

GST/HST ADMINISTRATION

THE INCONSISTENT TREATMENT OF GST/HST PRIORITIES

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Inconsistent Treatment of GST Priorities in CCAA between Alberta and Ontario

On December 19, 2003, the Ontario Superior Court of Justice rejected following two Alberta Court of Queen's Bench decisions,¹ in finding that GST deemed trusts do not survive a *Companies' Creditors Arrangement Act* ("CCAA")² proceeding, with the result that the Crown loses its super-priority. The federal Crown had sought priority in relation to GST collectible/collected by the Ottawa Senators hockey club. The *Ottawa Senators* decision leads to harmonious treatment of GST claims in Ontario under the two principal pieces of federal insolvency legislation, the *Bankruptcy and Insolvency Act* ("BIA")⁴ and the CCAA.⁵ In Alberta, however, previous case law supports inconsistent treatment of GST claims between the BIA and CCAA.

GST Deemed Trusts

Section 222 of the *Excise Tax Act* ("ETA")⁶ establishes a statutory scheme whereby monies collected as or on account of GST (or property equal to the value thereof) are deemed to be held separate and apart from the debtor's estate. Since the deemed trust monies or property do not form part of the debtor's estate, they are not available to the debtor's creditors (other than the Crown) to satisfy their claims. The Crown thereby avoids having its GST claims subject to the general distribution scheme available to secured and unsecured creditors. The Crown, in effect, acquires a super-priority in satisfaction of its GST deemed trust claim.

ETA and CCAA Conflict

The source of the conflicting jurisprudence between Alberta and Ontario is found in inconsistencies between the ETA and the CCAA. Subsections 222(1.1) and (3) of the ETA provide that a GST deemed trust does not survive a bankruptcy. The Crown, therefore, does not enjoy a super-priority for a GST deemed trust relating to any GST liability arising before a bankruptcy. Section 222 makes no reference to an exception from the GST super-priority in the case of a CCAA proceeding, however.

In this regard, section 18.3 of the CCAA directly conflicts with section 222 of the ETA. According to this CCAA provision, only a GST trust at common law ("legal trust") can retain its integrity and priority in a CCAA proceeding.

Typically, a legal trust is not present because of an inability to trace any GST trust monies into the debtor's hands. The debtor would not normally retain a separate bank account for segregated GST monies collected in trust on behalf of the Crown. In fact, Parliament designed the statutory GST deemed trust scheme to overcome the problem of the absence of a legal trust, so that the Crown could establish a super-priority for monies collected as or on account of GST, even where such GST monies are co-mingled with other monies.⁷

Alberta Jurisprudence

Two Alberta Queen's Bench decisions found that the GST deemed trust does establish a super-priority in a CCAA proceeding. The GST deemed trust legislation was amended (in 2000), subsequent to the CCAA amendments introducing section 18.3 (in 1997). Had Parliament intended to make an exception from the super-priority of the GST deemed trust in CCAA proceedings, it could have explicitly said so in 2000 when it amended the GST deemed trust provisions. Parliament explicitly did so in the case of the BIA. The Alberta Queen's Bench invoked the "implied *repeal* rule" of statutory interpretation, by which the more recently enacted provisions must prevail to the exclusion of earlier, conflicting provisions.

Ottawa Senators Case (Ontario)

In the *Ottawa Senators* case, the Ontario Superior Court of Justice applied the "implied *exception* rule" of statutory interpretation, by which the earlier, more specific amendments contained in section 18.3 of the CCAA are read as an exception to the later, GST deemed trust amendments imposed by the ETA (a general taxing statute). The Court was persuaded by the underlying policy considerations for harmonizing the treatment of the Crown's GST claims under the BIA and CCAA. One intention of the recent reform and overhaul of federal insolvency legislation during the 1990s was to harmonize and rational-

¹ *Solid Resources Ltd., Re* [2003] G.S.T.C.21, 40 C.B.R. (4th) 219 (Alta. Q.B.); and *Gauntlet Energy Corp. (Re)*, [2003] A.J. No. 1062, 2003 ABQB 718 (Alta. Q.B.).

² R.S.C. 1985, c. C-36, as amended.

³ *Ottawa Senators Hockey Club Corp., Re*. (December 19, 2003), Doc. 03-CV-22850 (Ont. S.C.J.).

⁴ R.S.C. 1985, c. B-3, as amended.

⁵ The *Ottawa Senators* decision is consistent with an earlier Ontario Superior Court judgment decided before the two Alberta Court of Queen's Bench decisions. See *Blue Star Battery Systems International Corp. Re*, In the Matter of the CCAA, In the Matter of a Plan of Compromise or Arrangement of Blue Star Battery Systems International Corp. and Blue Star Systems Canada Corp., 2000 Carswell Ont. 4837, [2001] G.S.T.C. 2, 10 B.L.R. (3d) 221 (Ont. S.C.J. [Commercial List]).

⁶ R.S.C. 1985, c E-15, as amended.

⁷ In *Royal Bank v. Sparrow Electric Corp.*, 143 D.L.R. (4th) 385, [1997] 1 S.C.R. 411, 97 D.T.C. 5089 (S.C.C.), at paragraphs 24 to 29, Mr. Justice Gonthier, in his dissenting judgment, provides a helpful, conceptual analysis of the legal and policy reasons for the development of statutory deemed trusts to safeguard the Crown's interests in tax monies collected.

ize formerly inconsistent treatments under different pieces of federal insolvency legislation. The intent was to discourage insolvency “statute-shopping” to achieve a preferred result, based on an anomaly in one piece of insolvency legislation.

Policy Considerations

The *BIA* and *CCAA* accommodate different needs and objectives. To stay true to their intended objectives, they should discourage creditors from seeking *BIA* protection for an insolvent debtor for the purpose of preventing a GST super-priority, where the flexibility for restructuring permitted by the *CCAA* legislation would better suit the interests of the parties involved. The *BIA* and *CCAA* should be consistent and neutral as to the relative priority of the Crown’s GST claims.

In our view, Parliament intended for the GST deemed trust to collapse in both *BIA* and *CCAA* proceedings. The *BIA*, *CCAA* and *ETA* amendments are, for the most part, consistent with this intention. Only a presumed drafting oversight in amending the GST deemed trust rules in the *ETA* in 2000 prevented this intention from being more clearly expressed. There is no policy justification for inconsistent treatments of GST priorities between the *BIA* and *CCAA*. In fact, it undermines one of the stated policy objectives of federal insolvency reform, which is to rationalize and harmonize different pieces of federal insolvency legislation. Mr. Justice LoVecchio of the Alberta Queen’s Bench admitted as much in *Gauntlet*, but felt bound by the Supreme Court decision in *Dore v. Verdun (City)*,⁸ which applied the “implied *repeal* rule” of statutory interpretation, when he said:

The decision in *Dore* is binding on me and the reasoning in the case dictates that the deemed trust provision of the *ETA* apply in *CCAA* proceedings, notwithstanding ss. 18.3 of the *CCAA*.

Nevertheless, this result is perhaps troubling for insolvency practitioners and insolvency law generally.

...

...The problem is, however, that there is no policy reason to treat GST differently under the *BIA* than it would be treated under the *CCAA*. Further, this distinction is entirely contrary to the rationale of the harmonization.

The disruption of the harmony between the *BIA* and *CCAA* will only encourage statute shopping and may force troubled companies and their creditors to resort to the proposal process under the *BIA* when they might otherwise prefer the flexibility of the *CCAA*. This is particularly troubling given that an unsuccessful proposal under the *BIA* results in automatic bankruptcy whereas a defeated plan under the *CCAA* does not. These potential outcomes are similarly wholly inconsistent with Parliament’s intention embodied in the 1992 and 1997 amendments.

Need for Uniformity — Parliament Should Act

It is time for Parliament to step into the breach and resolve the inconsistent treatment by Alberta and Ontario jurisprudence of Crown GST claims, by amending the *ETA* to add a *CCAA* proceeding as an excepted circumstance to the GST super-priority. This exception would stand alongside the exception for a *BIA* proceeding and be consistent with section 18.3 of the *CCAA* and the presumed intent of Parliament to treat GST claims in the same manner in a *CCAA* proceeding as in a *BIA* proceeding. Alternatively, the Supreme Court of Canada may ultimately settle this issue, hopefully bringing uniformity to the law, across the different pieces of insolvency legislation and across the various provincial and territorial jurisdictions. [This may come to pass, as the Crown has sought leave to take the *Ottawa Senators* case to the Ontario Court of Appeal.]

⁸ 150 D.L.R. (4th) 385, [1997] 2 S.C.R. 862 (S.C.C.).