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## INCOME TAX

### ADMINISTRATION AND ENFORCEMENT

Motion for determination of two questions of law pursuant to *Federal Courts Rules*, SOR/98-106, r. 220 — Questions relating to interpretation of deemed trust provisions in *Income Tax Act*, R.S.C., 1985 (5th Supp), c. 1 (Act), s. 227 that apply to payroll deductions in respect of employee income tax that employers withhold but fail to remit — Questions arose in context of within action by plaintiff (Crown), against defendant relating to proceeds defendant received from its customer H.N.J. Enterprises Ltd. (debtor) after debtor had failed to remit payroll deductions to Crown — Those proceeds resulted from debtor's sale of its business, were applied by defendant in payment of debtor's overdraft with defendant — Defendant is unsecured creditor of debtor — Argued that deemed trust provisions of Act, s. 227 not applying to it; that, when it received proceeds from debtor, it provided value to debtor through reduction of its overdraft — Debtor operated restaurant for 15 years; had employees to whom it paid wages — During debtor's 2013, 2014, 2015 taxation years, debtor withheld, but failed to remit to Canada Revenue Agency (CRA), \$74,518.17 in prescribed amounts under Act, etc. — Amount of \$36 250.86 of payroll source deductions were for employee CPP/EI contributions, employee federal/provincial income taxes, were therefore subject to deemed trust in favour of Crown pursuant to Act, ss. 222, 227 — Debtor eventually ceased operating business, sold it to unrelated third party for \$100 000 — Defendant provided banking services to debtor, its director — Debtor had previously opened business account (corporate account) with defendant in 2004 — Debtor incurred overdrafts on corporate account both before, after sale of business in October 2015, until account was closed in March 2016, making defendant unsecured creditor of debtor — Defendant unaware of debtor's failure to remit payroll source deductions until received notice from CRA in January 2018 — After receiving notice of CRA's claim to \$36 250.86 plus interest, Defendant not paying Crown; thus Crown commenced action — Questions of law be determined herein whether: (1) deemed trust provisions in Act, s. 227 applying to unsecured creditors; (2) unsecured creditors can rely on *bona fide* purchaser for value defence to defend against deemed trust claim — With respect to first question, dispute between parties in this case focussed upon operation of Act, s. 227(4.1) — Deemed trust created thereby imposed both on property of tax debtor, property held by any secured creditor of tax debtor that, but for security interest, would be property of tax debtor — Present dispute involved situation where debtor no longer held its property — Defendant of view that once money conveyed by debtor to defendant, deemed trust no longer applied, that s. 227 provisions not applying to unsecured creditors in that context — Crown disagreed with defendant's position, relied on language at end of Act, s. 227(4.1) requiring proceeds of deemed trust property be paid to Crown — Argued that such money representing proceeds of trust property, secured creditor receiving that money therefore having to remit it to Crown pursuant to statutory obligation — Disagreement between parties arose from deemed trust being similar in nature to floating charge, coupled with statutory obligation to pay proceeds of trust property to Crown — Defendant's submissions failing to engage with Crown's position as to how s. 227(4.1) applies in situation where tax debtor's property has been sold — *Canada v. Toronto-Dominion Bank*, 2018 FC 538, [2018] 4 F.C.R. D-9 (TD Bank FC), affd 2020 FCA 80, [2020] 3 F.C.R. 201 (TD Bank FCA) most instructive in considering application of statutory obligation — TD Bank FC explained, in considering parallel provisions in *Excise Tax Act*, R.S.C., 1985, c. E-15 (ETA), s. 222 that this obligation is often referred to as "statutory obligation",

distinguishing it from establishment of deemed trust itself — TD Bank FCA conducted required textual, contextual, purposive analysis of deemed trust provisions in ETA, including language surrounding statutory obligation — Concluded that, when bank in that case lent money to debtor, took its security interests, debtor's property to extent of tax debt was already deemed to be beneficially owned by Crown pursuant to deemed trust — Accordingly, when debtor's property was sold, bank was under statutory obligation to remit proceeds received to Crown — These conclusions favoured Crown's position on first question of law herein — When bank lent money to debtor, took its security interests, debtor's property, to extent of tax debt, was already deemed to be beneficially owned by Crown — When debtor's property sold, bank was under statutory obligation to remit proceeds it received to Crown — First question of law answered in positive — Regarding second question of law, defendant characterized itself as *bona fide* purchaser for value when it engaged in transactions with debtor that resulted in extension of credit to debtor, debtor's subsequent repayment thereof, such that it had defence to Crown's claim under Act, s. 227(4.1) — TD Bank FC analysed availability of equitable defences, concluded that defence is generally available [83] but that certain conditions needing to be met, that defence must not be inconsistent with scheme of legislation — Conclusion on second question of law turned not on Crown's argument on general unavailability of equitable defences but rather on availability of that defence being inconsistent with legislative intent, case law — TD Bank FCA stated that purpose of deemed trust provision is collection of unremitted tax; that purpose is effected by granting priority to deemed trust in respect of property that is also subject to security interest — That purposive analysis recognized Parliament's intention to afford Crown priority access to value of tax debtor's assets, notwithstanding existence of security interest — That analysis was not dependent on existence of security interest but rather, applying despite its existence — Analysis applied now to second question of law, it would be inconsistent with Parliament's intent in enacting deemed trust provisions to afford unsecured creditors recourse to *bona fide* purchaser defence — Therefore, second question of law answered in negative.

CANADA V. TORONTO DOMINION BANK (TD CANADA TRUST) (T-1841-21, 2024 FC 441, Southcott J., reasons for order dated March 19, 2024, 42 pp.)