

TREBILCOCK ON TAX AVOIDANCE

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I. INTRODUCTION

Michael Trebilcock is by all accounts one of his generation's most prolific and important scholars of law and economics.¹ Although he received his undergraduate and graduate legal training in New Zealand and Australia, respectively, Canadian academia has claimed him as one of

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¹ This claim scarcely needs justification to anyone familiar with the field of law and economics; nevertheless, consider that he was invited to contribute a chapter to a recent book celebrating the founding of the field of law and economics: see, Francesco Parisi and Charles Rowley, eds., *The Origins of Law and Economics: Essays by the Founding Fathers* (Edward Elgar, 2005). Included in the volume are essays by notable pioneering law and economics scholars (three of whom are Nobel Laureates in Economics) including Gary Becker, James M. Buchanan, Guido Calabresi, Ronald H. Coase, Robert D. Cooter, Harold Demsetz, Richard A. Epstein, E.W. Kitch, William M. Landes, Harry G. Manne, Francesco Parisi, Richard A. Posner, George L. Priest, Charles K. Rowley, Paul H. Rubin, Steven Shavell, Gordon Tullock, and Oliver E. Williamson.

our own since he visited as a young scholar in the early 1970s at McGill University and shortly thereafter joined the Faculty of Law at the University of Toronto. After visits at the University of Chicago Law School in 1976 and Yale Law School in 1985 cemented his interest in the economic analysis of law, Trebilcock established the Canadian Law and Economics Association in 1989. In 2002 he served as the first non-American President of the American Law and Economics Association.²

Through more than 200 articles, book chapters, books, edited volumes, and other academic publications, Trebilcock has made lasting contributions to many fields including (and this is a partial list): contracts,³ torts,⁴ consumer protection,⁵ antitrust,⁶ international trade,⁷ immigration,⁸ regulation,⁹ and law and development.¹⁰ Moreover, he has been a mentor

² For a list by year of Presidents of the American Law and Economics Association since its founding in 1991 (an event that Michael Trebilcock incidentally and unsurprisingly had a hand in), see “About the American Law and Economics Association” <http://www.amlecon.org/assoc.html> < accessed September 3, 2009> .

³ The most well-known of his works in contract law is Michael J. Trebilcock, *The Limits of Freedom of Contract* (Harvard University Press, 1993).

⁴ The foremost example is Donald Dewees, David G. Duff and Michael J. Trebilcock, *Exploring the Domain of Accident Law: Taking the Facts Seriously* (Oxford University Press, 1996).

⁵ In addition to serving for a time as National Vice-President of the Consumers’ Association of Canada, he has also published widely regarding consumer protection, particularly early in his career. See, for example, Michael J. Trebilcock, “Consumer Protection in the Affluent Society” (1970) 16 *McGill L.J.* 263; Michael J. Trebilcock, “Protecting Consumers Against the Purchase of Defective Merchandise” (1971) 4 *Adelaide L.R.* 12; David Cayne and Michael J. Trebilcock, “Market Considerations in the Formulation of Consumer Protection Policy” (1973) 23 *University of Toronto Law Journal* 396; and Michael J. Trebilcock, “Regulators and the Consumer Interest” (1977) 2 *Canadian Business L.J.* 101.

⁶ One of these many contributions is Michael J. Trebilcock, Ralph Winter, Paul Collins, and Edward M. Iacobucci, *The Law and Economics of Canadian Competition Policy* (University of Toronto Press, 2002). An earlier work was awarded the Walter Owen Book Prize awarded by the Foundation of Legal Research for the best book published in the previous two years: Michael J. Trebilcock, *The Common Law of Restraint of Trade: A Legal and Economic Analysis* (Toronto: Carswell, 1986).

⁷ Michael Trebilcock and Robert Howse, *The Regulation of International Trade*, 3rd edition (Routledge, 2005).

⁸ Michael J. Trebilcock and Ninette Kelley, *The Making of the Mosaic: A History of Canadian Immigration Policy* (University of Toronto Press, 1999).

⁹ See, for example, Edward Iacobucci, and Michael Trebilcock, and Ralph A. Winter, “The Canadian Experience with Deregulation” (2006) 56 *University of Toronto L.J.* 1; and Michael J. Trebilcock and Ronald J. Daniels, *Rethinking the Welfare State: The Prospects for Government by Voucher* (London: Routledge, 2005).

¹⁰ Some recent examples of this work includes, Michael J. Trebilcock and Ronald J.

to countless law students, dozens of graduate students, and numerous faculty members.¹¹ Trebilcock has also influenced domestic and international public policy on, among other topics, telecommunications regulation,¹² the electricity market,¹³ the professions,¹⁴ and legal aid.¹⁵ In recognition of his teaching and research, he has received awards and distinctions from students, universities, governments, and scholarly societies.¹⁶ This symposium is only the latest token of appreciation for Trebilcock's profound and prominent contributions to the intellectual depth and breadth of legal thought. Indeed, it would be difficult to find words that would overstate Trebilcock's gravitational influence and formidable presence in the Canadian legal academy. We are proud to call him ours.

And yet, despite the accolades, the attention, and the richly-deserved scholarly fame, there is a comparatively unlit corner of Trebilcock's oeuvre—the part dealing with income tax law. Although it would be inaccurate to say that it has been entirely overlooked,¹⁷ most participants

Daniels, *Rule of Law Reform and Development: Charting the Fragile Path of Progress* (Edward Elgar, 2008); Kevin Davis and Michael J. Trebilcock, "The Relationship Between Law and Development" (2008) 56 *American Journal of Comparative Law* 895; Michael J. Trebilcock and Paul-Erik Veel, "Property Rights and Development: The Contingent Case for Formalization" (2008) 30 *University of Pennsylvania Journal of International Law* 397.

¹¹ With gratitude, I would include myself in this list.

¹² Michael J. Trebilcock and Edward M. Iacobucci, "The Design of Regulatory Institutions for the Canadian Telecommunications Sector" (2007) 33 *Canadian Public Policy* 127.

¹³ Michael J. Trebilcock, Richard Pierce, and Evan Thomas, "Beyond Gridlock: The Case for Greater Integration of Regional Electricity Markets" C.D. Howe Commentary, March 2006.

¹⁴ These works include Michael J. Trebilcock and Edward M. Iacobucci, "The Competition Bureau's Report on Competition and Self-Regulation in the Canadian Legal Profession: A Critical Evaluation" (2009) *Canadian Competition Record* 92; and Phillip Slayton and Michael J. Trebilcock, eds., *The Professions and Public Policy* (University of Toronto Press, 1978).

¹⁵ Michael J. Trebilcock, *Review of Ontario Legal Aid Program*, prepared for the Ministry of the Attorney General, Government of Ontario (March 2008).

¹⁶ These accolades include being named a Fellow in the Royal Society of Canada, being made an Honorary Foreign Fellow of the American Academy of Arts and Sciences,

¹⁷ Indeed, Trebilcock's article in the *Australian Law Journal* (see *infra* note 20) has been cited on a number of occasions, including P.K. Waight, "A Commentary on Section 260 of the Income Tax and Social Services Contribution Assessment Act 1936-1965" (1965) 1 *Federal Law Review* 292 at 295 fn. 16, 296 fn. 21, 297 fn. 26, and 299 fn. 35; Julius Stone, *Social Dimensions of Law and Justice* (Stanford University Press, 1966) at 326 fn. 219; Yuri Grbich, "Section 260 Re-Examined: Posing Critical

in the symposium and most readers of Trebilcock's more discussed work will not be acquainted with the fact that his scholarly career began, inauspiciously as it might seem, nearly five decades ago with a 224 page long LL.M. thesis at the University of Adelaide.¹⁸ Almost unbelievably, this substantial piece of work was dedicated to analyzing just a single provision of Australian income tax law—a general provision aimed at combating tax avoidance. This essay seizes control of the spotlight that has been trained on Trebilcock's other work and redirects it to Trebilcock's tax scholarship.

Trebilcock's LL.M. thesis assessed a problem that was acute at the time and has been recurrent in the decades since in Australia and elsewhere. The problem is that of the formulation of the appropriate government response to the corrosive effects on public revenues of aggressive tax planning.¹⁹ More specifically, the thesis explored the limits of the effectiveness of section 260 of Australia's *Income Tax Assessment Act*. At the time section 260 established a "general anti-avoidance rule" ("GAAR"), ostensibly intended to provide the Australian courts with the statutory tools thought to be necessary to effectively curb aggressive tax avoidance. Leading up to the time of Trebilcock's LL.M. thesis the provision had been applied erratically by the Australian courts, with several cases prior to 1932 applying the provision, then no mention or application of it from 1932 to 1953, and then again a flurry of cases in the

Questions about Tax Avoidance" (1975-1976) 1 *University of New South Wales L.J.* 211 at 213 fn. 13; Martin J. McMahon, Jr., "Expanding the Taxable Unit: The Aggregation of the Income of Children and Parents" (1981) 56 *N.Y.U. L. Rev.* 60 at 77 fn. 61 and 78 fn. 64; and Walter J. Blum, "Motive, Intent, and Purpose in Federal Income Taxation" (1966-1967) 34 *U. Chi. L. Rev.* 485 at 524-525 fn. 107.

Trebilcock also authored a note that appeared in the *Australian Law Journal* that has been cited on at least one occasion. The note is M.J. Trebilcock, "Section 260 further considered—Peate's case" (1966) 40 *Australian Law Journal* 244. It is cited by Denis F. Dalton, "Avoidance of Taxation: Section 260 of the Income Tax Assessment Act" (1973-1974) 9 *Melbourne U. L. Rev.* 95 at 121 fn. 61.

¹⁸ I am grateful to Michael Trebilcock for sharing an original bound version of his LL.M. thesis. This obviously would not otherwise have been readily available to me: M.J. Trebilcock, "Section 260 of the Income Tax Assessment Act: A Study in the Combating of Tax Avoidance," LL.M. thesis submitted to the University of Adelaide, 1964, 224 pages.

¹⁹ As evidence, consider that Quebec recently published a working paper addressing this very issue, see Finances Quebec, *Aggressive Tax Planning Working Paper* (2009), http://www.finances.gouv.qc.ca/documents/Autres/en/AUTEN_DocCons_PFA.pdf < accessed September 3, 2009 > . The working paper reports that a conservative estimate of the tax revenues recovered through the actions of Revenu Quebec to counter aggressive tax avoidance schemes is \$500 million; *ibid.* at 20.

1950s and 1960s.²⁰ Trebilcock argued in the wake of this renewed interest and application of section 260 that the provision was unsound, and that any general legislative standard proscribing tax avoidance would be inadequate to the task of combating tax avoidance effectively.

I acknowledge and emphasize upfront that the sort of *ex post* reckoning that this essay engages in has the prospect of being grossly unfair to Trebilcock. Indeed, I expect that timorous scholars would shudder at the prospect of sustained scrutiny of their earliest work, fearing that the work (and the reviewer's reception of it) would fail to do justice to the subtlety of their subsequent thinking. For these scholars, the discomfort would probably be especially acute with respect to an area of academic inquiry in which they have not subsequently worked, not least because there would be no further writings that might clarify, revise, or refine their early and, by assumption, provisional views. This potentially obvious source of unfairness does not arise with its full power in this case because the topic of this essay was, in fact, Trebilcock's suggestion.²¹ For this reason I assume that I have complete licence to pan or praise Trebilcock's earliest serious scholarly writing as I see fit. Nevertheless, there remain some potential sources of unfairness that remain that I should make clear that I am setting aside before proceeding.

The first potential source of unfairness relates to the style of presentation of the ideas in the thesis. Trebilcock was writing before the law and economics movement had seriously taken hold at the University of Chicago, Yale Law School, and elsewhere in the US (although of course there had been precursors and intellectual forbears and it would be inaccurate to say that the field did not exist).²² It would be unreasonable, for example, to expect that as writing as a graduate student in the early 1960s in Adelaide that Trebilcock would frame his analysis as he would if he were addressing the same topic today in Toronto. Indeed, at the time that he authored his LL.M. thesis he had little (if any) economics training. Although he is obviously blessed with an abundance of natural economic intuition and talent, it would have been utterly inconceivable for him to have produced an explicitly economic analysis of tax avoidance in the preparation of his LL.M. thesis.

²⁰ For additional details, see M.J. Trebilcock, "Section 260: A Critical Examination" (1964) 38 *Australian Law Journal* 237 at 237.

²¹ And it was a good suggestion—thank you.

²² For an illuminating introduction to the history of law and economics see Ejan Mackaay, "History of Law and Economics" in Boudewijn Bouckaert and Gerrit De Geest, eds., *Encyclopedia of Law and Economics, Volume I. The History and Methodology of Law and Economics* (Cheltenham: Edward Elgar, 2000) at 65-117.

Secondly, even if he could have produced an economic analysis—one cannot rule this out since it is Trebilcock we are discussing after all—it is extremely unlikely, that it would have received a warm reception from his thesis supervisor. The model of legal scholarship in the early 1960s in Australia was doctrinal and aimed principally at providing materials useful to the bench and bar.²³ Trebilcock's thesis thus is—unsurprisingly, given the time and place—consistent with this prevalent doctrinal focus.²⁴ One can assume that an economically-focused analysis would have been returned with comments demanding greater focus on the text of the legislation and the jurisprudence. Trebilcock apparently anticipates this and crafts his arguments so as to avoid this sort of criticism, while at the same time making clear his conceptual concerns.²⁵ Trebilcock knew his audience.²⁶

A third and even more profound reason to suspect the unfairness of an *ex post* assessment of Trebilcock's LL.M. thesis relates to the benefit of hindsight. Indeed, this is probably the most difficult to side-step of the three potential sources of unfairness. It will probably not come as a shock to any legal scholar familiar with Trebilcock's work, however, that even removed by nearly five decades in time and half-a-world in space from the University of Adelaide, his analysis identified the shortcomings in the GAAR of the day and anticipated many of the reforms GAARs have undergone to become more effective and useful to governments. Moreover, although the Australian GAAR has subsequently been amended and GAARs have been enacted elsewhere, their effectiveness and utility continue to be bounded for the conceptual reasons Trebilcock adumbrated. Indeed, despite the potential sources of unfairness in this evaluative enterprise, the central claim of this examination of Trebilcock's work on

²³ See Erwin N. Griswold, "Observations on Legal Education in Australia" (1952) 5 *J. Legal Education* 139; and Michael Chesterman and David Weisbrot, "Legal Scholarship in Australia" (1987) 50 *Modern Law Review* 709.

²⁴ It is nevertheless obvious at various points in his argument that Trebilcock is not entirely comfortable with conducting only an analysis of the statutory language and its interpretation and application by the courts. This is entirely to his credit.

²⁵ Three of these conceptual concerns are addressed below in Part II.

²⁶ It is clear that he had tremendously impressed the law school with his scholarship because he was hired on at the University of Adelaide even before he had submitted the final version of his LL.M. thesis. When a senior member of the faculty in commercial law announced an intention to leave the Dean of the law school hired Trebilcock to fill the position. See Michael J. Trebilcock, "Keynote Address—Professor Michael Trebilcock: Ottawa Call to the Bar Ceremony, July 10, 2003" <http://www.lsuc.on.ca/media/july1003_callottawaapeech.pdf> (accessed September 16, 2009).

tax avoidance is that although he was purporting principally to analyze the Australian GAAR, Trebilcock presaged the challenges, struggles, and obstacles faced in the subsequent battle by governments against aggressive tax avoidance in Canada and throughout the English speaking world in the following half century.

Two weaknesses of Trebilcock's thesis are worth mentioning, and they are both camouflaged strengths. The first is that the analysis was at points overly strident and pessimistic regarding the prospects of an efficacious GAAR. A second would be that Trebilcock assumed that strict interpretation of tax legislation would continue (it has not; or, at least, has not officially). These weaknesses should not be overstated. Entirely in keeping with Trebilcock's insights, for example, the highest courts in Canada and Australia, among others, continue to struggle with how to understand and operationalize the concept of a general legislative standard against aggressive tax avoidance. In addition, the Supreme Court of Canada continues to prioritize the text of the *Income Tax Act* in its interpretative strategy (though it claims to consider the context and purpose of the Act as well).²⁷ Indeed, as I will explain, Trebilcock's broadest insights have stood the tests of time and travel remarkably well.

The essay proceeds as follows. To set some context, Part II provides a thumbnail sketch of the history of statutory and judicial anti-avoidance doctrines in Canada up to 1988. Part III identifies and extracts three conceptual challenges for all GAARs from Trebilcock's LL.M. thesis, borrowing also from the law review article²⁸ that was subsequently

²⁷ This is what the Court refers to as the "textual, contextual, and purposive" approach to statutory interpretation. This phrase was first used in *Canada Trustco Mortgage Co. v. R.* [2005] 5 C.T.C. 215; 2005 D.T.C. 5523 (S.C.C.). At para. 11, the Court remarked that,

As a result of the Duke of Westminster principle (*Commissioners of Inland Revenue v. Duke of Westminster*, [1936] A.C. 1 (H.L.)) that taxpayers are entitled to arrange their affairs to minimize the amount of tax payable, Canadian tax legislation received a strict interpretation in an era of more literal statutory interpretation than the present. There is no doubt today that all statutes, including the Income Tax Act, must be interpreted in a textual, contextual and purposive way. However, the particularity and detail of many tax provisions have often led to an emphasis on textual interpretation. Where Parliament has specified precisely what conditions must be satisfied to achieve a particular result, it is reasonable to assume that Parliament intended that taxpayers would rely on such provisions to achieve the result they prescribe.

²⁸ *Ibid.*

published as an abridged version of the arguments from his LL.M. thesis. Part IV examines the three conceptual issues that Trebilcock's work raises given the developments in Canada's battle against aggressive tax avoidance post-1988 with the introduction of the Canadian GAAR. In light of the insight Trebilcock brought to the topic, Part V concludes with a lament that he elected to leave further work on anti-avoidance measures to others.

II. BRIEF HISTORY OF TAX AVOIDANCE IN CANADA

Canada has had a federal income tax since 1916. However, Canada adopted its current GAAR only in 1988 after the Supreme Court of Canada rejected a judicial "bona fide business purpose" test in *Stubart Investments Limited v. The Queen*.²⁹ This section provides some background for understanding the context of the federal income tax in the pre-GAAR era in Canada.

As I have written recently elsewhere with my colleague, David Duff, from its inception the Canadian income tax system has been heavily influenced by the approach taken to income taxation in the UK.³⁰ Originally, this influence was very strong, and it has waxed and waned throughout the decades. When the Supreme Court of Canada put an end to an emerging "bona fide business purpose" doctrine in *Stubart Investments* in 1984 the federal government embraced fully the possibility that a made in Canada version of a robust GAAR might be necessary and prudent. This development arrived, of course, long after the problems with tax avoidance had been diagnosed and understood.

Tax avoidance in Canada was based on two central aspects of the income tax system: the strict interpretation of fiscal legislation and an attendance to legal substance of transactions; both influences were inherited from the UK.³¹ Both influences contributed significantly to tax avoidance.³² As early as 1966, Canada's Royal Commission on Taxation (the "Carter Commission") explained in its exhaustively researched report³³ that in its view tax avoidance was undesirable for several reasons, including: (i) the reduced tax revenues received by the government; (ii)

²⁹ [1984] CTC 294; 84 DTC 6305 (SCC).

³⁰ See Benjamin Alarie and David Duff, "The Legacy of UK Tax Concepts in Canadian Income Tax Law" [2008] *British Tax Review* 228.

³¹ For an extensive discussion, see *ibid.*

³² See Chapter 3 of David G. Duff, Benjamin Alarie, Kim Brooks, and Lisa Philipps, *Canadian Income Tax Law*, 3rd ed. (LexisNexis, 2009) for a more detailed account.

³³ Canada, *Report of the Royal Commission on Taxation*, vols. 1-6 (Ottawa: Queen's Printer, 1966).

diversion of valuable intellectual and financial resources into the planning and execution of tax avoidance; (iii) the “sense of injustice and inequality” experienced by those taxpayers not privy to tax avoidance schemes; and (iv) the resultant need for other taxpayers, either in the present or the future, to bear the burden of taxes avoided.³⁴ In the wake of the refashioning of the *Income Tax Act* in 1972, largely on the basis of the recommendations of the Carter Commission (the most notable change was the introduction of the taxation of capital gains), there was apparently some hope on the part of the federal government that existing anti-avoidance provisions would be up to the task of defending the Canadian tax base against aggressive tax avoidance.

These legislative efforts were bolstered to an extent by an emerging openness in the 1970s on the part of the Canadian courts to examine the “*bona fide* business purpose” (if any) of a transaction or series of transactions as a way of diagnosing whether the transaction or series of transactions should be legally respected for tax purposes or disregarded as a “sham.”³⁵ The incremental move toward a judicial test of “*bona fide* business purpose” in Canada was perhaps inspired by the earlier adoption of a similar doctrine in the US.³⁶ It contrasted significantly with the adherence in the UK to the legal substance of transactions, which had been famously established by the House of Lords in *Duke of Westminster* case.³⁷

If it is clear that a GAAR was Parliament’s inevitable response to concerns about tax avoidance, why did it take so long for Canada to respond to aggressive tax avoidance with the GAAR in 1988? Perhaps it was the continuing influence of the UK and the fact that the UK tax system did not have a GAAR.³⁸ Although the UK has from time to time mooted the possibility of enacting a GAAR, it has not yet done so.³⁹ But this engenders a further question: why has the UK itself not encountered problems with tax avoidance leading it to enact a GAAR?

Although the UK does not have a GAAR, it is not because the UK has dramatically and effectively succeeded in combating tax avoidance through specific anti-avoidance rules (though it has these). Tax avoidance remains

³⁴ *Ibid.*, vol. 3, at 541-542.

³⁵ The key decision in this respect is *M.N.R. v. Leon*, [1976] CTC 532; 76 DTC 6299 (F.C.A.). The Federal Court of Appeal in *Leon* held that, “It is the agreement or transaction in question to which the Court must look. If the agreement or transaction lacks a *bona fide* business purpose, it is a sham.”

³⁶ See the discussion below.

³⁷ See the discussion below.

³⁸ Rachel Anne Tooma, *Legislating Against Tax Avoidance* (IBFD, 2008) at 54.

³⁹ *Ibid.*

a live concern. The history of anti-avoidance in the UK combines a strict approach to interpreting income tax legislation and a strong adherence to the legal substance (as compared with economic substance)⁴⁰ of transactions engaged in by taxpayers. This appears to have been motivated by the idea that taxation is punitive and, similarly to criminal law, any ambiguity in a charging provision ought to be resolved in favour of the individual taxpayer rather than in favour of the state.⁴¹ Indeed, the House of Lords had relatively early on established the principle that taxpayers are entitled to arrange their affairs so as to minimize the obligation to pay tax in its famous judgment in the *Duke of Westminster*.⁴² The strict approach in the UK has been abandoned since the early 1980s, however.⁴³ The subsequent development of the House of Lords tax judgments has veered to and fro in its hostility to tax avoidance.⁴⁴ With the greater certainty provided by the 2004 decisions of the House of Lords in *Barclays Mercantile*⁴⁵ and *Scottish Provident*,⁴⁶ it is clear now that the position in the UK is that taxation statutes should be given a purposive interpretation just as should any other legislation.

The purposive approach to statutory interpretation has also been adopted by the Supreme Court of Canada⁴⁷ and has come to be known as

⁴⁰ For additional details on the doctrine of economic substance in US income tax law, see Jinyan Li, “ ‘ Economic Substance ’ : Drawing the Line Between Legitimate Tax Minimization and Abusive Tax Avoidance” (2006) 54(1) *Canadian Tax Journal* 23 at 46-52; and Joseph Bankman, “ The Economic Substance Doctrine” (2000) 74(1) *Southern California Law Review* 5; Marvin A. Chirelstein and Lawrence A. Zelenak, “ Tax Shelters and the Search for a Silver Bullet” (2005) 105(6) *Columbia Law Review* 1939; and Joseph Isenbergh, “ Musings on Form and Substance in Taxation” (1982) 49(3) *University of Chicago Law Review* 859.

⁴¹ See Alarie and Duff, *supra* note 30.

⁴² [1936] A.C. 1 (H.L.) [“ *Duke of Westminster*”]. The most commonly quoted phrase from the decision is from the speech of Lord Tomlin. Lord Tomlin stated at 19-20 that,

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

⁴³ The first clear indication of this was the judgment of the House of Lords in *W.T. Ramsay Ltd. v. IRC*, [1982] AC 300.

⁴⁴ See the discussion in Tooma, *supra* note 38 at 54-63.

⁴⁵ *Barclays Mercantile Business Finance Limited v. Mawson*, [2004] UKHL 51.

⁴⁶ *IRC v. Scottish Provident Institution*, [2004] UKHL 52.

⁴⁷ The original move in abandoning strict interpretation came in the Supreme Court of Canada’s judgment in *Stuart Investments*.

the “textual, contextual, and purposive” approach.⁴⁸

Although it is clear that UK tax law has moved towards a more pragmatic method of interpreting income tax legislation, it has arguably not yet adopted a more robust approach to characterizing transactions according to their economic substance. This contrasts sharply with the approach of the US. The US, like the UK, does not have a GAAR. In the US, it is arguable that the need for a GAAR has been less acute in large part because American courts have been more aggressive at tackling tax avoidance. More specifically, the US Supreme Court’s 1935 judgment in *Gregory v. Helvering, Commissioner of Internal Revenue*⁴⁹ has been used in the decades since to establish a more robust judicially-driven approach to tax avoidance. This more aggressive approach by the US courts to tax avoidance contrasts sharply with the approach of the House of Lords in the *Duke of Westminster*.⁵⁰ Canada has been (whether this is for the better or worse is unclear) more influenced by the House of Lords and the *Duke of Westminster* than by the US Supreme Court and *Gregory v. Helvering*.⁵¹

And yet, a number of considerations, not least the revenue needs of a federal government severely in the red in the mid-late 1980s, prompted Canada’s foray into the implementation of a GAAR. This foray took shape after the Supreme Court of Canada’s decision in *Stuart Investments*. Ostensibly, the Court was motivated in part by an existing provision that denied deductions that would “unduly or artificially reduce” a taxpayer’s income.⁵² The relevant provision at the time that

⁴⁸ For a discussion of the trajectory of tax avoidance doctrines in the UK, see Tooma, *supra* note 44. For a discussion of the co-evolution of tax avoidance in Canada and the UK, see Judith Freedman, “Converging Tracks? Recent Developments in Canadian and UK Approaches to Tax Avoidance” (2005) 53(4) *Canadian Tax Journal* 1038. For extensive discussion of statutory interpretation in Canadian income tax law, see David G. Duff, “Interpreting the Income Tax Act—Part 1: Interpretive Doctrines” (1999) 47(3) *Canadian Tax Journal* 464; and David G. Duff, “Interpreting the Income Tax Act—Part 2: Toward a Pragmatic Approach” (1999) 47(4) *Canadian Tax Journal* 741.

⁴⁹ 293 U.S. 465 (1934) [“*Gregory v. Helvering*”].

⁵⁰ The contrast between the US result in *Gregory v. Helvering* and the UK result in the *Duke of Westminster* is subjected to illuminating scrutiny by Assaf Likhovski, “The Duke and the Lady: *Helvering v. Gregory* and the History of Tax Avoidance Adjudication” (2004) 25 *Cardozo Law Review* 953.

⁵¹ In light of the considerable mobility of capital, it is not obvious that an aggressive approach to combating tax avoidance is optimal for a small open economy such as Canada’s; it seems that for a large open economy like that of the US, it probably makes more sense.

⁵² *Ibid.* at 557: “The presence of a provision of general application to control

Stuart Investments was decided provided that, “ In computing income for the purposes of this Act, no deduction may be made in respect of a disbursement or expense made or incurred in respect of a transaction or operation that, if allowed, would unduly or artificially reduce the income.”⁵³ This provision was almost entirely ineffective in combating tax avoidance and was repealed when the GAAR was introduced in 1988 following extensive consultations and discussions with the Canadian tax community.⁵⁴

At the time of its introduction, the Canadian GAAR was touted as a solution to tax avoidance and the federal government had high hopes that it would be able to effectively combat the most egregious and aggressive tax avoidance schemes without having to resort to patchwork and stopgap specific anti-avoidance rules. The hope surrounding the introduction of Canada’ s GAAR was that it would, in the words of David A. Dodge, at the time the Senior Assistant Deputy Minister of the Department of Finance, “ foster simplicity and compliance by reducing the need to enact complex specific rules to deal with sophisticated avoidance schemes.”⁵⁵ Dodge also emphasized that the new GAAR “ most of all ...addresses the issue of fairness. Sophisticated tax avoidance schemes are used mostly by wealthy and well-advised taxpayers; the resulting higher rates of tax are unfair to the majority of taxpayers.”⁵⁶

The legislation that amended the *Income Tax Act* in Canada to include the GAAR was known as Bill C-139. The explanatory notes issued by the Minister of Finance, Michael Wilson, accompanying Bill C-139, outlined the purpose of Canada’ s new GAAR as follows.

New section 245 of the Act is a general anti-avoidance rule which is intended to prevent abusive tax avoidance transactions or arrangements but at the same time is not intended to interfere with

avoidance schemes looms large in the judicial approach to the taxpayer’ s right to adjust his sails to the winds of taxation unless he thereby navigates into legislatively forbidden waters.”

⁵³ *Ibid.* at 546.

⁵⁴ For an excellent account of this history and the prospects of the Canadian GAAR, see Brian J. Arnold and James R. Wilson, “ The General Anti-Avoidance Rule—Part 1” (1988) 36(4) *Canadian Tax Journal* 829; Brian J. Arnold and James R. Wilson, “ The General Anti-Avoidance Rule—Part 2” (1988) 36(5) *Canadian Tax Journal* 1123; and Brian J. Arnold and James R. Wilson, “ The General Anti-Avoidance Rule—Part 3” (1988) 36(6) *Canadian Tax Journal* 1369.

⁵⁵ David A. Dodge, “ A New and More Coherent Approach to Tax Avoidance” (1988) 36(1) *Canadian Tax Journal* 1 at 3.

⁵⁶ *Ibid.*

legitimate commercial and family transactions. Consequently, the new rule seeks to distinguish between legitimate tax planning and abusive tax avoidance and to establish a reasonable balance between the protection of the tax base and the need for certainty for taxpayers in planning their affairs.⁵⁷

It seems unlikely that Canadian policymakers were blind to the challenges facing the effective implementation of a GAAR. With the benefit of hindsight one can imagine that it was foreseen that it would be difficult to impose a standards-based proscription of tax avoidance onto the rules-based *Income Tax Act*, which had grown even at that time into an incredibly detailed and densely drafted statute.⁵⁸ Perhaps in adopting the GAAR in 1988, Canadian policymakers had abundant confidence in the courts to apply the GAAR effectively. Perhaps they felt that it would forestall the development of even more aggressive tax avoidance schemes in the future. Perhaps there was a sense of desperation relating to a diminishing tax base and felt that they had nothing to lose. Perhaps all these factors played into the introduction of the GAAR. In any event, one can easily form the impression that if Canadian policymakers had paid attention to Michael J. Trebilcock's article published in the *Australian Tax Journal* more than 20 years earlier, they would perhaps not have been as optimistic about the prospects of the new GAAR of section 245 of the *Income Tax Act* in combating tax avoidance.

But what exactly did Trebilcock earlier see in the Australian GAAR that caused him to be so pessimistic about the prospects of addressing tax avoidance using a GAAR?

III. TREBILCOCK'S CONCEPTUAL OBJECTIONS TO GAARS

Before proceeding on to examine Trebilcock's broad conceptual objections to GAARs, it is worthwhile to examine the text of section 260 of the Australian income tax legislation to see precisely and specifically what Trebilcock was responding to in his LL.M. thesis. Section 260 at the time provided, in part, that any "contract, agreement, or arrangement" insofar "as it has or purports to have the purpose or effect of in any way, directly or indirectly" of "defeating, evading or avoiding any duty or liability imposed on any person by this Act" would be "absolutely void, as against the Commissioner, or in regard to any

⁵⁷ Department of Finance, *Explanatory Notes to Legislation Relating to Income Tax* (CCH, 1988) at 313.

⁵⁸ Or so it seems now that it was transparently going to be difficult.

proceeding under this Act, but without prejudice to such validity as it may have in any other respect or for any other purpose.”⁵⁹ The attack made by the Australian GAAR legislation was thus on the legal effectiveness of tax avoidance schemes vis-à-vis the Australian government; the government could simply disregard transactions it believed gave rise to tax avoidance.

It is probably not immediately obvious to an outside observer who has not studied tax law in depth or thought much about tax avoidance why such a provision might be insufficient. For this reason, it would have been ambitious enough for Trebilcock to have pointed out the numerous quandaries and issues associated with the interpretation and application of the provision. It appears, however, that Trebilcock has always been inclined to, in the words of former NFL quarterback Kenny ‘the Snake’ Stabler, “throw deep.”⁶⁰ He went for section 260’s jugular. The

⁵⁹ M.J. Trebilcock, “Section 260: A Critical Examination” (1964) 38 *Australian Law Journal* 237 at 237.

⁶⁰ Stabler was NFL MVP in 1974, a four-time Pro-Bowl selection, and led the NFL in passing touchdowns in 1974 and 1976. The reference to Stabler’s words in this context apposite, in light of a speech that Trebilcock gave at a special convocation of the Law Society of Upper Canada on July 10, 2003 in Ottawa, at which he was awarded an honorary doctorate in laws from the Law Society of Upper Canada. The full-text of Trebilcock’s address is available online: see Michael J. Trebilcock, “Keynote Address—Professor Michael Trebilcock: Ottawa Call to the Bar Ceremony, July 10, 2003” <http://www.lsuc.on.ca/media/july1003_callottawaapeech.pdf> (accessed September 16, 2009). Trebilcock closed his address to convocation with the following:

During a television interview with Kenny ‘the Snake’ Stabler, former NFL quarterback for the Oakland Raiders and the New Orleans Saints—a great quarterback but also a notorious ‘free spirit’—the interviewer read the following quote from novelist Jack London: ‘I would rather be ashes than dust. I would rather my spark burn out in a brilliant blaze than that I should be stifled by dry rot. I would rather be a superb meteor than a sleepy permanent planet.’ Then the interviewer asked Stabler: ‘What message do you think London was trying to convey?’ Stabler thought for a moment and said, ‘Throw deep.’ I, as one of your educators, expect no less of you. The great traditions of this profession expect no less of you. But most of all, you should expect no less of yourselves.

Three or four years ago I told the Stabler story at an awards ceremony. One of my favourite students from twenty-five years ago, John Stransmann, of Stikeman, Elliott, one of Canada’s most respected corporate lawyers, heard me tell this story and arrived unannounced one day a few weeks later at my law school office with a framed picture of Kenny Stabler in throwing mode, personally autographed by Kenny Stabler, with a brass plaque with the words, Throw Deep, at the bottom of the picture. Tragically, John became terminally ill with cancer a few months later and died cruelly prematurely about two years ago. However, the picture and the axiom occupies pride of place in my home

introductory chapter of Trebilcock's LL.M. thesis declares boldly that,

The thesis will be maintained that Section 260 displays unmitigatedly the weaknesses suggested as inherent in any general prohibition of 'tax avoidance', and that its continued retention in the Act cannot be supported on any recognized legal or fiscal principle."⁶¹

This is indeed "throwing deep."

For one thing, even if Trebilcock can be granted the claim that section 260 as it was then drafted was apt to be essentially entirely ineffective in combating tax avoidance, it is not at all obvious that the ineffectiveness of the provision ought to result in its being eliminated from the Australian Act. The more obvious response, one might reasonably have thought, would be simply to amend the provision to remedy its shortcomings. Indeed, Trebilcock's suggestion was that "any general prohibition of tax avoidance" would exhibit a set of common conceptual weaknesses and, therefore, no amendment of section 260 could save it from these conceptual defects. This meant that Trebilcock had raised the bar significantly from arguing against a single GAAR embodied in a particular text. Instead, he had taken a position against the whole *idea* of combating tax avoidance through the enunciation of a general standard against the practice. This is an example of a "black swan" problem,⁶² because for the claim to fail, Trebilcock would only have to be confronted with one effective GAAR (or one "black swan"); correspondingly, for the claim to

study. Whenever I feel flat, enervated, or a trifle disjointed, I look at this picture and remember John and his and his family's courage during their suffering. I tell myself to pick up my game and attempt another big play, given the bounties that life has been kind enough to bestow on me—the award conferred on me today being prominent among them. So set your sights high. God bless and good speed.

⁶¹ M.J. Trebilcock, "Section 260 of the Income Tax Assessment Act: A Study in the Combating of Tax Avoidance," LL.M. thesis submitted to the University of Adelaide, 1964 at 25.

⁶² The 'black swan' problem arises whenever one's argument demands that one show that there is in existence no example of a particular thing. Here, Trebilcock's argument demands that he shows that no version of a GAAR is sufficient to overcome the conceptual difficulties he raises, not merely that the particular instantiation of a GAAR in section 260 suffered from conceptual difficulties. The popularization of this phrase is largely attributable to the recent success of a bestselling book of the same name: see Nassim Nicholas Taleb, *The Black Swan: The Impact of the Highly Improbable* (Random House, 2007).

succeed fully, he would have to show the inadequacy of all possible GAARs. It would have been much easier, for example, to explain that there were significant weaknesses in section 260 of the Australian tax legislation of the time.

Even if Trebilcock succeeded in showing that *any* conceivable amendment of the Australian GAAR would be indefensible and ineffective in satisfactorily countering tax avoidance directly, it does not necessarily follow that Australia's GAAR would have to be eliminated from the Act. For example, one residual role that might be played by even a grossly ineffective GAAR provision is that despite being toothless it might nevertheless provide fair notice to taxpayers that the most audacious and aggressive tax avoidance schemes would be contested by the tax authorities and, failing that, by the legislature. It could thus perhaps serve as a signal that taxpayers ought to expect specific anti-avoidance rules of a retroactive nature to reverse the tax advantages asserted by aggressive tax avoiders.⁶³

Finally, Trebilcock's thesis was audacious in that to sustain it he was forced to argue that the cases in which the provision had been found to have been validly and successfully applied by the Australian government had been wrongly decided and had reached indefensible outcomes—a high burden indeed for an LL.M. thesis.⁶⁴ In all these respects, therefore, Trebilcock was from the outset clearly not averse to “throwing deep.”

A. *Problem 1: What does it mean to ‘avoid tax liability’?*

Trebilcock recognized that GAARs must summon an answer to questions such as, “When has an arrangement the purpose or effect of avoiding liability to tax?”⁶⁵ Or, as he puts it later, “What constitutes an avoidance of liability to tax?”⁶⁶ This was conceptually difficult in Trebilcock's view, because after “a liability has been incurred by a

⁶³ As I have written about elsewhere, retroactive tax legislation of this kind is a possibility in Canada since it is not barred by any constitutional principle and, to the contrary, appears to have been used on a number of occasions by Canadian governments. See Benjamin Alarie, “Retroactivity and the General Anti-Avoidance Rule” in D. Duff and H. Erlichman, eds., *Tax Avoidance in Canada after Canada Trustco and Mathew* (Irwin Law, 2007) 197; and also, “*Kingstreet Investments: Taking a Pass on the Defence of Passing On*” (2008) 46(1) *Canadian Business Law Journal* 36.

⁶⁴ Trebilcock notes himself that “judicial interpretation...has rendered the section very far from impotent.” M.J. Trebilcock, “Section 260: A Critical Examination” (1964) 38 *Australian Law Journal* 237 at 237.

⁶⁵ *Ibid.* at 238.

⁶⁶ *Ibid.* at 238.

taxpayer, there is nothing he can do, by private bargaining or otherwise, to displace it.”⁶⁷ In other words, Trebilcock’s argument was that a tax liability cannot be avoided after it comes into existence through transactions that the taxpayer engages in with other private parties. After all, once it comes into existence tax liability is fixed and inviolable. Instead, Trebilcock argued that GAARs must be focused on transactions that sidestep tax liability before the tax liability crystallizes. Thus, “tax avoidance” must be the avoidance of a tax liability that is as yet, inchoate. Indeed, Trebilcock states that, “the section must be taken as striking at arrangements which have the effect of preventing a liability from coming into existence. The question to which the section must then give rise is when has an arrangement prevented a liability from arising?”⁶⁸ What conditions show that tax liability has been sidestepped? In Trebilcock’s view, “no future liability to tax can strictly be regarded as inevitable.”⁶⁹

As an example, Trebilcock argues that a decision not to continue to work overtime hours on account of the disincentive arising from the income tax applicable on the additional wages would satisfy most ordinary understandings of “tax avoidance” since a taxpayer is responding to the additional tax that would be payable on the additional income to choose to not work overtime.⁷⁰ A future tax liability is being avoided. In the event that the future tax liability almost certainly would have been incurred if the “arrangement” of not working overtime had not been put in place, it is clear that the measures taken (i.e., not working overtime) ensured that the additional tax liability did not arise. Could it, however, make sense to insist that the taxpayer pay the income tax that would have been payable on the overtime wages in order to combat the avoidance of tax liability? Trebilcock argued that it would not. Though he did not put it in precisely these terms, the thrust of his argument is that doing so would effectively impose a tax on the consumption of leisure (presumably this was a choice that had been considered and rejected by the legislature) and not only on the economic returns to labour effort.

Trebilcock’s conceptual dissatisfaction with understanding what “tax avoidance” entails suggests in addition that even if one can be sure that a taxpayer has avoided tax (though, as Trebilcock says, no future tax liability can be inevitable) it cannot be the case that all avoidance of future tax liability will trigger the application of a GAAR. Instead, there must

⁶⁷ *Ibid.* at 238.

⁶⁸ *Ibid.* at 238.

⁶⁹ *Ibid.* at 239.

⁷⁰ *Ibid.* at 239.

be a further distinction made between objectionable and unobjectionable tax avoidance, of which “not working overtime” almost certainly ought to be considered unobjectionable. Trebilcock found accounting for *why* some tax avoidance is relatively more objectionable conceptually problematic as well.

B. Problem 2: What makes certain tax avoidance ‘objectionable’ ?

The second conceptual problem that Trebilcock identifies is that to the extent that a GAAR seeks to reverse, counter or combat the avoidance of tax liability, there must be some concept of what tax consequences are contemplated and allowed by the tax statute and what tax consequences are not contemplated and are disallowed by the tax statute. The trick is distinguishing one from the other. This is difficult in Trebilcock’s view because tax legislation often pursues several (if not many) policy ends simultaneously, and establishes certain tradeoffs among them, often within a politically contested environment. Moreover, although it is clear that a motivation behind a GAAR is to combat tax avoidance that in some respect goes too far in reducing the tax liability of taxpayers, it is difficult to see how a court is supposed to determine what constitutes tax avoidance of the kind that should be considered objectionable in the absence of clear legislative guidance.

Naturally, making this sort of distinction between allowable tax avoidance and the sort of tax avoidance that is intended to be countered by a GAAR requires discerning what the operating motivations of the legislature were in providing explicitly or implicitly for the various tax benefits that are provided for in the tax statute. This requires knowing the mind of the legislature which, Trebilcock asserts, is a slippery fiction, since all that is enacted as law is the text of the legislation.

Trebilcock notes that it cannot be the case that a GAAR will apply wherever a taxpayer has been lured into a certain transaction or mode of conduct by the prospect of tax benefits. In his view, this would result in an absurd outcome. To return to the overtime wages example, it is unlikely that the legislature would want to impose a tax on leisure when the entire point of the income tax, one would have thought, was to tax income rather than leisure. Presumably, if the legislature had desired to tax leisure, it would have done so. More broadly, if interpreted and applied without conditions, the Australian GAAR “would appear to deprive a number of specific provisions of the Act which, for example, create concessional deductions, of any meaning or content.”⁷¹ According

⁷¹ *Ibid.* at 240.

to Trebilcock,

It is inconceivable that s. 260 should have been intended as having this effect for the Act would then give, in some provisions, what it took away in another. The clear purpose of these provisions is in many cases to encourage socially desirable expedients by holding out the additional attraction of taxation advantages. These advantages produce, in effect, legally permissible forms of tax avoidance.⁷²

It follows for Trebilcock that because of the presence of explicitly authorized and “legally permissible forms of tax avoidance,”⁷³ skepticism is warranted regarding the utility of GAARs in combating what amounts to desirable and anticipated uses of the tax benefits granted by tax legislation, and the undesirable and unanticipated uses of the tax benefits granted by the tax legislation. Indeed, Trebilcock argues that,

if the courts in determining whether a particular instance of tax avoidance is or is not objectionable under s. 260 cannot refer to what the legislature contemplates in this circumstance, it must follow that in making this distinction, the courts in fact apply their own criteria for determining when a taxpayer has avoided a liability to tax which he ought properly to have incurred. This extra-statutory “ought” inherent in the concept of tax avoidance and in the absence of a statutory definition of the expression must remain an entirely subjective concept—the concept of a proper liability to tax which a man should not be allowed to avoid. That the concept of a proper liability to tax is subjective is clear when it is recognized as true that any number of people through differing combinations of genes, environment and economic and political inclinations may genuinely hold any number of views as to what constitutes the proper liability to tax of various taxpayers.⁷⁴

Trebilcock also noted plainly that “to treat the term ‘tax avoidance’ as the legislature appears to have done in the section as having an objective content readily ascertainable by reference to absolute criteria and capable of application mechanistically to particular cases is conceptually

⁷² *Ibid.* at 240.

⁷³ *Ibid.*

⁷⁴ *Ibid.* at 241.

mistaken.”⁷⁵

The insight underlying Trebilcock’s second conceptual objection relates to the problem in reconstructing the purposes and intentions of a text that has been drafted, revised, debated, voted upon, passed, amended, and had parts repealed, parts added, and so on and so forth over many years. It is likely that most legislators who voted on the original legislation or on many of the amendments to the original legislation had only a vague sense of what they were voting upon at the time. Very few legislators are likely to be tax experts sufficiently well-versed and interested in the minutiae of tax law to have come to a full understanding of the demands placed on taxpayers through the provisions constituting income tax law. And even if each legislator did have a concrete and well-formed understanding of what they understood the legislation to demand of taxpayers, it is unlikely that the views of any given legislator would match with the views of a majority of the other legislators. All that makes up the income tax legislation is the text of the statute. In general, the more technical and arcane are the provisions that taxpayers rely on or make use of in engaging in an avoidance transaction, the less likely it is that the provision was designed in anticipation of the taxpayer’s use of the provision.

The gravity of this second objection then suggests that the appropriate focus in combating tax avoidance should not be on the purposes or intentions of the legislature in crafting the applicable legislation, since this is by necessity a fiction, but the focus of a GAAR should be on the motivations of the taxpayer. In other words, what has motivated the taxpayer in pursuing a certain arrangement? For Trebilcock, this too is conceptually problematic.

C. Problem 3: How to discern proper from improper purposes?

If one insists that it is not enough that a taxpayer could have done something differently that would have triggered greater tax liability (i.e., the taxpayer has engaged in an arrangement that avoided future tax liability, such as deciding to discontinue working overtime, which gives rise to Trebilcock’s first objection) and that one cannot easily discern those types of not incurring tax liability are objectionable from unobjectionable because the policies underlying modern fiscal legislation are multiple and pragmatically unknowable (this is essentially Trebilcock’s second objection), then perhaps one is left with turning to the taxpayer’s own motivation in pursuing a given course of conduct. More specifically, if a

⁷⁵ *Ibid.*

taxpayer is motivated entirely by reducing tax liability, then this is perhaps a signal that something is amiss and ought to be challenged by the authorities.

For example, in the case of a taxpayer considering whether to choose to work overtime or not, it is likely that the decision will turn in part on tax considerations and in part on the value of not having to exert the labour effort necessary to earn the additional wages. Moreover, the taxpayer's liberation from work for those hours to engage in leisure activities such as watching television, reading fiction, or sleeping, is likely to have an appeal. All in all, it is unlikely (though not impossible) that at non-confiscatory income tax rates the additional tax liability could be said to be the primary motivation for a taxpayer turning down the opportunity to work overtime. The idea, then, of focusing on a taxpayer's motivation in not choosing the "highest tax" alternative seems to have some *prima facie* intuitive appeal.

This intuitive appeal is almost certainly why this approach was suggested by the Privy Council in *Newton's Case*.⁷⁶ Trebilcock discusses the approach of the Privy Council in this case, which is described as a test of "plausibility." More specifically, the test is framed as applying to the tax avoidance conduct of taxpayers where "it is possible to predicate by reference to the overt acts by which it was implemented that its purpose was the avoidance of tax, being not explicable as 'an ordinary business or family dealing.'" ⁷⁷

There is a significant concern associated with unearthing in a compelling way a taxpayer's motivation or intent in pursuing a certain course of conduct. In the UK, the House of Lords in the *Duke of Westminster* appeal were disinclined to consider the fact that he had been motivated by a desire to avoid surtax as a factor in adjudicating the success of the Duke's plan to avoid the relevant surtax. Indeed, it was quite clear from the evidence adduced that the Duke's plan was to avoid the surtax. This fact apparently played no role in the outcome, which famously favoured the Duke.⁷⁸

Trebilcock's own view coincided to a significant extent with that of the House of Lords in the *Duke of Westminster*, as illustrated by the following passage:

What is an 'ordinary' business or family dealing? One can accept

⁷⁶ Discussed by Trebilcock, *ibid*.

⁷⁷ *Ibid*.

⁷⁸ See the quote from Lord Tomlin's speech, *supra* note 42.

as necessary, in many contexts, the concept of the reasonable man, and as necessary evils, the difficulties to which it gives rise, but with respect to the Privy Council in *Newton's Case*, 'ordinary' business or family dealing is an almost impossible conception. The combination of circumstances which may comprise a business or family dealing is infinite. It is impossible to characterize any one combination or class of circumstances as ordinary and all others as extraordinary. It does not follow that a dealing which has the effect of avoiding tax and which is extraordinary in some way must inevitably as a matter of logic, have a purpose of avoiding tax. It is one thing to say that a dealing is extraordinary; it is quite another to say that it has the purpose of avoiding tax.⁷⁹

Trebilcock continues, stating that the rule suggested by the Privy Council in *Newton's Case* is "little more than an injunction to the courts to exercise discrimination in the application of the section."⁸⁰

Indeed, Trebilcock is skeptical of the value of the ordinary business or family dealing test enunciated by the Privy Council in *Newton's Case*, stating that it is "little more than the recognition of a judicial discretion to determine and strike down 'obvious' attempts at tax avoidance, yet to so delimit the sphere of operation of the section as to leave untouched transactions occurring in the normal flow of business or family affairs whether or not these transactions have the effect of avoiding tax, and whether or not they are animated by this purpose."⁸¹ His conclusion on this point is no rosier: "a proposition unfounded in authority, disregarded by the courts, and largely imprecise in nature, is likely to prove to those who rely upon it, a disappointing and insubstantial ally."⁸²

In light of the foregoing, Trebilcock can be interpreted as raising three related but distinct objections to the conceptual coherence of GAARs. The first is that the concept of "tax avoidance" is difficult to define; it suggests that a certain quantum of tax liability is inevitable. At an extreme it would suggest that taxpayers have an obligation to maximize tax liability. The second builds on the first, suggesting that because tax legislation itself contemplates some attractive tax concessions, it is dangerous and difficult to go beyond the statutory text to try to discern what policies are being promoted and adopted. The related third objection

⁷⁹ See Trebilcock, *supra* note 64 at 241.

⁸⁰ *Ibid.* at 242.

⁸¹ *Ibid.*

⁸² *Ibid.*

is that paying heed and emphasizing a taxpayer's own motivation as being the avoidance of tax also cannot be dispositive and is apt to be uninformative as a guide to fairly and effectively identifying offensive tax avoidance.

IV. THE CANADIAN GAAR AND TREBILCOCK'S CONCEPTUAL OBJECTIONS

Now consider how Trebilcock's conceptual objections to the effectiveness of GAARs have played out in the Canadian context. More specifically, consider the extent to which Trebilcock has been vindicated in his indictment of GAARs considered as a class in light of the Canadian experience, in the construction of the legislation (i.e., in terms of how the Canadian GAAR is textually constructed) and also with respect to its judicial application (i.e., in terms of how the Canadian GAAR has been received by the courts). The Supreme Court of Canada has decided three GAAR appeals in the past four years, two in favour of the government, and one in favour of the taxpayer.⁸³

With regard to the legislation, the most general provision of the Canadian GAAR is subsection 245(2), which provides that, "Where a transaction is an avoidance transaction, the tax consequences to a person shall be determined as is reasonable in the circumstances in order to deny a tax benefit that, but for this section, would result, directly or indirectly, from that transaction or from a series of transactions that includes that transaction."⁸⁴

Subsection 245(2) stipulates that the Canadian GAAR applies to an "avoidance transaction." This term is defined in subsection 245(3) to mean "any transaction" or "series of transactions" that "would result, directly or indirectly, in a tax benefit." Expressly excepted from the definition are transactions or series of transactions that "may reasonably be considered to have been undertaken or arranged primarily for *bona fide* purposes other than to obtain the tax benefit."

This definition of "avoidance transaction" thus raises two further questions: what counts as a "tax benefit" and what is a "*bona fide* purpose"? The definition of "tax benefit" is broad and appears in subsection 245(1) in the Act. A "tax benefit" is defined as "a reduction,

⁸³ The appeals in favour of the government are *Mathew v. Canada*, [2005] 2 S.C.R. 643, 2005 SCC 55; and *Lipson v. Canada*, 2009 SCC 1. The appeal in favour of the government was *Canada Trustco*, *supra* note 27.

⁸⁴ A number of the terms, such as "avoidance transaction," "tax consequences," "tax benefit" and "series of transactions" are specifically defined elsewhere in section 245 or elsewhere in the Act.

avoidance or deferral of tax or other amount payable under this Act or an increase in a refund of tax or other amount under this Act, and includes a reduction, avoidance or deferral of tax or other amount that would be payable under this Act but for a tax treaty or an increase in a refund of tax or other amount under this Act as a result of a tax treaty.” This definition is considered to be wide-ranging and insensitive to the quantum of the benefit conferred.⁸⁵ With respect to the second question raised by the definition of “avoidance transaction” in 245(3), what would constitute a “*bona fide* purpose other than to obtain the tax benefit”? This part of the definition of an “avoidance transaction” definition requires that at least one part of a series of transactions be motivated by a purpose of obtaining the tax benefit. In other words, at least one part of a series of transactions must be regarded as being principally tax motivated. If this requirement is met, then the taxpayer will be regarded as having engaged in an “avoidance transaction.”

A final requirement is stipulated in subsection 245(4), which states that subsection 245(2) applies “only if it may reasonably be considered that the transaction” would “result directly or indirectly in a misuse of the provisions” or “would result directly or indirectly in an abuse having regard to those provisions ...read as a whole”. This is commonly referred to as the “misuse or abuse” requirement.

What can one say about the Canadian GAAR in light of Trebilcock’s conceptual objections? The first is that Trebilcock has anticipated many of the central problems with establishing a standard against tax avoidance in the context of a highly detailed statutory scheme. The Canadian GAAR exhibits all three problems at different levels.

Consider first the definition of “avoidance transaction.” In order to be considered an “avoidance transaction” there must be some element of the transaction that is principally tax motivated. This requires examining the taxpayer’s purpose, which Trebilcock is skeptical of doing so effectively. If every element of the transaction can be accounted for as being “for *bona fide* purposes other than to obtain the tax benefit” then the transaction will be outside of the scope of the GAAR. This invites too much judicial discretion in Trebilcock’s view.

These concerns are amplified even more in the context of determining

⁸⁵ See the decision of the Supreme Court of Canada in *Canada Trustco*, *supra* note 27 at para. 19, where the Court remarks with respect to statutory use of the term ‘tax benefit’ that, “Whether a tax benefit exists is a factual determination, initially by the Minister and on review by the courts, usually the Tax Court. The magnitude of the tax benefit is not relevant [...]”

whether there has been a misuse or abuse within the meaning of 245(4). Even if there has been, for example, a transaction that is principally motivated by securing a tax benefit, the Minister must show that it was a misuse or abuse of the provisions of the Act (or some other relevant instrument) that violates the “object and spirit” of the legislation. On this count, it appears *prima facie* that the Canadian GAAR fares well relative to Trebilcock’s skepticism. Return to Trebilcock’s example of a taxpayer discontinuing working overtime. In this case it seems quite clear that the Minister would be wholly incapable of showing that the taxpayer’s tax motivated refusal to work additional overtime would run afoul of, misuse, or abuse any of the provisions of the Act. On the other hand, where the “object and spirit” of the legislation is less clear, and reference must be made to legislative purpose or intention, Trebilcock’s skepticism would seem manifestly warranted.

At around the time the GAAR was introduced one Canadian commentator, Joel Nitikman, asked whether the Canadian GAAR is void for vagueness.⁸⁶ As far as I know, no Canadian court has seriously considered declaring the GAAR void for vagueness in the ensuing twenty years. The question was rooted in the observation that it is difficult to determine what the purpose of the Act is, what the legislative intention was, and hence what constitutes a misuse or abuse. The analysis proceeded on the basis that since the law is set by the text of the legislative provision, the “GAAR’s validity must stand or fall on the basis of the wording of GAAR itself” and that “any extralegislative material, such as technical notes from the Department of Finance ... must be ignored.”⁸⁷ In addition, the vagueness is rooted in the unknown standard that it sets for tax avoidance; more specifically, “GAAR is uncertain not so much in its meaning as in its potential application.”⁸⁸ The tentative conclusion reached was that, indeed, the GAAR “is void for vagueness.”⁸⁹ Nitikman’s conclusion states,

The vagueness in GAAR is apparent when one envisions a series of unrelated transactions and tries to determine with any degree of certainty whether these transactions result in a tax benefit, whether they result in a misuse of a provision of the Act or in an abuse, and

⁸⁶ Joel Nitikman, “Is GAAR Void for Vagueness?” (1989) 37(6) *Canadian Tax Journal* 1409.

⁸⁷ *Ibid.* at 1435.

⁸⁸ *Ibid.*

⁸⁹ *Ibid.* at 1443.

what the tax consequences might be if one were caught by GAAR. We appear to have moved from the right to order our transactions, if we can, so as to minimize taxes, to simply ordering our transactions and hoping for the best.⁹⁰

This aligns well with Trebilcock's conceptual objections, and suggests that his concerns have not been dissolved with the Canadian GAAR.

That the argument that the GAAR is void for vagueness—though it is probably one that Trebilcock would have found congenial given his conceptual objections—has not been warmly received by the courts is probably most easily explained by the reluctance that the Canadian courts have had in finding that taxpayers have run afoul of the GAAR. Indeed, there is a strong adherence to the view that the GAAR is an exceptional remedy that can be applied only after all the other provisions of the Act have been considered, and that the *Duke of Westminster* principle is well-entrenched in Canadian income tax law.⁹¹

The survival of the *Duke of Westminster* principle is exhibited by the repeated reference by the justices at the Supreme Court of Canada to the principle by name, and also the emphasis the Court places on the three values of predictability, certainty, and fairness, even as they have applied the GAAR on two occasions out of three opportunities in the past five

⁹⁰ *Ibid.* at 1447.

⁹¹ The latest Supreme Court of Canada judgment addressing the GAAR, *Lipson v. Canada*, 2009 SCC 1, makes reference to the *Duke of Westminster* decision several times. For example, the majority reasons given by LeBel J. state at paragraph 21 that:

It has long been a principle of tax law that taxpayers may order their affairs so as to minimize the amount of tax payable (*Commissioners of Inland Revenue v. Duke of Westminster*, [1936] A.C. 1 (H.L.)). This remains the case. However, the *Duke of Westminster* principle has never been absolute, and Parliament enacted s. 245 of the ITA, known as the GAAR, to limit the scope of allowable avoidance transactions while maintaining certainty for taxpayers.

The dissenting reasons of Binnie J. begin with the following, “How healthy is the *Duke of Westminster*? There is cause for concern.” At para. 98 Binnie J. concludes that,

I do not believe the Minister has shown that the abusive nature of this transaction is “clear”. The application of the GAAR in these circumstances, in my respectful view, means paying lip service to the *Duke of Westminster* principle without taking seriously its role in promoting consistency, predictability and fairness in the tax system.

years⁹² to disallow the tax benefits accruing to taxpayers from tax avoidance transactions.⁹³

V. CONCLUSION

It will probably not come as a shock to any serious scholar that even removed five decades in time and half-a-world away in space from the University of Adelaide that Trebilcock's analysis indentified the shortcomings in the GAAR of the day and in fact anticipated many of the types of systemic issues GAARs would have to overcome to become more effective and useful to governments—for example, by being more specific about what the hallmarks of the offensive transactions would be. Nevertheless, despite these efforts at improving and sharpening GAARs, their effectiveness and utility continues to be bounded for the broad conceptual reasons Trebilcock adumbrated.

Although GAARs are probably not as conceptually flawed as Trebilcock—perhaps out of youthful exuberance, perhaps out of a penchant for “throwing deep”—made them out to be, as the recent 4-3 Supreme Court of Canada decision in *Lipson* shows,⁹⁴ they are still unwieldy and difficult to apply. It is tempting to lament that it is too bad that Trebilcock abandoned further work in income tax law (and more specifically, tax avoidance) in order to focus on other areas of scholarly interest. Perhaps, too, however, this is just another example of Trebilcock rationally and coolly staking out what appeared to him to be the most important and overlooked salient arguments in an area before seeking out new and interesting areas where he could make important contributions.

In light of the conceptual challenges Trebilcock identified and the limited progress that has been made in GAAR technology since he authored his LL.M. thesis, Trebilcock's decision to put his abundant talents to work in other areas looks astute. We can hardly be surprised. We should expect nothing less from a path-breaking and socially-minded law and economics scholar with a penchant for throwing deep.

⁹² The two cases are *Lipson*, *ibid*, and *Mathew v. Canada*, [2005] 2 S.C.R. 643, 2005 SCC 55, which was the companion appeal to *Canada Trustco*, *supra* note 27.

⁹³ The justices appear to be reluctant to hear more GAAR appeals, however. This is a reasonable inference from the Court's characterization of the misuse or abuse requirement of subsection 245(4) of GAAR cases as being a “finding of fact.” See *Canada Trustco*, *ibid.*, at para. 45. Because findings of fact are based on the evidence adduced at trial, they are far less susceptible to appeal and will be overturned usually only in the presence of “palpable and overriding error” on the part of a trial judge: *Housen v. Nikolaisen*, [2002] 2 S.C.R. 235, 2002 SCC 33, at para. 10.

⁹⁴ See *Lipson*, *supra* note 92.