

Michael J. Trebilcock is by all accounts one of his generation's most prolific and important scholars of law and economics. Through more than 200 articles, book chapters, books, edited volumes, and other academic publications, Trebilcock has made lasting contributions to many fields, including contracts, torts, consumer protection, antitrust, international trade, immigration, regulation, and law and development. In recognition of his teaching and research, he has received awards and distinctions from students, universities, governments, and scholarly societies. The symposium for which this essay was prepared is only the latest token of appreciation for Trebilcock's profound and prominent contributions to the intellectual depth and breadth of legal thought. 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. Most readers of Trebilcock's more discussed work will not be aware that his scholarly career began, inauspiciously as it might seem, nearly five decades ago with a 224-page LLM thesis at the University of Adelaide. Almost unbelievably, this substantial piece of work was dedicated to analysing just a single provision of Australian income-tax law: a general anti-avoidance rule 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 his early tax scholarship.

Keywords: tax avoidance/income tax/anti-avoidance/general anti-avoidance rules/taxation

1 Introduction

Through more than 200 articles, book chapters, books, edited volumes, and other academic publications, Michael Trebilcock has made lasting contributions to many fields, including (and this is a partial list) contracts, torts, consumer protection, antitrust, international trade, immigration, regulation, and law and development. For these efforts and contributions he has been richly decorated with awards, prizes, and fellowships too numerous to list. And yet, despite the accolades, the attention, and the amply 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, most readers of Trebilcock's more discussed work will not be acquainted with the fact that his scholarly career began nearly five

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† Thanks go to an anonymous referee, as well as to Tony Duggan and Karen Knop for helpful suggestions.

decades ago with a 224-page LLM thesis at the University of Adelaide.¹ Almost unbelievably, this substantial piece of work was dedicated to analysing 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 his tax scholarship.

Trebilcock's LLM 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 formulating the appropriate government response to the corrosive effects on public revenues of aggressive tax planning. More specifically, the thesis explored the limits of the effectiveness of s. 260 of Australia's Income Tax Assessment Act.² At the time, s. 260 established a 'general anti-avoidance rule' (GAAR), which was 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 LLM 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 another flurry of cases in the 1950s and 1960s.³ Trebilcock argued, in the wake of this renewed interest and application of s. 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.

An observation befitting a law and economics scholar (*i.e.*, one that is two-handed) is in order before proceeding further. On the one hand, it is interesting to note that as an Australian graduate student Trebilcock was writing before the law and economics movement had seriously taken hold as an academic field. It would be unreasonable, for example, to expect that, writing as a graduate student in the early 1960s in Adelaide, Trebilcock would frame his analysis as he would if he were addressing the same topic today in Toronto. Indeed, at the time when he wrote his LLM thesis he had little (if any) economics training. It would be utterly inconceivable for him to have produced an explicitly economic analysis of tax avoidance in preparing his thesis. The model of legal scholarship in the early 1960s in Australia was doctrinal and aimed principally

1 I am grateful to Michael Trebilcock for sharing an original bound version of his LLM thesis: M.J. Trebilcock, *Section 260 of the Income Tax Assessment Act: A Study in the Combating of Tax Avoidance* (LLM Thesis, University of Adelaide, 1964) [Trebilcock, *Section 260*].

2 *Income Tax Assessment Act 1936* (Cth.), s. 260.

3 For additional details see M.J. Trebilcock, 'Section 260: A Critical Examination' (1964) 38 *Austl.L.J.* 237 at 237 [Trebilcock, 'Section 260'].

at providing materials useful to the bench and bar.⁴ Trebilcock's thesis thus is – unsurprisingly, given the time and place – consistent with this prevalent doctrinal focus.

On the other hand, it will not come as a shock to any legal scholar familiar with Trebilcock's work that his analysis sharply identified the shortcomings of the GAAR of the day. 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, the central claim of this examination of Trebilcock's work on tax avoidance is that although he was purporting principally to analyse the Australian GAAR, Trebilcock – nearly five decades ago, and half a world away – presaged many of the challenges, struggles, and obstacles faced in subsequent battles by governments against aggressive tax avoidance, in Canada and throughout the English-speaking world, in the ensuing half-century.

Two weaknesses of Trebilcock's thesis are worth mentioning, and both are camouflaged strengths. The first is that the analysis is at points perhaps overly pessimistic regarding the prospects of an efficacious GAAR. A second would be that Trebilcock assumes, without explaining why, that strict interpretation of tax legislation will continue indefinitely (it has not – or, at least, has not officially). With respect to the first observation, 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. Nevertheless, beginning with a 2005 discussion paper by the South African Revenue Agency, there has arguably been some headway made in addressing the conceptual challenges identified by Trebilcock's analysis in South Africa.⁵ With respect to the second observation, the Supreme Court of Canada continues to prioritize the text of the Income Tax Act in its interpretative strategy (though it also considers the context and purpose of the provisions of the legislation as well). The text is prioritized by the Court because of the difficulties associated with reading detailed technical rules in a purposive manner. In addition, Tim Edgar has recently argued persuasively that statutory interpretation plays a limited

4 See Erwin N. Griswold, 'Observations on Legal Education in Australia' (1952) 5 J. Legal Educ. 139; Michael Chesterman & David Weisbrot, 'Legal Scholarship in Australia' (1987) 50 Mod.L.Rev. 709.

5 I am grateful to an anonymous referee for this observation. For the relevant discussion paper issued by the tax authorities in South Africa see South African Revenue Service, *Discussion Paper on Tax Avoidance and Section 103 of the Income Tax Act* (2005), online: South African Revenue Service <<http://www.sars.gov.za/home.asp?pid=5981>>.

role in tax-avoidance cases.⁶ Despite these weaknesses, however, Trebilcock's LLM thesis travels remarkably well.

The remainder of this 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 LLM thesis, borrowing also from the law review article⁷ that Trebilcock subsequently published as an abridged version of the arguments from that thesis. Part IV examines the three conceptual issues that Trebilcock's work raises against the developments in Canada's battle against aggressive tax avoidance post-1988, with the introduction of the Canadian GAAR. The Canadian GAAR is used throughout only as a representative experience with a GAAR, for the purposes of illustrating how Trebilcock's broadest insights have withstood the twin tests of time and space. 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 *A 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 *Stuart Investments Ltd. v. The Queen*.⁸

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 United Kingdom.⁹ 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 *Stuart* in 1984, the federal government fully embraced 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

6 See Tim Edgar, 'Building a Better GAAR' (2008) 27 Va. Tax Rev. 833 at 833 [Edgar, 'Better GAAR'] ('the relevance of statutory interpretation in the identification of prohibited [tax avoidance] behavior should be much more limited than is currently the case').

7 Trebilcock, 'Section 260,' *supra* note 324.

8 [1984] 1 S.C.R. 536, [1984] C.T.C. 294, 84 D.T.C. 6305 [*Stuart* cited to S.C.R.].

9 See Benjamin Alarie & David Duff, 'The Legacy of UK Tax Concepts in Canadian Income Tax Law' [2008] Brit. Tax Rev. 228 [Alarie & Duff, 'Legacy'].

attendance to legal substance of transactions. Both influences were inherited from the United Kingdom,¹⁰ and both contributed significantly to tax avoidance.¹¹ As early as 1966, Canada's Royal Commission on Taxation (the Carter Commission) explained in its exhaustively researched report¹² that in its view tax avoidance was undesirable for several reasons, including (i) the reduced tax revenues received by the government; (ii) 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 in the future, to bear the burden of taxes avoided.¹³ 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 in the 1970s by an emerging openness 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.'¹⁴ 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 United States.¹⁵ It contrasted significantly with the adherence in the United Kingdom to the legal substance of transactions, which had been famously established by the House of Lords in the *Duke of Westminster* case.¹⁶

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 United Kingdom and the fact that

10 For an extensive discussion see *ibid.*

11 See c. 3 of David G. Duff *et al.*, *Canadian Income Tax Law*, 3d ed. (Markham, ON: LexisNexis, 2009) for a more detailed account.

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

13 *Ibid.*, vol. 3 at 541–2.

14 The key decision in this respect is *M.N.R. v. Leon*, [1976] C.T.C. 532, 76 D.T.C. 6299 (F.C.A.) [*Leon*]. The Federal Court of Appeal in *Leon* held that '[i]t 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.'

15 See text accompanying notes 27–29 *infra*.

16 See text accompanying notes 20–25 *infra*.

the UK tax system did not have a GAAR.¹⁷ Although the United Kingdom has from time to time mooted the possibility of enacting a GAAR, it has not yet done so.¹⁸ But this raises a further question: Why has the United Kingdom itself not encountered problems with tax avoidance leading it to enact a GAAR?

Although the United Kingdom does not have a GAAR, this is not because it has dramatically and effectively succeeded in combating tax avoidance through specific anti-avoidance rules (though it has these). Tax avoidance remains a live concern. The history of anti-avoidance in the United Kingdom combines a strict approach to interpreting income-tax legislation and a strong adherence to the legal substance (as compared with economic substance) of transactions engaged in by taxpayers. This appears to have been motivated by the idea that taxation is punitive and that, as in 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.¹⁹ Indeed, in addition to finding that the legal substance of arrangements is to be focused upon in *Duke of Westminster*, the House of Lords also established the principle that taxpayers are entitled to arrange their affairs so as to minimize the obligation to pay tax.²⁰ The strict approach in the United Kingdom has been abandoned since the early 1980s, however.²¹ The subsequent development of the House of Lords' tax judgments has veered to and fro in its hostility to tax avoidance.²² With the further guidance provided by the 2004 decisions of the House of Lords in *Barclays Mercantile*²³ and *Scottish Provident*,²⁴ it is clear now that the position in the United Kingdom is that taxation statutes should be given a purposive interpretation, just as should any other legislation.

17 Rachel Anne Tooma, *Legislating Against Tax Avoidance* (Amsterdam: IBFD, 2008) at 54 [Tooma, *Legislating*].

18 *Ibid.*

19 See Alarie & Duff, 'Legacy,' supra note 9.

20 *Commissioners of Inland Revenue v. Duke of Westminster*, [1936] A.C. 1 (H.L.) [*Duke of Westminster*]. The most commonly quoted phrase from the decision is from the speech of Lord Tomlin, who 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.

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

22 See the discussion in Tooma, *Legislating*, supra note 17 at 54–63.

23 *Barclays Mercantile Business Finance Ltd. v. Mawson*, [2004] UKHL 51.

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

The purposive approach to statutory interpretation has also been adopted by the Supreme Court of Canada,²⁵ and here in Canada it has come to be known as the ‘textual, contextual, and purposive’ approach, signalling the ongoing predominant influence of the text of the act.

Although it is clear that UK tax law has moved toward a more pragmatic method of interpreting incometax 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 United States. The United States, like the United Kingdom, does not have a GAAR. In the United States, the need for a GAAR has arguably been less acute, in large part because American courts have been more aggressive in tackling tax avoidance. More specifically, the US Supreme Court’s 1935 judgment in *Gregory v. Helvering, Commissioner of Internal Revenue*²⁶ 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 contrasts sharply with the approach of the House of Lords in *Duke of Westminster*.²⁷ Canada has been (whether this is for the better or worse is unclear) more influenced by the House of Lords and *Duke of Westminster* than by the US Supreme Court and *Gregory v. Helvering*.²⁸

And yet a number of considerations, not least the revenue needs of a federal government severely in the red in the mid- to late 1980s, prompted Canada’s foray into the implementation of a GAAR. This foray took shape after the Supreme Court’s decision in *Stubart*. In rejecting a more intrusive inquiry into a taxpayer’s motivations, the Court was motivated in part by an existing provision denying deductions that would ‘unduly or artificially reduce’ a taxpayer’s income.²⁹ The relevant provision at the time when *Stubart* was decided provided that ‘[i]n 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

25 The original move in abandoning strict interpretation came in the Court’s judgment in *Stubart*, supra note 8.

26 293 U.S. 465 (1934) [*Gregory v. Helvering*].

27 The contrast between the US result in *Gregory v. Helvering* and the UK result in *Duke of Westminster* is subjected to illuminating scrutiny in Assaf Likhovski, ‘The Duke and the Lady: *Helvering v. Gregory* and the History of Tax Avoidance Adjudication’ (2004) 25 *Cardozo L.Rev.* 953.

28 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 United States, it probably makes more sense.

29 *Stubart*, supra note 8 at 557: ‘The presence of a provision of general application to control 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.’

reduce the income.³⁰ This provision was almost entirely ineffective in combating tax avoidance, and it was repealed when the GAAR was introduced in 1988, following extensive consultations and discussions with the Canadian tax community.³¹

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 effective in combating the most egregious and aggressive tax-avoidance schemes without 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, then 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.'³² 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.'³³

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 to accompany 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 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.³⁴

It seems unlikely that Canadian policy makers were blind to the challenges facing the effective implementation of a GAAR. They probably foresaw 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. Perhaps, in adopting the GAAR in 1988, Canadian policy makers had abundant confidence in the courts to apply the GAAR effectively. Perhaps they

30 Ibid. at 546.

31 For an excellent account of this history and the prospects of the Canadian GAAR see Brian J. Arnold & James R. Wilson, 'The General Anti-Avoidance Rule – Part I' (1988) 36 *Can. Tax J.* 829, 1123, & 1369.

32 David A. Dodge, 'A New and More Coherent Approach to Tax Avoidance' (1988) 36 *Can. Tax J.* 1 at 3.

33 Ibid.

34 Department of Finance, *Explanatory Notes to Legislation Relating to Income Tax* (Ottawa: Department of Finance, 1988) at 313.

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 they 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 policy makers had paid attention to Trebilcock's earlier work, they would perhaps not have been so optimistic about the prospects of the new GAAR for 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*

Section 260 of the Australian Income Tax Assessment Act at the time provided, in part, that any 'contract, agreement, or arrangement' insofar 'as it has or purports to have the purpose or effect 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 proceeding under this Act, but without prejudice to such validity as it may have in any other respect or for any other purpose.' 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 would have been ambitious enough for Trebilcock to point out the numerous quandaries and issues associated with the interpretation and application of this provision. It appears, however, that Trebilcock has always been inclined to, in the words of former NFL quarterback Kenny 'The Snake' Stabler, 'throw deep.' He went for s. 260's jugular. The introductory chapter of Trebilcock's LLM thesis declares boldly that

[t]he 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.³⁵

This is indeed 'throwing deep.'

For one thing, even if Trebilcock can be granted the claim that s. 260 was apt to be 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 Income Tax Act. The more obvious response,

³⁵ Trebilcock, *Section 260*, supra note 1 at 25.

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 that, therefore, no amendment of s. 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 to taking 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,³⁶ because for the claim to fail, Trebilcock would have only to be confronted with one effective GAAR (or one 'black swan'); correspondingly, for the claim to 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 s. 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 tax legislation. 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.

Finally, Trebilcock's thesis was audacious in that to sustain it, he was forced to argue that those cases in which the provision had been found to be validly and successfully applied by the Australian government had been wrongly decided and had reached indefensible outcomes – a high burden indeed for an LLM thesis.³⁷ 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?'³⁸ Or, as he puts it later, 'What constitutes an avoidance of

36 See Nassim Nicholas Taleb, *The Black Swan: The Impact of the Highly Improbable* (New York: Random House, 2007).

37 Trebilcock himself notes that 'judicial interpretation . . . has rendered the section very far from impotent': Trebilcock, 'Section 260,' *supra* note 3 at 237.

38 *Ibid.* at 238.

liability to tax?³⁹ This was conceptually difficult, in Trebilcock's view, because after 'a liability has been incurred by a taxpayer, there is nothing he can do, by private bargaining or otherwise, to displace it.'⁴⁰ 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?'⁴¹ What conditions show that tax liability has been sidestepped? In Trebilcock's view, 'no future liability to tax can strictly be regarded as inevitable.'⁴²

As an example, Trebilcock argued 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 by choosing not to work overtime.⁴³ 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

39 Ibid.

40 Ibid.

41 Ibid.

42 Ibid. at 239.

43 Ibid.

tax liability will trigger the application of a GAAR. Instead, there must be a further distinction made between objectionable and unobjectionable tax avoidance, and ‘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’?

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 are 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 trade-offs among them, often within a politically contested environment. Moreover, although it is clear that one 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 a GAAR is intended to counter 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.

It cannot be the case, Trebilcock notes, 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, is 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.’⁴⁴ According 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

44 Ibid. at 240.

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.⁴⁵

It follows for Trebilcock that because of the presence of explicitly authorized and 'legally permissible forms of tax avoidance,'⁴⁶ scepticism 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, on the other hand, 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.⁴⁷

Trebilcock also notes 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 mistaken.'⁴⁸

The insight underlying Trebilcock's second conceptual objection relates to the problem of reconstructing the purposes and intentions of a text that has been drafted, revised, debated, voted upon, passed, and amended and has 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 on 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

45 Ibid.

46 Ibid.

47 Ibid. at 241.

48 Ibid.

understanding of the demands placed on taxpayers through the provisions constituting incometax 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 the views of a majority of the other legislators. All that makes up the incometax 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; rather, 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 distinguish objectionable from unobjectionable means of not incurring tax liability 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 the taxpayer's own motivation in pursuing a given course of conduct. More specifically, if a taxpayer is motivated entirely by the goal of 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 or not to choose to work overtime, 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 incometax rates the additional tax liability could be said to be the primary motivation for a taxpayer who turns down the opportunity to work overtime. The idea of focusing on a taxpayer's motivation in not choosing the 'highest tax' alternative, then, 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 v. Federal Commissioner of Taxation*.⁴⁹ The approach 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.”’⁵⁰

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 United Kingdom, the House of Lords in the *Duke of Westminster* appeal were disinclined to consider the fact that the duke had been motivated by a desire to avoid surtax as a factor in adjudicating the success of his plan to avoid the relevant surtax. Indeed, it was quite clear from the evidence adduced that his plan was to avoid the surtax; this fact apparently played no role in the outcome, which famously favoured the duke.⁵¹

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

What is an ‘ordinary’ business or family dealing? One can accept 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.⁵²

Trebilcock continues by 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.’⁵³

49 (1958), 98 C.L.R. 1 (P.C.), discussed by Trebilcock, ‘Section 260,’ supra note 3.

50 Trebilcock, ‘Section 260,’ *ibid.*

51 See quoted passage from Lord Tomlin’s speech in *Duke of Westminster*, supra note 20 at 19–20.

52 Trebilcock, ‘Section 260,’ supra note 3 at 241.

53 *Ibid.* at 242.

Trebilcock is also sceptical of the value of the ‘ordinary business or family dealing’ test, 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.⁵⁴

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.’⁵⁵

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 several years, two in favour of the government and one in favour of the taxpayer.⁵⁶

The most general provision of the Canadian GAAR is s. 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.⁵⁷

Subsection 245(2) stipulates that the Canadian GAAR applies to an ‘avoidance transaction.’ This term is defined in s. 245(3) as meaning ‘any

54 *Ibid.*

55 *Ibid.*

56 The appeals decided in favour of the government are *Mathew v. Canada*, 2005 SCC 55, [2005] 2 S.C.R. 643 [*Mathew*]; *Lipson v. Canada*, 2009 SCC 1 [*Lipson*]. The appeal decided in favour of the taxpayer was *Canada Trustco Mortgage Co. v. Canada*, [2005] 2 S.C.R. 601, 2005 SCC 54 [*Canada Trustco*].

57 A number of the terms, such as ‘avoidance transaction,’ ‘tax consequences,’ ‘tax benefit,’ and ‘series of transactions,’ are specifically defined elsewhere in s. 245 or elsewhere in the act. *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.).

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 s. 245(1) of the Act. A 'tax benefit' is defined as

a reduction, avoidance or deferral of tax or other amount payable under this Act or an increase in a refund of tax or other amount under this Act, 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.⁵⁸ With respect to the second question raised by the definition of 'avoidance transaction' in s. 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 the 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 s. 245(4), which states that s. 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 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,' a transaction must have some

58 See the decision of the Supreme Court of Canada in *Canada Trustco*, supra note 56 at para. 19, where the Court remarks with respect to statutory use of the term 'tax benefit' that '[w]hether 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 ...'

element that is principally tax motivated. This requires examining the taxpayer's purpose, which Trebilcock is sceptical about. 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 the scope of the GAAR. This invites too much judicial discretion, in Trebilcock's view.

These concerns are amplified in the context of determining whether there has been a misuse or abuse within the meaning of s. 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 scepticism. 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 legislation. 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 scepticism 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.⁵⁹ 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 an abuse. Nitikman's analysis proceeds 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.'⁶⁰ In addition, the vagueness is rooted in the unknown standard that the GAAR sets for tax avoidance; more specifically, 'GAAR is uncertain not so much in its meaning as in its potential application.'⁶¹ The tentative conclusion reached was that, indeed, the GAAR 'is void for vagueness.'⁶² 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

59 Joel Nitikman, 'Is GAAR Void for Vagueness?' (1989) 37 Can.Tax J. 1409.

60 *Ibid.* at 1435.

61 *Ibid.*

62 *Ibid.* at 1443.

transactions result in a tax benefit, whether they result in a misuse of a provision of the Act or in an abuse, and 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.⁶³

This aligns well with Trebilcock's conceptual objections, and it suggests that his concerns have not been dissolved with the Canadian GAAR. Trebilcock's conceptual concerns are also well reflected in recent theoretical work by Tim Edgar on improving GAARS through a better understanding of their workings.⁶⁴

That the argument that the GAAR is void for vagueness has not been warmly received by the courts is probably most easily explained by the Canadian courts' reluctance to find 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 Income Tax Act have been considered, and that the *Duke of Westminster* principle is well entrenched in Canadian income-tax law.⁶⁵

The survival of the *Duke of Westminster* principle is exhibited by the repeated reference by justices of the Supreme Court of Canada to the principle by name, and also by 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 several years⁶⁶ to disallow the tax benefits accruing to taxpayers from tax-avoidance transactions.⁶⁷

V Conclusion

Despite the five decades that have passed since Trebilcock wrote his LLM thesis half a world away at the University of Adelaide, his analysis

63 Ibid. at 1447.

64 See Edgar, 'Better GAAR,' supra note 6.

65 The latest Supreme Court of Canada judgment addressing the GAAR makes reference to the *Duke of Westminster* decision several times: *Lipson*, supra note 56, e.g. at para. 2, per LeBel J., and para. 98, per Binnie J. (dissenting).

66 The two cases are *Lipson*, *ibid.*, and *Matheu*, supra note 56, which was the companion appeal to *Canada Trustco*, supra note 56. The decisions of the lower courts in these appeals have also been erratic, and the minister has met with only mixed success.

67 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 s. 245(4) of GAAR cases as 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 usually be overturned only in the presence of 'palpable and overriding error' on the part of a trial judge: *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235 at para. 10.

identified the shortcomings in the GAAR of the day and, in fact, anticipated many of the types of systemic issues that GAARS would have to address in order 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 adumbrated by Trebilcock.

Although GAARS are probably not as conceptually flawed as Trebilcock made them out to be, as the recent 4–3 Supreme Court of Canada decision in *Lipson* shows,⁶⁸ they are still unwieldy and difficult to apply. In light of the conceptual challenges identified by Trebilcock and the limited progress that has been made in GAAR technology since he authored his LLM 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.

68 *Supra* note 56.