the Appellant entered into an Investment Agreement ("**Investment Agreement**") with Newco and a venture capital company, Matco Investments Ltd. ("**Matco**").[16] The purpose of the Investment Agreement was for the Appellant to "pursue a corporate business opportunity with Matco's assistance ".[17] In order to accomplish this purpose, the Appellant's failing business would be transferred to Newco and Matco would facilitate the search for a new business opportunity (a "**Corporate Opportunity**").

15. On May 9, 2008, pursuant to the Investment Agreement, Matco subscribed for and purchased a $2.96 million convertible debenture (the "**Convertible Debenture**") from the Appellant, which was a debt instrument that was convertible into shares, including 35% of the Appellant's voting shares. While the Convertible Debenture remained an outstanding debt, Newco would continue to own all of the issued shares of the Appellant, except for a nominal number of shares (*i.e.*, 100 shares) owned by a company controlled by Alan Ross, the managing director of Matco ("**Ross**"). At this point, pursuant to the Convertible Debenture and a General Security Agreement under which the Appellant, as a debtor, granted security to Matco over all of the Appellant's present and after-acquired property, Matco was a lender to the Appellant, but not a shareholder.[18]

16. The Investment Agreement also required Matco to find an investor that would purchase Newco's common shares of the Appellant (the "**Remaining Shares**") for a guaranteed amount

---

[15] TCC Reasons at paras 15–17(**Appellant's Record, Tab 2**); Agreed Facts paras 42–44 (**Appellant's Record, Tab 8**).
[16] Investment Agreement dated March 19, 2008 (**Appellant's Record, Tab 10.3**).
[17] Investment Agreement, first recital on page 1 (**Appellant's Record, Tab 10.3**).
[18] Convertible Debenture dated May 9, 2008 and General Security Agreement dated May 9, 2008 (**Appellant's Record, Tabs 10.4 and 10.5**).

("**Guaranteed Amount**") of $800,000 (such purchase opportunity being a "**Sale Opportunity**"). Newco, however, was under no obligation to sell its shares pursuant to a Sale Opportunity and could choose to continue to hold the Appellant's shares at its discretion for as long as it wanted.[19]

17. The Investment Agreement gave Matco one year to find a Corporate Opportunity and a Sale Opportunity. If Matco failed to find a Corporate Opportunity and a Sale Opportunity within one year (*i.e.*, by April 30, 2009), it would be obligated to pay Newco the Guaranteed Amount.[20]

18. Under the Investment Agreement, Matco had no control over the Appellant's board of directors and Newco retained control of the Appellant's business and affairs. As well:

(a) Newco owned nearly all of the shares of the Appellant, which entitled it to vote in and control the board of directors;

(b) Newco appointed the majority of the directors of the board;

(c) Newco remained free to sell its shares of the Appellant to any party at any time as it saw fit;[21] and

(d) the Appellant and Newco were free to accept or reject at their sole discretion any Corporate Opportunity Matco presented.[22]

19. In exchange, the Investment Agreement protected Matco's investment through a number of covenants that were intended to ensure that Newco and the Appellant would not unilaterally take certain actions that could put Matco's financial investment at risk while Matco sourced potential business opportunities. These included promises not to change or amend the Appellant's constating documents or bylaws, issue or cancel shares, warrants, etc.; declare and pay dividends; or enter into, assign, terminate or amend any contract or agreement of the Appellant. The trial judge found that these restrictions under the Investment Agreement did not give Matco control over the Appellant.[23]

---

[19] TCC Reasons at para 22 (**Appellant's Record, Tab 2**).
[20] TCC Reasons at paras 22–23 (**Appellant's Record, Tab 2**).
[21] TCC Reasons at paras 157–160 (**Appellant's Record, Tab 2**).
[22] TCC Reasons at para 23 (**Appellant's Record, Tab 2**); Investment Agreement, Section 4.1 (**Appellant's Record, Tab 10.3**).
[23] TCC Reasons at paras 21, 25–27, and 160 (**Appellant's Record, Tab 2**); Trial testimony of Ross, p. 6, line 25–p. 7, line 8 (**Appellant's Record, Tab 12**).

20. Matco's search for new business opportunities led it to a fund manager, Deans Knight Capital Management ("**DKCM**").[24] DKCM was looking to sponsor a new investment fund as, in its assessment, there was an opportunity to start an investment business in high-yield corporate bonds in the "BBB" rating category. These bonds were trading at low prices because of the financial crisis in 2008. The high-yield investment business therefore became the Corporate Opportunity for the Appellant, which would raise new money to start the business by selling shares to the public through an initial public offering ("**IPO**"). The Sale Opportunity for Newco would be the IPO itself, as Newco would become able to sell the Remaining Shares at any time on the public market.[25]

21. The parties proceeded with the IPO, which closed on March 18, 2009. The transactions that day occurred in the following sequence:

(a) Matco exercised its conversion right under the Convertible Debenture, resulting in the issuance to it of 35% of the Appellant's voting common shares together with non-voting common shares totaling 79% of the Appellant's equity. At this point, Newco held 65% of the Appellant's voting common shares, representing 21% of its total equity.

(b) The Appellant then issued 10,036,890 new voting common shares to a wide group of investors, raising a total of $100,368,900 with which to start its new business.

(c) At the end of the day on March 18, 2009, Newco's common shares represented approximately 1% of the outstanding equity of the Appellant. Matco's common shares represented approximately 3.8% of the outstanding equity of the Appellant and approximately 0.5% of the Appellant's voting common shares.[26]

22. One month later, on April 16, 2009, Matco offered to purchase Newco's Remaining Shares of the Appellant for approximately $7.85 per share. The Appellant's chief financial officer, David

---

[24] Matco, the Appellant and DKCM were not related.
[25] TCC Reasons at paras 28–34 (**Appellant's Record, Tab 2**); Agreed Facts at paras 64–65 (**Appellant's Record, Tab 8**). Trial testimony of Craig Langdon, partner in DKCM ("**Langdon**"), p. 54, line 20–p. 57, line 21 (**Appellant's Record, Tab 17**); Appellant's IPO prospectus March 9, 2009 at p. 25 (**Appellant's Record, Tab 10.7**).
[26] TCC Reasons at paras 36–38 (**Appellant's Record, Tab 2**); Agreed Facts at paras 69–70 and 72–73 (**Appellant's Record, Tab 8**).

Goold ("**Goold**"), testified that Newco accepted the offer despite it being at a discount to the IPO price because Newco needed the money for its operations and its Board was concerned that the share price might fall before the end of its 180-day post-IPO lockup period. The trial judge found Goold to be a credible witness and accepted his testimony as well as the confirming testimony of Ross.[27]

23. The Appellant's high-yield bond investment business was largely successful, and the Appellant paid dividends of approximately $26.4 million to shareholders between 2009 and 2012. The Appellant's portfolio was substantially liquidated by April 30, 2014, and the shareholders received a special distribution of $9.75 per share as a result.[28]

24. The Canada Revenue Agency reassessed the Appellant's income tax returns for its taxation years ending on December 31, 2009 through December 31, 2012, disallowing the Appellant's claims of $64.7 million in non-capital losses, SR&ED and ITCs.[29]

a. The Tax Court of Canada Decision

25. The Crown raised two arguments before the Tax Court of Canada. First, the Crown argued (unsuccessfully) that Matco obtained a right under the Investment Agreement to acquire the majority of voting shares of the Appellant. The Tax Court judge found that no such right existed; the Crown did not appeal this finding.[30]

26. In the alternative, the Crown argued that the GAAR should apply. The Tax Court rejected this position as well. Justice Paris found that that the object, spirit and purpose of s. 111(5) is "to target manipulation of losses of a corporation by a new person or group of persons, through effective control over the corporation's actions". He held that the *de jure* control test in s. 111(5) is a reasonable marker chosen by Parliament between situations where a corporation is a free actor

---

[27] TCC Reasons at paras 39–40 and 64 (**Appellant's Record, Tab 2**); Agreed Facts at paras 74–77 (**Appellant's Record, Tab 8**).
[28] TCC Reasons at para 41 (**Appellant's Record, Tab 2**); Trial testimony of Langdon, p. 80 line 1–p. 81, line 5 (**Appellant's Record, Tab 17**); Appellant's audited financial statement for its year ending December 31, 2010 prepared by PricewaterhouseCoopers LLP (**Appellant's Record, Tab 10.12, p. 123**).
[29] TCC Reasons at paras 42–44 (**Appellant's Record, Tab 2**).
[30] TCC Reasons at para 66 (**Appellant's Record, Tab 2**); Reasons for Judgment of the Federal Court of Appeal dated August 4, 2021 ("**FCA Reasons**") at para 49 (**Appellant's Record, Tab 4**).

or a passive participant whose actions can be manipulated by a new person or group of persons in order to utilize the losses of a corporation for their own benefit. He then rejected the Crown's position that the avoidance transactions were abusive, relying on the evidence of the series of transactions and his interpretation of the Investment Agreement.[31]

27. Justice Paris recognized that the fundamental issue before him was whether Matco had acquired effective control of the Appellant, thereby circumventing the object, spirit and purpose of s. 111(5) and related loss restrictions.[32] He concluded that a change in management, business activity, assets, liabilities, and corporate name are not markers of a change in effective control. Moreover, since the new shareholders under the IPO were not connected in any way for purposes of s. 111(5), the Appellant could have undertaken the recapitalization and restart transactions without Matco, and without the Investment Agreement. Since the IPO did not result in an acquisition of effective control, the Appellant could claim its tax attributes against income from a new business.[33] Ultimately, these findings of fact led the trial judge to conclude that the avoidance transactions did not amount to an abuse of the loss restrictions in ss. 111(5), 37(6.1) and 127(9.1).[34]

b. The Federal Court of Appeal Decision

28. The FCA overturned the Tax Court's decision by introducing and applying a new test for control under ss. 37(6.1), 111(5) and 127(9.1) pursuant to the GAAR.

29. Despite stating that it agreed with the Tax Court's conclusion on the object, spirit and purpose of s. 111(5), the FCA went on to "rearticulate" these conclusions to arrive at a new test for control under the *Act*: "actual control".[35] In doing so, the FCA relied on two indicators of government intent:

(a) a statement made in 1963 by the Minister of Finance when introducing an acquisition of control rule for the first time that the rule was aimed at the trafficking in the shares of companies with loss carryovers; and

---

[31] TCC Reasons at paras 134, 146–154, 157–160 and 162–166 (**Appellant's Record, Tab 4**).
[32] TCC Reasons at paras 140–144 (**Appellant's Record, Tab 2**).
[33] TCC Reasons at paras 147–151 (**Appellant's Record, Tab 2**).
[34] TCC Reasons at para 154 (**Appellant's Record, Tab 2**).
[35] FCA Reasons at paras 71–73 (**Appellant's Record, Tab 4**).

(b) an article written by a senior Department of Finance official in 1988 commenting that one of the objectives of the creation of the GAAR itself was to deal with the "unexpected" application of loss carryforwards.[36]

30. The FCA also looked to a statement from this Court in *Mathew*[37] that "the general policy of the *Act* is to prohibit the transfer of losses between taxpayers, subject to specific exemptions".[38] Ultimately, this led the FCA to conclude that:

(a) the object, spirit and purpose of s. 111(5) includes forms of *de jure* and *de facto* control;

(b) the actual control test is different from the statutory *de facto* control test in s. 256(5.1);

(c) the GAAR is intended to supplement the *Act* in order to deal with abusive tax avoidance; and

(d) it is not inconsistent to say that the object, spirit and purpose of s. 111(5) takes into account different forms of control even though the text of that provision is limited to *de jure* control.[39]

31. The FCA thus held that the object, spirit and purpose of s. 111(5) is to restrict losses where a person or group of persons "has acquired actual control over the corporation's actions whether by *de jure* control or otherwise."[40] Under this test of "actual control", the FCA found that the Tax Court had erred in concluding that the series of transactions was not abusive and that Matco had achieved "actual" control of the Applicant under the Investment Agreement,[41] and allowed the Crown's appeal.

PART II - ISSUES

32. This appeal raises the following issues:

---

[36] FCA Reasons at paras 42 and 79–80 (**Appellant's Record, Tab 4**).
[37] *Mathew v. Canada*, 2005 SCC 55 ("***Mathew***") at para 49.
[38] FCA Reasons at para 81 (**Appellant's Record, Tab 4**).
[39] FCA Reasons at para 83 (**Appellant's Record, Tab 4**).
[40] FCA Reasons at para 93 (**Appellant's Record, Tab 4**).
[41] FCA Reasons at paras 98 and 105 (**Appellant's Record, Tab 4**).

(a) Did the Federal Court of Appeal err in relying on the GAAR to conclude that "actual control" was Parliament's intended test under ss. 37(6.1), 111(5) and 127(9.1) of the *Act*? and

(b) Did the Federal Court of Appeal err in concluding, contrary to the trial judge's findings, that the avoidance transactions resulted in an abuse of ss. 37(6.1), 111(5) and 127(9.1) of the *Act*?

PART III - ARGUMENT

A. Standard of Review

33. In the first step of the abuse analysis, which involves determining the object, spirit and purpose of the applicable provisions of the *Act*, the applicable standard of review is correctness, as the object, spirit and purpose of the relevant provisions giving rise to a tax benefit is a question of law.[42] The determination of whether an avoidance transaction results in an abuse having regard to the object, spirit and purpose of the relevant provisions is a question of mixed fact and law. As this Court found in *Canada Trustco*, the applicable standard of review is palpable and overriding error, with the findings of the trial judge being entitled to deference:

> Provided the Tax Court judge has proceeded on a proper construction of the provisions of the *Act* and on findings supported by the evidence, appellate tribunals should not interfere, absent a palpable and overriding error.[43]

B. The Federal Court of Appeal erroneously applied the GAAR to create a new "actual control" test under ss. 37(6.1), 111(5) and 127(9.1) of the *Act*

a. Introduction to the GAAR

34. Parliament created the GAAR as an instrument to ensure that abusive tax planning does not frustrate the provisions of the *Act* and intentions of Parliament. The GAAR permits a court to deny the benefits of an arrangement that complies with the provisions of the *Act*, but frustrates or

---

[42] *Canada Trustco* at para 44.
[43] *Canada Trustco* at para 46.

defeats their object, spirit and purpose.[44] This Court has directed courts to apply the GAAR only where the abusive nature of the transactions at issue is clear.[45]

35. It is well-established that the GAAR applies when three conditions are met:

(a) there must be a "tax benefit" within the meaning of s. 245(1) of the *Act*;

(b) the tax benefit must result from an avoidance transaction or from a series of transactions that includes an avoidance transaction (ss. 245(2) and (3)); and

(c) the avoidance transaction or series results, directly or indirectly, in abusive tax avoidance in that it amounts to a misuse or abuse of the relevant statutory provisions (s. 245(4)).[46]

36. The only element at issue in this appeal is whether the Appellant's series of transactions resulted in abusive tax avoidance. The heart of the abusive tax avoidance analysis under the GAAR is the court's textual, contextual and purposive interpretation of the provisions of the *Act*. The first step is to determine the object, spirit and purpose (the "**OSP**") of the provisions that gave rise to the tax benefit. The second step is to determine whether the tax benefit achieved by the taxpayer frustrates or defeats that OSP.[47]

37. The burden of demonstrating the abuse of a provision falls on the Crown and any benefit of the doubt goes to the taxpayer.[48] This Court has long recognized that tax law should be certain, predictable and fair,[49] and the *Duke of Westminster* principle that taxpayers ought to be able to rely on the provisions of the *Act* when planning their affairs remains good law.[50] Parliament intends for taxpayers to take full advantage of the provisions of the *Act* that confer tax benefits. For this reason, the language of the GAAR itself indicates that the starting point is an assumption that the tax benefit conferred by the plain words of the *Act* is not abusive.[51]

---

[44] *Canada Trustco* at para 16.
[45] *Canada Trustco* at para 50; *Copthorne* at para 72.
[46] *Alta Energy* at para 31.
[47] *Alta Energy* at para 31.
[48] *Canada Trustco* at para 66, points 2 and 3.
[49] *Copthorne* at para 67.
[50] *Canada Trustco* at para 11; *Copthorne* at para 65; *Alta Energy* at para 29.
[51] *Canada Trustco* at paras 61–62; *Alta Energy* at paras 118–119.

38. In this case, a textual, contextual and purposive analysis reveals that Parliament has carefully crafted the loss restriction provisions in the *Act* to only deny the tax benefits of losses, SR&ED and ITCs in specific and clear instances. Those circumstances have always been determined by a certain and predictable test, whether it be the *de jure* control test, or some other bright line test. Parliament has never chosen to deny these tax benefits under a test that considers a wider range of facts and circumstances such as those allowed under the *de facto* control test.

39. The GAAR is not meant to disturb the certainty Parliament has drafted into a provision of the *Act*, but only to disallow *abusive* tax avoidance that frustrates that provision's purpose. Courts should not infuse the GAAR analysis with value judgments of what is right or wrong, or with their own theories about what tax law ought to be or ought to do.[52] A court's role is not to act as a protector of government revenues, but only to interpret Parliament's legislative intentions and determine whether they have been frustrated.

b. The FCA erred by searching for an overriding policy of the *Act* not rooted in its provisions.

40. The Tax Court properly articulated the OSP of the relevant provisions: the tax benefit of claiming losses, SR&ED and ITCs is restricted where *de jure* control of a corporation has been acquired by a new person or group of persons.[53] *De jure* control is the ability to control a corporation without any legal impediment. The restriction makes sense as an acquisition of control by a new person or group of persons is "the means by which Parliament has determined that a loss has notionally been transferred to an unrelated party".[54]

41. In conducting the first step of the analysis, the FCA failed to properly conduct the textual, contextual, and purposive analysis required to find the OSP and instead:

---

[52] *Alta Energy* at para 48.

[53] The meaning of a "group of persons" was considered in *Silicon Graphics Ltd. v. Canada*, 2002 FCA 260 at para 36, where the Court held that a group of persons requires a common connection that is more than a simple mathematical majority of shares by a random aggregation of shareholders in a widely held corporation.

[54] TCC Reasons at para 103 (**Appellant's Record, Tab 2**).

(a) searched for an overriding policy of the *Act* that was divorced from a unified textual, contextual, and purposive interpretation of the provisions at issue;

(b) conflated the object, spirit and purpose of the provisions with the broadest of policy statements, in direct contravention of this Court's admonition in *Canada Trustco*;

(c) eliminated the distinction between *de jure* and *de facto* control, contrary to this Court's decision in *Duha*; and

(d) supplemented the provisions of the *Act* by creating an actual control test found nowhere in the *Act*.

42. Instead of examining the historical evolution of Parliament's rules against loss trading under a unified textual, contextual, and purposive analysis, the FCA searched for an overarching policy (*i.e.*, the policy against loss trading) and then relied on this policy to supplement the legislation. Specifically, the FCA relied on (1) a statement made in 1963 by the Minister of Finance about the first iteration of an acquisition of control rule in the *Act*, and (2) an article written by a Department of Finance official in 1988 about the creation of the GAAR.[55]

43. In *Copthorne*, this Court specifically found that a court cannot rely on general policy statements to find a policy that is not rooted in the provisions of the *Act* itself.[56] This is just what the FCA did by relying on these general policy statements and the broad policy statement of this Court in *Mathew* to support creating a new test of actual control.

44. In relying on general statements as opposed to conducting a proper analysis of the provisions of the *Act*, the FCA ignored this Court's analysis of the *de jure* and *de facto* control tests in *Duha*. In particular, it blurred the distinction between the tests in contravention of the finding in *Duha* that if this test were to be changed, it must be left to Parliament to do so.[57] Despite this Court's invitation to Parliament to make such a change, Parliament has not altered *Duha's* definition of control for over 24 years. Given this inaction and its actions to clarify control throughout the *Act*, it is reasonable to infer that Parliament is satisfied that the meaning of control in *Duha* properly reflects the OSP of the section.

---

[55] FCA Reasons at paras 42 and 79–80 (**Appellant's Record, Tab 4**).
[56] *Copthorne* at para 118.
[57] *Duha* at para 52.

45. There is no dispute that the *Act* contains a general policy against loss trading between taxpayers who deal with each other at arm's length. The scope of this policy, however, must be discovered from specific provisions of the *Act*, as the abuse analysis under the GAAR cannot be divorced from the legislation.[58]

46. The FCA's decision has resulted in a new test for control that has no foundation in this Court's long-standing jurisprudence, and it has opened the door to future applications of the GAAR on an unprincipled basis. The FCA Reasons provide the Minister of Revenue *carte blanche* to recharacterize a broad swathe of everyday transactions whose purposes may be both commercial and tax-motivated by relying on broad statements of policy and unfettered by the text, context and purpose of Parliament's actual legislative choices. This erodes the certainty, predictability and fairness that Parliament intended in the provisions of the *Act* and which Parliament had no intention of undermining with the GAAR.[59]

C. Textual, Contextual and Purposive Analysis of 37(6.1), 111(5) and 127(9.1)

a. The text of the provisions reflects Parliament's intention to restrict loss trading on acquisitions of *de jure* control

47. Each of ss. 37(6.1), 111(5) and 127(9.1) restricts a taxpayer's ability to claim non-capital losses, SR&ED and ITCs where "control" of a corporation has been acquired by a person or group of persons. In *Duha*, this Court determined that the term "control" when used in an unqualified manner means *de jure* control, which it equated with effective control.[60] By contrast, when Parliament intends to apply the *de facto* control test, it uses the phrase "controlled directly or indirectly in any manner whatever".[61]

48. *De jure* control has long been understood as the ability of a shareholder to elect the majority of the board of directors. This has been the case in Canada since the 1964 case of *Buckerfield's*,[62]

---

[58] *Canada Trustco*, at paras 41–42.
[59] *Canada Trustco* at para 61.
[60] *Duha* at para 85.
[61] *Duha* at para 52.
[62] *Buckerfield's Ltd. v. Minister of National Revenue*, 1964 CarswellNat 351, [1964] C.T.C. 504 ("***Buckerfield's***") (**ABoA, Tab 13**).

and this Court has endorsed this definition in *Dworkin*[63] and in *Duha.*[64] This Court explained in *Duha* that insofar as *de jure* control seeks to ascertain who is in "effective control" of the affairs and fortunes of the corporation, it requires an investigation beyond the board of directors to the majority shareholder who can elect the majority of the directors.[65]

49. In *Duha*, this Court conducted what was tantamount to an object, spirit and purposive analysis of s. 111(5) and found that Parliament had chosen the *de jure* control test in s. 111(5) in large part because of the certainty and predictability it gives to taxpayers.[66] Effective control is determined through voting control because the governing corporate statute specifically provides that a corporation's affairs and fortunes are controlled by its board of directors. Therefore, the person with the ability to elect the majority of the board of directors under that corporate law is in effective control of the corporation.

50. While restricting *de jure* control to control over the board, *Duha* recognizes that effective control can arise from more than just voting rights and can arise from documents that affect control of the corporation pursuant to a corporate statute (which includes constating documents such as by-laws and unanimous shareholder agreements). Such documents affect *de jure* control because they are binding in that parties are not free to act other than in accordance with them. Thus if a constating document affects the power of the board to control the corporation, it can be considered in determining who holds effective control of a corporation.[67] This can be contrasted with ordinary contracts which are not taken into account as determinants of *de jure* control, although they may be considered as indicia of *de facto* control.[68] *Duha's* notion of control, as Justice Paris found, is central to how s. 111(5) (and ss. 37(6.1) and 127(9.1)) operate.[69]

51. Parliament has employed the test of "control" in over 90 provisions of the *Act*, distinguishing it from *de facto* control, which is specified in the *Act* by the words "controlled

---

[63] *Minister of National Revenue v. Dworkin Furs (Pembroke) Ltd. et al.*, [1967] S.C.R. 223 ("***Dworkin***") at para 227.
[64] *Duha* at para 35.
[65] *Duha* at para 36.
[66] *Duha* at para 52.
[67] *Duha* at paras 42 and 49–51.
[68] *Duha* at para 51.
[69] TCC Reasons at paras 103-104 and 143 (**Appellant's Record, Tab 2**).

directly or indirectly in any manner whatever" and employed in over 18 provisions. The trial judge recognized the importance of Parliament's choice of control test when he stated:

> …Parliament has chosen a particular mechanism, an acquisition of control, to be used to identify when a tax attribute is considered to be transferred to an unrelated taxpayer and has made that mechanism an integral part of the loss-streaming rules. That element cannot be read out of the abuse analysis under the guise of a general policy argument.[70]

52. In choosing its words in ss. 37(6.1), 111(5) and 127(9.1), Parliament has carefully chosen its test. The courts should not rewrite Parliament's deliberate choice of test under the guise of the GAAR unless the Crown can clearly show that the OSP of ss. 37(6.1), 111(5) and 127(9.1) is to restrict taxpayers from claiming their losses, SR&ED and ITCs where some other indicator of control has been acquired.

b. The context of the provisions demonstrate Parliament's deliberate choice of a *de jure* control test

i. Absent an acquisition of control Parliament provides full deductibility of losses, SR&ED and ITCs

53. Parliament's approach is to provide the tax benefit of full deductibility to taxpayers. Subsections 37(6.1), 111(5) and 127(9.1) are, put simply, restrictive anti-avoidance provisions that Parliament has specifically crafted to restrict what are otherwise permissible deductions under the *Act*.

54. The starting point of a contextual analysis therefore must consider the operative provision in s. 111(1), where Parliament provides for the scheme allowing a taxpayer to deduct losses against any source of income whatsoever. Similarly, ss. 37(1) and 127(9) are the operative provisions that allow taxpayers to deduct SR&ED and claim ITCs generated by scientific research and experimental development conducted in Canada, again against any source of income. All of these tax attributes are unrestricted, meaning that taxpayers are entitled to claim them regardless of whether they change the name of their business, their business activities, their management teams, their assets, or their investors.[71]

---

[70] TCC Reasons at para 143 (**Appellant's Record, Tab 2**).
[71] Changes in investors are allowed, so long as there is no acquisition of control.

55. The Tax Court properly acknowledged s. 111(1) as the starting point of its contextual analysis, recognizing that Parliament intends to allow taxpayers to deduct losses from one source of income against income from another.[72] This context is important, because it demonstrates Parliament's intention to support Canadian taxpayers who invest in commercial business activities.[73] The FCA failed to acknowledge the deduction scheme in which the specific restrictions in ss. 37(6.1), 111(5) and 127(9.1) operate, focusing solely on the anti-avoidance rules[74] and losing sight of the fact the GAAR analysis must occur in the context of provisions that work together.[75] The scheme of the *Act* in which the loss restrictions operate confirms Parliament's intent to apply restrictions only on an acquisition of *de jure* control.

ii. Parliament has chosen *de jure* control for loss trading despite having a menu of other control tests

56. In this context of the general ability to claim losses, SR&ED and ITCs, those tax attributes become restricted under ss. 37(6.1), 111(5) and 127(9.1) when a corporation experiences an acquisition of control. The fact that Parliament has consistently maintained *de jure* control as the test for restricting such losses, SR&ED and ITCs, even while creating a menu of other control tests under the *Act*, demonstrates Parliament's clear understanding of different forms of control and intention to restrict those tax attributes only in specific circumstances.

57. Parliament's first test for loss trading was based not on control, but on changes to shareholdings. In 1958, when losses from one business first became deductible against income from other businesses, Parliament enacted a loss restriction rule that denied the deduction of losses

---

[72] TCC Reasons at para 98 (**Appellant's Record, Tab 2**).
[73] Canada describes the SR&ED program as using "tax incentives to encourage Canadian businesses of all sizes and in all sectors to conduct research and development in Canada". It is a specific incentive scheme by Parliament that provides "more than $3 billion in tax incentives to over 20,000 claimants annually, making it the single largest federal program that supports business R&D in Canada" (April 28, 2022), Canada, *Scientific research and experimental development tax incentive – Overview*.
[74] FCA Reasons at para 90 (**Appellant's Record, Tab 4**).
[75] *Copthorne* at para 91.

if a corporation experienced a 50% change in ownership during the year.[76] This original test, however, was abandoned in 1972 when Parliament stopped testing for simple changes in shareholdings and instead focused its attention on what it saw as the true mischief—acquisitions of control where a new person acquires the unconstrained, legal ability to control a corporation's losses. By 1972, the sole test applicable to restrict a corporation's losses was the acquisition of control test.[77] This has remained the case for the last fifty years.[78]

58. Most notable on the menu of control tests is the *de facto* control test defined in s. 256(5.1). *De facto* control is broader than *de jure* control. It allows a court to look beyond legal sources of control under the relevant corporate law to consider all of the surrounding facts to determine who is "in fact" in control of the corporation. In *Duha*, Iacobucci J. contrasted *de jure* to *de facto* control and specifically found that Parliament "has now recognized the distinction between *de jure* and *de facto* control, adopting the latter as the new standard for the associated corporation rules". He further found that Parliament had rejected the *de facto* standard in s. 111(5) because it involves ascertaining control in fact, which would require considering a myriad of indicators apart from the corporation's governing statute and constating documents.[79]

59. As the Tax Court described in *Lyrtech*, the creation of the *de facto* control test in 1988 was a specific legislative response to the interpretation of "control" by the courts:

> In light of the case law, Parliament has had to make many clarifications with respect to the concept of control in order to reach specific legislative goals. Thus, since September 13, 1988, when subsection 256(5.1) was introduced, the *Act* is clear as to which are the provisions that specifically refer to the concept of *de jure* control as opposed to those that involve, rather, the application of *de facto* control.[80]

---

[76] Subsections 27(1), 27(1)(e), and 27(5) of the Consolidated *Income Tax Act*, RSC 1952, c 148 (following 1958 amendments) ("***ITA 1958***") (**ABoA, Tab 2**).
[77] Subsections 111(1) and (5) of the *Income Tax Act*, SC 1970-71, c 63 (**ABoA, Tab 3**).
[78] A Nijhawan, "When is 'Loss Trading' Permissible? A Purposive Analysis of subsection 111(5)", *Report of Proceedings of the Sixty-Seventh Tax Conference*, 2015 Conference Report (Toronto: Canadian Tax Foundation, 2016) ("**Nijhawan**") at 9:5–9:6 (**ABoA, Tab 18**).
[79] *Duha* at paras 52 and 58.
[80] *Lyrtech RD Inc. c. R.*, 2013 TCC 12 at para 14, aff'd 2014 FCA 267 at para 36.

60. When Parliament defined the phrase "controlled, directly or indirectly in any manner whatever" in 1988, it indicated the need for a control test other than the *de jure* test as interpreted by the courts—and it expressly created such a test and applied it to some provisions and not others.

61. Parliament's continued understanding of the control tests is demonstrated by the 2016 case of *McGillivray*, where the FCA interpreted the scope of *de facto* control in a limiting manner.[81] Parliament responded within one year of that decision, enacting new s. 256(5.11), which requires that the scope of factors considered for *de facto* control not be so limited.[82]

62. Another control test created by Parliament is the substantial equity test in s. 256(1.2)(c), which was enacted at the same time as the *de facto* control test. This provision deems control to exist where a person acquires shares representing more than 50% of the fair market value of all the issued and outstanding shares of the capital stock of a corporation for certain purposes. Notably, Parliament chose not to apply this test to the loss restriction provisions.

63. Finally, the *Act* contains a detailed set of control rules in s. 251(5), which defines control by groups and incorporates tests for determining control where a broad range of options and rights exist. These rules do not apply, and have never applied, to the loss restriction provisions of the *Act*.

64. The menu of control tests in the *Act* shows that Parliament is well aware of the different forms of control that can be exercised over a corporation. Importantly, Parliament enacted several of these control tests (including the *de facto* control test) at the same time it enacted the GAAR itself (*i.e.*, during the tax reform of 1988). At that time, Parliament turned its mind to the question of control throughout the *Act*. It created new control tests for specific purposes[83] and retained the *de jure* control test for others. Importantly, Parliament not only applied the *de facto* control test to

---

[81] *McGillivray Restaurant Ltd. v. R.*, 2016 FCA 99.
[82] Canada, Department of Finance, *Tax Measures Supplementary Information* (March 22, 2017); Canada, Department of Finance, *Explanatory Notes Relating to the Income Tax Act, Excise Tax Act and Related Legislation* (October 27, 2017).
[83] For instance, in ss. 256(5.1) and 256(1.2)(c).

existing provisions in the *Act*, but also removed it from others, demonstrating that Parliament understood the difference between *de facto* and *de jure* control and intended that difference.[84]

iii. Parliament's modifications to the acquisition of control test through deeming rules demonstrates that it acts specifically and carefully

65. In certain circumstances, Parliament has modified the control test to ensure that loss restrictions occur even where *de jure* control has not been technically acquired. Each of these modifications has been carefully crafted as an explicit and clear deeming rule that affects whether or not an acquisition of "control" has occurred.

66. An example of this is s. 256(8), which Parliament added to the *Act* in 1983 to address options and rights to shares. Subsection 265(8) deems a person who has certain rights in respect of shares to be in the same position as if those rights had been exercised, but only if one of the main purposes of those rights was to avoid the loss restriction rules. The effect of s. 256(8) is to determine whether a person has avoided an acquisition of control by having, but not exercising, rights that, if exercised, would result in *de jure* control.

67. The Tax Court in this case conducted an OSP analysis of s. 256(8), concluding that its purpose was to allow the Minister to look beyond the strict voting rights of a corporation to determine who in substance has control over the voting rights of the shares of the corporation.[85] Justice Paris correctly noted that every one of the rights contemplated under s. 256(8) relates to the shares of a corporation. Notably, however, s. 256(8) does not consider factors unrelated to shares or their voting rights.

---

[84] Canada, Department of Finance, *Explanatory Notes* (Ottawa: Finance, June 1988) at 30, 127, 149, 165-166, 169, and 502-504 ("***1988 Explanatory Notes***"). The 1988 Explanatory Notes explain the creation of the de facto test and apply it to the following list of sections: 24(2); 40(2)(a), (e) and (h); 44(7)(b); 87(2)(kk); 54(i); 83(2.2) and (2.4); 89(1)(b); 89(1.1); 85(4) and (5.1); 95(6)(b); 125(7)(b); 127.1(2); 241(4)(j); and 256(1)-(2.1) (*1988 Explanatory Notes* at 502-504). They explain the removal of the words "directly or indirectly in any manner whatever" from the following sections: 18(1)(m)(iii), 69(6)(c), 69(7)(c), 85.1(2), 89(1)(f), and 95(1)(a) (*1988 Explanatory Notes* at 30, 127, 149, 165-166, and 169) (**ABoA, Tab 4**).

[85] TCC Reasons, at paras 112–115 (**Appellant's Record, Tab 2**).

68. Another example is s. 256(7), which Parliament enacted in 1977 to facilitate the preservation of losses in mergers and acquisitions.[86] This provision deems control to be acquired, or not acquired, in amalgamations and reverse takeover transactions[87] on the basis of clear numerical tests.[88] Similar to s. 256(8), the deeming provisions in s. 256(7) consider share ownership only, and there is no consideration of any other facts or circumstances.

69. Finally, in 2013, Parliament enacted s. 256.1 to deem an acquisition of control where a person acquires a significant amount (*i.e.*, more than 75%) of the equity in a corporation but does not acquire *de jure* control. This provision was enacted after the Appellant's transactions and thus does not apply to this case. However, it is notable that Parliament enacted s. 256.1 to address transactions like the Appellant's, and in doing so it did not change the meaning of control as interpreted in *Duha.*

70. Parliament had known about recapitalization and restart-type transactions (*i.e.*, transactions where a new investor acquires more than 50% of the equity value of a company while not acquiring *de jure* control) as early as 2003, when the Canada Customs and Revenue Agency (as it then was) first granted a taxpayer ruling that confirmed the GAAR would not apply to such a transaction (the "**Hemosol Ruling**").[89] Ten years later, after an apparent change of heart, Parliament addressed such transactions by enacting s. 256.1.

71. Parliament's response in enacting s. 256.1 demonstrates yet another careful and deliberate decision to expand the conditions under which "control" exists, deeming control where three specific, expressly articulated criteria are met. Importantly, Parliament did not create a test that

---

[86] Brian Arnold and David Poynton, "Tax Treatment of Losses on Amalgamation and Winding-up" (1978) 26:4, *Canadian Tax Journal* at 444-445, 459 (**ABoA, Tab 19)**.

[87] The deemed control rule applied to amalgamations from inception in 1977, but was not extended to reverse takeovers until 1988.

[88] The tests in s. 256(7) ensure that a smaller corporation experiences an acquisition of control (and thus the loss restrictions apply) when it mergers with or acquires a larger corporation.

[89] Canada Revenue Agency Ruling 2003-0031823, "Transfer of a business by a shareholder" (2003) (**ABoA, Tab 14**). *See also* Canada Revenue Agency Ruling 2004-0056501, "Transfer of business" (2004) (**ABoA, Tab 15**); Canada Revenue Agency Ruling 2004-0069151R3, "Transfer of a business" (2004) (**ABoA, Tab 16**); Ontario Securities Commission, "In the matter of Hemosol Inc. MRRS Decision Document," (March 17, 2004).

considers a broad range of factors, such as *de facto* control or, as the FCA has done in this case, it did not create an "actual control" test.

c. The purpose of the provisions is to restrict loss trading in a certain and predictable manner

i. The legislative history of the provisions demonstrates Parliament's purpose

72. Since 1919, Parliament has developed its policy with respect to loss deductions and restrictions on loss trading. The Tax Court has described the legislative and jurisprudential history as "a lengthy story of ebb and flow".[90] Each extension of the loss restrictions by Parliament has been measured by reference to *de jure* control. Moreover, each enactment has occurred by way of a certain, predictable test. At no point has Parliament indicated that any element of factual control is relevant to the loss restrictions in ss. 37(6.1), 111(5) and 127(9.1).

73. With the inception of the *Income War Tax Act*, losses were simply not deductible, and taxes were levied on income on a per year basis.[91] Over time, Parliament has repeatedly expanded loss deductibility by: providing carryforwards and carrybacks, allowing losses to be deducted against income from other sources, and facilitating corporate mergers and acquisitions involving companies with accrued losses. These measures have provided certainty to taxpayers who engage in productive business activities in Canada.

74. At the same time, Parliament has enacted targeted measures to curtail loss trading. Loss-restrictions have been consistently aimed at transactions that do not promote new economic activity but instead allow a person with known or expected income to simply access another person's losses.

75. The evolution of the *Act* is particularly informative to determining Parliament's object, spirit and purpose of the provisions. This Court has confirmed that "[t]he use of legislative history as a tool for determining the intention of the legislature is an entirely appropriate exercise."[92] As *Sullivan* notes:

> …the court…retraces the steps of the legislative drafter, examining the relationship among provisions to surmise the overall plan. It

---

[90] *MMV Capital Partners Inc. v. The Queen*, 2020 TCC 82 ("***MMV Capital***") at para 77.
[91] Nijhawan at 9:5 (**ABoA, Tab 18**).
[92] *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 S.C.R. 27 at para 31.

> attempts to discover why each provision was included and the contribution each makes toward implementing the legislature's goals.[93]

ii. The origins of Canadian loss restrictions

76. Prior to 1958, loss deductions were restricted to the same business. A taxpayer could carry losses forward and back[94] but could apply them only against income from the business that generated the losses. This changed in 1958 when Parliament expanded the deductibility of losses to allow taxpayers to deduct them on an unrestricted basis, meaning that a taxpayer with more than one business could deduct its business losses against income from any other business. This remains the case today.

77. At the same time Parliament enacted its first loss trading rule. This new rule restricted losses where more than 50% of the shares of a corporation were acquired by new persons during the year, and the business that created the losses ceased to be carried on. This rule also contained a "same business" test that preserved the losses to the extent that the corporation continued to carry on the same business in which the losses arose.[95]

78. Five years later, in 1963, Parliament amended the loss restriction rule to include an acquisition of control test in addition to the "more than 50% of the shares" test. The reason for this amendment was to close a "loophole" whereby a person could acquire legal voting control of a corporation, but avoid acquiring more than 50% of the total shares of the corporation by creating different classes of shares.[96]

---

[93] Ruth Sullivan, *The Construction of Statutes*, 6th ed. (Markham, Ont.: LexisNexis Canada, 2014) at 10 of 27 (**ABoA, Tab 20**).

[94] Loss carryforwards were introduced in 1942 with a one-year carry-forward. In 1944, this carryforward was extended to three years and a carryback of one year was created. In 1949, the carryforward was extended to five years.

See Nijhawan at 9:5 (**ABoA, Tab 18**); Gordon Bale, "The Tax Reform Bill and the Problem of Income Fluctuation" (1971) 19:6 *Canadian Tax Journal* at 487-488 (**ABoA, Tab 21**).

[95] Subsections 27(5) of the *ITA 1958* (**ABoA, Tab 2**).

[96] Sections 27(1), 27(1)(e), 27(5), 27(5a) of the Consolidated *Income Tax Act*, RSC 1952, c 148 (following 1963 amendments) ("***ITA 1963***") (**ABoA, Tab 5**); Heward Stikeman, A. V. Neil, and George Tamaki, eds., *Canada Tax Service* (Toronto: De Boo, 1972) (looseleaf) at 27-167–27-168 (**ABoA, Tab 23**).

79. By this time, Parliament recognized that control was the key to the mischief it sought to address, as opposed to simple changes in numerical share ownership. Soon after, the Exchequer Court affirmed the meaning of "control" (*i.e.*, in 1964) in *Buckerfield's* as *de jure* and not *de facto* control.[97] This Court subsequently affirmed *Buckerfield's* finding on the meaning of "control" in *Dworkin*[98] in 1967 and in *Duha* in 1998. In each case, this Court endorsed the *de jure* control test and rejected *de facto* control.

80. This early version of the loss restriction rule is the predecessor of s. 111(5), and the similarity of many of its characteristics to s. 111(5) helps demonstrate the OSP of the provisions at issue:

(a) Losses were restricted where an acquisition of control occurred, or where more than 50% of the shares was acquired by a new person or persons. This was Parliament's recognition that a person with more than 50% of the voting shares can control a corporation for their own benefit.

(b) Losses were eliminated if the corporation's loss business ceased to be carried on. This was Parliament's recognition that losses are restricted where a new controlling person simply sought to use the losses, but not carry on business.

iii. The modernization of Canadian loss restriction rules

81. Since the 1960s, Canada has taken varying approaches to the application of tax policy to the Canadian economy. Notwithstanding its shifting approaches, Parliament has been consistent in basing its tax loss restriction provisions on the *de jure* control standard. Each amendment to the restrictions by Parliament throughout history has been measured by reference to *de jure* control and effected by way of a certain and predictable test. At no point in its legislative history has Parliament indicated that any elements of factual control are relevant to the loss restrictions.

82. In its 1969 White Paper, the Department of Finance announced sweeping systemic reforms to Canada's tax system in response to the recommendations of the *Royal Commission on Taxation.* Parliament began to actively use the tax system to pursue economic and social objectives.[99] In the

---

[97] *Buckerfield's* at para 10 (**ABoA, Tab 13**).
[98] *Dworkin* at 227.
[99] Canada, Department of Finance, *Proposals for Tax Reform* (Ottawa: Department of Finance, November 7, 1969) ("**1969 White Paper**") at 5-7 (**ABoA, Tab 6**).

1970s, tax incentives abounded, as tax policy was considered to be an efficient economic lever to create growth in the Canadian economy.[100] At this time, ITCs were introduced for a wide range of purposes, including for SR&ED activities.[101]

83. Also, the loss restrictions became more targeted as the former 50% change in shareholdings test was dropped.[102] At the same time, Parliament eased the loss restrictions to support Canadian merger and acquisition transactions, allowing losses to survive and be carried forward through amalgamations and wind-ups of corporations.[103]

84. The acquisition of control rule was adopted in other sections of the *Act* to restrict other tax attributes such as capital losses and the capital dividend account (but not for SR&ED or ITCs).[104] Parliament also created complex rules that deem an acquisition of control in certain amalgamations.[105]

85. By the early 1980s, Canadian companies had built up an enormous inventory of undeducted losses and other tax attributes as a result of a combination of tax incentives delivered in the 1970s and a significant recession in the Canadian economy starting in 1980.[106]

86. Parliament proposed to significantly tighten the loss trading rules in 1981 by restricting the carryforward of losses after an acquisition of control to income from that loss business only. However, after significant criticism, it instead adopted the "same or similar" business test in 1982, restricting the deduction of losses after an acquisition of control to income from the loss business

---

[100] David Holland and Alain Castonguay, "The Corporate Income Tax: Preliminary Results on the Impact of Tax Reform," *Report of Proceedings of the Forty-Third Tax Conference*, 1991 Conference Report (Toronto: Canadian Tax Foundation, 1992) ("**Holland & Castonguay**") at 20:2 (**ABoA, Tab 24**).
[101] Holland & Castonguay at 20:2 (**ABoA, Tab 24**); Canada, *Evolution of the SR&ED Program–a historical perspective*.
[102] Subsection 111(5) in *Income Tax Act*, SC 1970-71, c 63 (**ABoA, Tab 3**).
[103] Subsections 87(2.1) and 88(1.1). See *An Act to amend the statute law relating to income tax*, SC 1977-78, c 1, ss. 42(6) and 43(11), adding ss. 87(2.1) and 88(1.1) ("***ITA 1977-78***") (**ABoA, Tab 7**).
[104] Subsection 89(1.1), added by s. 44 of the *ITA 1977-78*, and s. 111(4). (**ABoA, Tab 7**).
[105] Subparagraphs 256(7)(b)(ii) and (iii), added by s. 99 of the *ITA 1977-78* (**ABoA, Tab 7**).
[106] Holland & Castonguay, 20:3 (**ABoA, Tab 24**).

that created them, or a similar business, so long as the loss business continued to be carried on.[107] This rule continues to this day.

iv. 1988 Tax reform: Parliament codifies control throughout the *Act* while enacting the GAAR

87. Significant tax reform occurred again in the late 1980s. In a reversal of the policy of the 1970s, Parliament now sought to eliminate the plethora of targeted tax incentives and instead broaden the Canadian tax base and lower tax rates overall.[108] ITCs for all activities other than SR&ED and certain regional businesses were eliminated at this time.

88. The tax reform of 1988 brought about: (1) the application of the loss restrictions to new areas of the *Act;* and (2) a proliferation of other control tests for other purposes. The acquisition of control test was newly applied to restrict SR&ED and ITCs, as well as to mergers and acquisitions structured as "reverse takeovers",[109] demonstrating Parliament's intent to apply the *de jure* control test to restrict losses in these new circumstances.

89. At the same time, Parliament enacted the *de facto* control test in s. 256(5.1) and the economic control test in s. 256(1.2)(c). As part of enacting these new control tests, Parliament took the opportunity to revisit the provisions of the *Act* that relied on control and expressly applied the *de facto* control test to numerous provisions by surgically removing the words that mark *de facto* control where it did not wish this broader control test to apply:

> Several provisions of the *Act* have been amended, as a consequence of the introduction of subsection 256(5.1), to delete therefrom the words "directly or indirectly in any manner whatever," thus ensuring that *de facto* control is not applicable in the case of corporations referred to in these provisions.[110]

---

[107] Andrew Trotta, "Business Losses–The New Rules, Taxation of Corporate Reorganizations" (1982) 30:6 *Canadian Tax Journal* at 920 (**ABoA, Tab 25**).
[108] Canada, Department of Finance, *Tax Reform 1987: Income Tax Reform* (Ottawa: Finance, June 1987), at 1–2, 17 and 24 (**ABoA, Tab 8**).
[109] See amendments to add s. 127(9.1) in *An Act to amend the Income Tax Act and related statutes*, SC 1986, c 6, s 71(15) adding ss 127(9.1) and (9.2) (**ABoA, Tab 9**); s. 37(6.1) in *An Act to amend the Income Tax Act, a related Act, the Canada Pension Plan and the Unemployment Insurance Act*, SC 1987, c 46, s 11, adding s 37(6.1) and amending s 127(9.1) (**ABoA, Tab 10**); and s. 256(7)(c) in *Income Tax Amendments Act, 1997*, SC 1998, c 19 (**ABoA, Tab 11**).
[110] *1988 Explanatory Notes* at 503. See also the list of provisions at footnote 85 (**ABoA, Tab 4**).

90. It is clear therefore that in 1988 Parliament: (1) turned its mind to the meaning of control within the Act and created the *de facto* control test; while (2) simultaneously making a determination of which provisions of the Act would be subject to *de facto* versus *de jure* control; and (3) at the same time applied the *de jure* control test to create new loss restriction provisions (i.e. those applicable to SR&ED, ITCs, and reverse takeovers).

91. The GAAR itself was created as part of this tax reform. The enactment of the GAAR in the same legislative package where Parliament clarified the distinction between "control" and "controlled, directly or indirectly, in any manner whatever" throughout the *Act* is strong evidence that Parliament did not intend to rely on the GAAR to eliminate the distinction between *de jure* and *de facto* control for loss restriction purposes. Accordingly, the FCA erred in finding that the GAAR was a response to *Duha*.

v. Parliament has not indicated a change in its intentions post tax reform

92. Since the tax reform of 1988, Parliament has done very little to the loss utilization rules, other than to increase the number of years during which losses could be carried forward from 7 years to 20 years.[111] Parliament has also done very little to the loss restriction provisions, other than to enact s. 256.1 in 2013 in response to tax planning structures where a new investor acquires significant equity but not voting control of a corporation.[112]

93. In 1998—ten years after the tax reform of 1988—*Duha* definitively settled the meaning and scope of *de jure* control under the *Act*. Parliament has taken no steps in response to that decision.

94. It is clear therefore that Parliament has engaged in a careful balancing act as it has developed the loss restriction provisions, endeavouring to ensure these restrictions do not discourage investment and business activity in Canada. Parliament has consistently provided certain and predictable criteria in its loss restriction provisions, which balance its intent to restrict loss trading against its desire to ensure that Canadian businesses are not inappropriately affected.

---

[111] See s 57 in *Budget Implementation Act*, 2006, SC 2006, c 4, s 57(1) amending s 111(1)(a) (**ABoA, Tab 12**).

[112] Canada, Department of Finance, *Explanatory Notes* (Ottawa: Finance, October 2013), excerpts at 138–139 (**ABoA, Tab 1**).

D. The FCA's new "actual control" test eliminates the distinction between *de jure* and *de facto* control

95. The FCA's creation of a new judge-made test for "actual control" ignores *Duha* and Parliament's intent to create certainty throughout the *Act*, well beyond ss. 37(6.1), 111(5) and 127(9.1). This is evidenced by the significant amount of criticism from the Canadian tax community since the decision was released.[113]

96. What the FCA means by "actual control" is unclear. The FCA Reasons provide no guidance on the scope of this new test, other than to state that it contains forms of both *de jure* and *de facto* control, but differs from the statutory *de facto* control test. Without identifying what "forms" of *de jure* and *de facto* control are included in the new test, and how it differs from the existing tests, taxpayers cannot apply this new standard with any certainty.[114]

97. The "actual control" test, in contrast to the *de jure* control test, seemingly requires a court to consider numerous factors from different sources. This Court specifically found in *Duha* that a test that required a court to consider "a myriad of indicators" was not appropriate in the context of s. 111(5), as it removes the certainty that Parliament intended in that provision.[115] Moreover, a textual, contextual, and purposive analysis of the loss restriction provisions reveals that Parliament never intended for courts to consider factors other than those that relate to shares and voting rights associated with shares.

98. In *Duha*, this Court explained that *de jure* control encompasses only those limitations that affect a person's ability to act as a free actor, such as those imposed by constating documents. Limitations that are imposed by ordinary contracts (such as the Investment Agreement) are not considered because they are freely agreed to by the shareholders and are not at all inconsistent

---

[113] See, for instance, Steve Suarez, "Taxpayer Seeks to Appeal Anti-Avoidance Case to Supreme Court of Canada" (September 27, 2021) *Tax Notes International* (**ABoA, Tab 26**); Mark Jadd and Joel Nitikman, Q.C., "The GAAR Analysis in Deans Knight: Apparently a cigar is not always just a cigar" (2021) 24:2 *Tax Litigation* (**ABoA, Tab 27**); Brian Nichols and Kelsey Horning, "Canada: Deans Knight Intersects Bill C-208: The Meaning of Control And Implications For Intergenerational Transfers" (September 16, 2021) *Mondaq* (**ABoA, Tab 28**); Ian Burns, "Legal expert says appeal decision 'introduces quite a bit of uncertainty' for tax professionals" (August 16, 2021) *The Lawyer's Daily* (**ABoA, Tab 29**); Richard W. Pound, Q.C., *Pound's Tax Case Notes* (September 24, 2021) (**ABoA, Tab 30**).

[114] FCA Reasons, at para 83

[115] *Duha* at para 58.

with their *de jure* power to control the company.[116] Contrary to this, the FCA relied on the restrictions under the Investment Agreement when determining whether Matco acquired control of the Appellant.

99. Parliament created the *de facto* control test for the very reason that in some circumstances it wishes for a myriad of factors to be considered that exist apart from the corporation's governing statute and constating documents. The FCA now asserts that this forms part of the OSP of the *de jure* control test, when in fact, the consideration of these factors is the very reason behind Parliament's creation of the *de facto* control test. Moreover the FCA's actual control test ignores the fact that actual control has been equated with *de facto* control both by this Court in *Duha*,[117] and by Parliament itself in the *1988 Explanatory Notes* to s. 256(1), which state that: "…Such manner of control is sometimes referred to as de facto or actual control".[118]

100. This Court has explained that the GAAR was enacted as a "provision of last resort",[119] and that it cannot apply unless the abuse is clear. There is no clear abuse in this case. The Tax Court, a highly specialized court that is uniquely tasked with interpreting the *Act*, proceeded with a proper analysis of the provisions of the *Act* to find that the GAAR did not apply. The FCA erred in intervening and using the GAAR to jettison this decision, replacing it with an amorphous test for control that finds no support in the provisions of the *Act* or the jurisprudence of this Court.

E. The FCA erroneously interfered with the trial judge's findings

a. Introduction

101. Even if the textual, contextual, and purposive analysis of the loss restriction provisions leads to a conclusion that the Tax Court was wrong, and Parliament intended that the OSP of ss. 37(6.1), 111(5) and 127(9.1) embody an "actual control" test or some test that is less certain than *de jure* control, the Appellant's series of transactions would still not be abusive tax avoidance under the GAAR.

102. The FCA found abusive tax avoidance by focusing inordinately on the Investment Agreement, instead of considering the Appellant's entire series of transactions as the Tax Court

---

[116] *Duha* at paras 42 and 49.
[117] *Duha* at para 49.
[118] *1988 Explanatory Notes* at 496 **(ABoA, Tab 4**).
[119] *Canada Trustco* at para 21.

did. The FCA found that Justice Paris had committed a palpable and overriding error in interpreting the Investment Agreement and substituted its own interpretation of the contract. In doing so, the FCA:

(a) effectively conducted a *de facto* control analysis;

(b) treated the Investment Agreement as a constating document that affected legal control instead of as an ordinary contract, contrary to *Duha*;

(c) failed to grant appropriate deference to the Tax Court's interpretation of the Investment Agreement, which was based on clear and unambiguous text, had been informed by findings of credibility, and was supported by the evidence at trial; and

(d) applied a correctness standard to the trial judge's interpretation of the Investment Agreement, and in any event misinterpreted its essential terms.

103. Justice Paris heard a week of evidence, accepted the testimony of the Appellant's witnesses, reviewed over 100 exhibits, considered the factual matrix surrounding the Investment Agreement, and found that Matco never acquired *de jure*, or effective control of the Appellant. Nevertheless, the FCA overturned the Tax Court's finding by isolating certain provisions of the Investment Agreement and reweighing the evidence. This was improper. An appellate court is not entitled to reassess the evidence and substitute its own interpretation. In doing so, the FCA failed to properly apply the standard of palpable and overriding error and virtually ignored the trial evidence.

b. Palpable and overriding error is "a beam in the eye"

104. The palpable and overriding error standard is exacting and highly deferential. It requires an appellate court to defer to the privileged position of the trial judge to make determinations based on the entirety of the evidence. It confines an appellate court's investigation into a trial judge's findings to whether there is support for the findings in the evidence.[120] It does not permit an appellate court to overturn a trial judge because the appellate court would accord more weight to certain pieces of evidence, would draw different inferences, or would interpret an agreement differently.[121] As this Court recently put it:

---

[120] *Housen v. Nikolaisen*, 2002 SCC 33 ("***Housen***"), *Salomon v. Matte-Thompson*, 2019 SCC 14 ("***Salomon***") at para 112.
[121] *Salomon* at para 110; *Nelson (City) v. Mowatt*, 2017 SCC 8 at para 3.

> …a palpable and overriding error is in the nature not of a needle in a haystack, but of a beam in the eye. And it is impossible to confuse these last two notions...[122]

105. In order to find a palpable and overriding error the appellate court must show why and in what respect a particular finding is marred with a "crucial flaw, fallacy, or mistake".[123] This standard applies to appellate review of a trial judge's interpretation of a contract. In *Sattva*, Justice Rothstein found that issues of contractual interpretation were subject to the palpable and overriding error standard because courts must have regard to the factual matrix (or surrounding circumstances of the contract); issues of contractual interpretation are not questions of law, rather they are questions of mixed fact and law that have limited impact beyond the parties to the dispute.[124] In a case like this one involving the specialist Tax Court's interpretation of a complex commercial agreement based on 5 days of *viva voce* evidence, the rationale for deference is strong.

c. The Federal Court of Appeal's search for a needle in a haystack

106. In *Salomon*, Justice Côté found that:

> Put another way, it would be inappropriate for the appellate court to conduct its own independent assessment of the evidence and then to take note of points of disagreement with the trial judge's findings and hold that those findings result from "palpable and overriding errors" in order to justify intervening (citations omitted). That would be not a review for error, but a disguised rehearing, which is not the proper role of an appellate court.[125]

107. This is what the FCA did here. It did not focus on the trial judge's reasons, but engaged in its own independent assessment of certain provisions of the Investment Agreement, noted points of disagreement with the trial judge, and then found that those points of disagreement amounted to a palpable and overriding error. In doing so, the FCA reweighed the evidence and failed to consider the factual matrix of the Investment Agreement, which emerged through several days of *viva voce* evidence.

---

[122] *Hydro-Québec c. Matta*, 2020 SCC 37 ("***Matta***") at para 33.
[123] *Salomon* at para 109 (Côté in dissent but not on this point).
[124] *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53 ("***Sattva***") at paras 46-51.
[125] *Salomon* at para 113.

108. This error is apparent in the FCA's approach to its analysis. The palpable and overriding error that the FCA claimed to identify was that the Tax Court's conclusion that the Investment Agreement did not give Matco effective control over the actions of the Appellant was "inconsistent with the terms of the Investment Agreement".[126]

109. There are several errors here. First, the FCA, in its search for an error, focuses solely on certain portions of the Investment Agreement, to the exclusion of all others. In doing so, the FCA identifies no specific errors in Justice Paris' analysis. Rather, the FCA simply finds that it would prefer a different interpretation, noting that Justice Paris' decision was "inconsistent with the terms of the Investment Agreement",[127] that the $800,000 was "not a trifling amount",[128] and that there was "no realistic chance" that the Corporate Opportunity would be rejected.[129] The FCA then found "[a]s a consequence of all these restrictions", control was handed over to Matco[130] and made a general finding that the Tax Court's decision "is not supported by the evidence".[131] The FCA compounds its error by divorcing the Investment Agreement from the surrounding circumstances and series of transactions.

110. This is what an appellate court should not do. The FCA does not find a clear mistake by the trial judge—there is no beam of light to the eye. Rather, it cherry-picks certain provisions from the Investment Agreement, divorced from the factual matrix, and substitutes its own interpretation of the Investment Agreement as a whole. This reweighing of the evidence to come to a different interpretation of the Investment Agreement is not the role of an appellate court.

111. Further, despite the requirement from *Matta* that an appellate court must precisely identify the palpable and overriding error and explain why it is palpable and overriding,[132] the FCA fails to do so. In its summary treatment of the palpable and overriding error issue, the FCA fails to identify what is palpable about any error in Justice Paris' interpretation of the Investment

---

[126] FCA Reasons at para 98 (**Appellant's Record, Tab 4**).
[127] FCA Reasons at para 98 (**Appellant's Record, Tab 4**).
[128] FCA Reasons at para 103 (**Appellant's Record, Tab 4**).
[129] FCA Reasons at para 104 (**Appellant's Record, Tab 4**).
[130] FCA Reasons at para 105 (**Appellant's Record, Tab 4**).
[131] FCA Reasons at para 111 (**Appellant's Record, Tab 4**).
[132] *Matta* at para 34.

Agreement and fails to explain why it would be overriding. The FCA's bare statement that a palpable and overriding error occurred does not satisfy the requirement in *Matta*.

d. The FCA's interpretation of the Investment Agreement includes a number of errors

112. The FCA's failure to consider the entirety of the evidence is an issue this Court has recognized, noting that one of the reasons for deference is that "appellate fact-finding is not likely to reflect an accurate appreciation of the entirety of the narrative",[133] and an appellate court "cannot hope to do a better job than the trial judge in assessing the evidence as a whole".[134]

113. In addition to failing to appreciate the entire series of transactions, the FCA makes several errors in its review of the Investment Agreement. For example:

(a) At paragraph 98, the FCA found that the terms of the Investment Agreement gave Matco actual control over the Appellant. This is not accurate. The terms of the Investment Agreement contained more than restrictions, they also provided rights to Newco, such as the right to sell its Remaining Shares (or not sell) to any party and there were no restrictions on Newco's right to vote its shares freely to elect the Appellant's board of directors. This ensured that Newco remained in control of the Appellant[135] and is consistent with the trial judge's finding that there were no provisions in the Investment Agreement that gave Matco control over the Appellant.[136]

(b) At paragraphs 102–103, the FCA found that the Investment Agreement "purports to allow" Newco or the Appellant an unfettered right to accept or reject a Corporate Opportunity. This is incorrect. The Investment Agreement expressly gave Newco and the Appellant that right.[137] The use of the term "purport" by the FCA suggests some type of sham agreement which the Crown did not argue and the Tax Court did not find.

---

[133] *Salomon* at para 114.
[134] *Salomon* at para 115.
[135] Investment Agreement s. 4.1, 5.5(f) and 5.8 (**Appellant's Record, Tab 10.3**).
[136] TCC Reasons at paras 57 and 155–166 (**Appellant's Record, Tab 2**).
[137] Investment Agreement s. 4.1 (**Appellant's Record, Tab 10.3**).

(c) At paragraphs 103–104, the FCA concludes that there was no "realistic" chance that Newco would reject the Corporate Opportunity. This again ignores the evidence of both Goold and Ross who testified that the board of directors of the Appellant conducted due diligence and decided to accept the Corporate Opportunity.[138]

114. The FCA's comments above ignore the actual terms of the Investment Agreement and the uncontradicted testimony of the witnesses. These are examples of the FCA drawing new inferences from the evidence that are found nowhere in the trial judge's reasons and that the evidence does not support. Drawing these types of inferences, in direct contradiction to the findings of the trial judge, is not the role of an appellate court.

115. In addition, in undertaking its analysis, the FCA recharacterizes the legal relationships and covenants under the Investment Agreement based on the economics of the transaction. This is an approach that the Tax Court properly rejected based on the principles set out in *Shell Canada Ltd. v. Canada*, where this Court found that the "economic realities" of a situation cannot be used to recharacterize *bona fide* legal relationships and, absent a finding of sham, "the taxpayer's legal relationships must be respected in tax cases".[139] There was no evidence at trial that would have warranted such a recharacterization, and Justice Paris' decision in this regard, informed by *viva voce* testimony of the series of transactions, warrants deference.

116. The evidence strongly supports Justice Paris' conclusion that Matco had no effective control over the Appellant, and the Appellant freely participated in the transactions[140] and, as well, explicitly contradicts the FCA's findings that:

(a) Matco had actual control in general over the Appellant, as the provisions of the Investment Agreement contained "severe restrictions on the actions" that could be taken by the Appellant and Newco, which were backed up by a penalty;[141] and

(b) Matco had control over the Corporate Opportunity as "there was no realistic chance that a Corporate Opportunity would be rejected" by the Appellant and Newco.[142]

---

[138] TCC Reasons at para 32 (**Appellant's Record, Tab 2**).
[139] *Shell Canada Ltd. v. Canada*, [1999] 3 SCR 622 at para 39.
[140] TCC Reasons at paras 32, 34, 39–40, 146–152, 155–165 (**Appellant's Record, Tab 2**).
[141] FCA Reasons at paras 98–101 (**Appellant's Record, Tab 4**).
[142] FCA Reasons at paras 102–104 (**Appellant's Record, Tab 4**).

117. The FCA's findings in this regard ignore the Tax Court's findings and the evidence that Justice Paris relied on, including that:

(a) The restrictions placed on the Appellant's activities under Article 6.1 of the Investment Agreement during the guarantee period did not amount to Matco having control over the shares of the Appellant.[143]

(b) The Appellant's board of directors discussed the proposed Corporate Opportunity and investigated DKCM's background before accepting it.[144] This supports Justice Paris' conclusion that "I also do not believe it can be said that Newco was indifferent to the terms of the Corporate Opportunity".[145]

(c) Under the Investment Agreement, Matco simply promised to present a Sale Opportunity with respect to the Remaining Shares within a year of closing and guaranteed a minimum price to the Appellant of $800,000 for those shares. Matco was liable to pay the entire Guarantee Amount if it did not present the Sale Opportunity. If Newco refused to accept the presented Sale Opportunity, Matco's liability to pay the Guaranteed Amount terminated.[146]

(d) Under section 5.8 of the Investment Agreement, Newco was not required to sell any of the Remaining Shares prior to or during the one year guarantee period or at any other time and this term was not a sham or inconsistent with any other rights in the Investment Agreement read as a whole.[147]

(e) The evidence of Ross and Goold, especially Goold, confirms there was no understanding that Newco would sell its Remaining Shares to Matco. Goold was clear that Newco's board chose to sell to Matco rather than wait until the end of the lockup under the IPO because it needed the cash for its operations. The board was also concerned about the possibility of a declining value in the Remaining Shares before the end of the lockup period. The trial judge accepted Goold's evidence on

---

[143] TCC Reasons at para 160 (**Appellant's Record, Tab 2**).
[144] TCC Reasons at para 32 (**Appellant's Record, Tab 2**).
[145] TCC Reasons at para 165 (**Appellant's Record, Tab 2**).
[146] TCC Reasons at para 58 (**Appellant's Record, Tab 2**).
[147] TCC Reasons at para 59–60 (**Appellant's Record, Tab 2**).

> this point and found him to be a credible witness who had no interest in the outcome of the trial. The trial judge also observed that Newco may have preferred to sell its Remaining Shares sooner than later given the shaky state of the financial markets in 2009.[148]

118. As such, on the evidence, at no time did any party acquire control of the Appellant, or seek to control its destiny to its own advantage. The relationship with Matco was one of lender, partner and ultimately investor.[149] Indeed, as the Crown acknowledged, Matco acted as a mere facilitator and never used the Appellant's losses, SR&ED or ITCs for itself.[150]

119. Each party had its own obligations under the Investment Agreement, and each party carried them out in its own best interest. At no time did Matco have the ability to control the affairs and fortunes of the Appellant. Instead, Matco was obligated to help the Appellant with its restart, and find a Corporate Opportunity.

120. At its heart, the Investment Agreement was Matco's promise to search for a new business, while Newco and the Appellant promised to not take steps that could diminish the value of the Appellant. If Matco failed to find a new opportunity, it promised to pay a penalty (the Guaranteed Amount). However, if it was successful and a Sale Opportunity was made available to Newco, then Matco was relieved of the obligation.

121. The protections granted to Matco under the Investment Agreement underscore the fact that Matco did not control the Appellant. Moreover, the Investment Agreement provided that Newco could enter into an alternative transaction with another party where an acquisition of control would occur and the tax attributes would be lost as long as it gave 90 days' notice to Matco,[151] and there was nothing that Matco could do to prevent it.

---

[148] TCC Reasons at para 64 (**Appellant's Record, Tab 2**).
[149] *See* the recitals to the Investment Agreement (**Appellant's Record, Tab 10.3**).
[150] TCC Reasons at para 152 (**Appellant's Record, Tab 2**).
[151] Investment Agreement s. 5.5(f) (**Appellant's Record, Tab 10.3**).

e. The Appellant's transactions are not abusive tax avoidance

122. The evidence and Justice Paris' findings show that the Appellant's transactions were not abusive, even if this Court were to find that Parliament intended the "actual control" test in ss. 37(6.1), 111(5) and 127(9.1).

123. This case involves losses that arose from true business activities, followed by the deduction of such losses from more business activities, all undertaken by the same corporation. No new losses were created inappropriately, as was the case in *Triad Gestco Ltd. v. R.*[152] The tax attributes were not inappropriately multiplied, as in *Copthorne*.[153] And the Appellant's losses were not somehow deducted by another party, as in *OSFC, Mathew* and *Birchcliff*.[154]

124. In the Appellant's case, the transactions at issue accomplished exactly what Parliament intended. The Appellant, a struggling, widely-held public corporation sought to reinvent itself, used its losses, SR&ED, and ITCs to attract new investment and reconstitute its business. It hired advisers, and entered into mutually beneficial relationships with both Matco and DKCM. Through these relationships, it successfully commenced an entirely new business, which earned profits and paid taxable dividends for a number of years.

125. Justice Paris examined the entire series of transactions and found that they did not constitute abusive tax avoidance. In fact, he noted that the Appellant could have restarted and recapitalized itself without the assistance of Matco.[155] The FCA on the other hand focused inordinately on the Investment Agreement, ignoring the fact that the Appellant's subsequent transactions were commercial in nature and accomplished the business goals of the recapitalization and restart of the company.

126. It is not abusive to hire advisers and experts, and seek help from investors in recapitalizing and restarting a company. It is also not abusive if, at the end of the day, the Appellant's shareholders are not the same:

---

[152] *Triad Gestco Ltd v. R.*, 2012 FCA 258 ("***Triad Gestco***").
[153] *Copthorne* .
[154] *Mathew; OSFC Holdings Ltd v. Canada*, 2001 FCA 260 ("***OSFC***"); *Birchcliff Energy Ltd v. Canada*, 2019 FCA 151 ("***Birchcliff***").
[155] TCC Reasons at para 151.

(a) Since 1972, the *Act* has not required that the shareholder base remain substantially the same in order for a taxpayer to make use of its tax attributes, nor would this be expected in a public company.

(b) If any public company changed its business in some other form of reorganization, it is likely that there would be significant, if not complete, turnover in shareholders, since public shareholders normally make investment decisions based on a company's business. If that business changes, shareholders may change their investment to other opportunities. Again, this would not cause an acquisition of control.

(c) This exact type of scenario explains why, for over 50 years Parliament has withdrawn from considering the make-up of the shareholder base, and instead has focused on acquisitions of control in crafting the loss restriction provisions.

127. There was no scenario where Matco had the ability to control the Appellant. At no time did Matco eliminate the risk that the Appellant's shareholders could derail its intention to have the Appellant start a new business. Matco did its best to mitigate that risk but it was always present, something the witnesses acknowledged at trial.[156] Moreover, Matco never achieved the mischief that Parliament seeks to address: it did not acquire the benefit of the Appellant's losses, SR&ED and ITCs for itself. It only sought to increase the potential returns on a new business investment with a wide and disparate group of other investors.

PART IV - COSTS

128. There is no reason to depart from the general principle that costs should follow the event. The Appellant requests its costs in this Court and in the Courts below.

PART V - ORDER SOUGHT

129. The Appellant respectfully requests that its appeal be allowed, the judgment of the Federal Court of Appeal dated August 4, 2021 be set aside, the Tax Court of Canada judgment dated April

---

[156] Trial testimony of Ross, p. 62, line 17 – p. 63, line 2 (**Appellant's Record, Tab 11**); and p. 134, line 24 – p. 138, line 1 (**Appellant's Record, Tab 12**).

5, 2019 be restored, and the reassessments of the Appellant's income tax returns for its 2009, 2010, 2011, and 2012 taxation years be vacated and set aside.

PART VI - SUBMISSIONS ON CONFIDENTIALITY

130. Not Applicable.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 3rd day of June 2022

Barry Crump /Heather DiGregorio /
Robert Martz
Burnet, Duckworth & Palmer LLP
Counsel for the Appellant

PART VII - TABLE OF AUTHORITIES
(Hyperlinked)

STATUTORY PROVISIONS			Cited at Paragraph
Income Tax Act, R.S.C., 1985, c. 1 (5th Supp.)	EN	FN	1
s. 2(1)	EN	FN	
s. 3	EN	FN	
s. 9	EN	FN	
s. 37(6.1)	EN	FN	4, 7, 8, 10, 27, 28, 32, 47, 50, 52, 53, 54, 55, 56, 72, 88, 101
s. 87(2.1)	EN	FN	
s. 111(1)	EN	FN	54, 55, 57
s. 111(5)	EN	FN	4, 7, 8, 10, 26, 27, 28, 29, 30, 31, 32, 47, 49, 50, 52, 53, 55, 56, 58, 72, 80, 101
s. 127(9)	EN	FN	54
s. 127(9.1)	EN	FN	4, 7, 8, 10, 27, 28, 32, 47, 50, 52, 53, 54, 55, 56, 72, 101
s. 245	EN	FN	5, 35
s. 251(5)	EN	FN	63
s. 256(1)	EN	FN	99
s. 256(1.2)(c)	EN	FN	62, 64, 89

CASES

SECONDARY SOURCES

PART VII - TABLE OF AUTHORITIES
(Non-Hyperlinked)