Federal Court  Cour fédérale

**Date: 20240319**

**Docket: T-1841-21**

**Citation: 2024 FC 441**

**Ottawa, Ontario, March 19, 2024**

**PRESENT: The Honourable Mr. Justice Southcott**

**BETWEEN:**

**HIS MAJESTY THE KING**

**Plaintiff**

**and**

**THE TORONTO-DOMINION BANK (TD CANADA TRUST)**

**Defendant**

# ORDER AND REASONS

## I. Overview

[1] This decision addresses a motion for the determination of two questions of law pursuant to Rule 220 of the *Federal Courts Rules*, SOR/98-106. The questions relate to the interpretation of the deemed trust provisions in section 227 of the *Income Tax Act*, RSC 1985, c 1 (5th Supp) [*ITA*] that apply to payroll deductions in respect of employee income tax that employers withhold but fail to remit.

[2] These questions arise in the context of the within action by the Plaintiff, His Majesty the King [the Crown], against the Defendant, The Toronto-Dominion Bank [the Bank], related to proceeds the Bank received from its customer H.N.J. Enterprises Ltd. [the Debtor] after the Debtor had failed to remit payroll deductions to the Crown. Those proceeds resulted from the Debtor's sale of its business and were applied by the Bank in payment of the Debtor's overdraft with the Bank. The Bank is an unsecured creditor of the Debtor and, in defence of the Crown's claim, it argues that the deemed trust provisions of section 227 of the *ITA* do not apply to it and that, when it received the proceeds from the Debtor, it provided value to the Debtor through the reduction of its overdraft.

[3] In the context of those defence positions, the parties proposed that two questions of law be determined by the Court under Rule 220. In an Order dated May 18, 2023, Associate Judge Horne approved this proposal and prescribed a process for written and oral submissions, leading to a determination of those questions, which the Order framed as follows:

> A. Do the deemed trust provisions in section 227 of the *ITA* apply to unsecured creditors?
>
> B. Can unsecured creditors rely on the *bona fide* purchaser for value defence to defend against a deemed trust claim?

[4] As explained in greater detail below, my conclusion is that the answer to the first question is "yes" and the answer to the second question is "no".

## II. Background

[5] In support of this motion, the parties provided an Agreed Statement of Facts, which sets out the factual foundation for their dispute. While not strictly necessary for the determination of the questions of law, that factual foundation assists the Court in understanding the context in which the questions are raised. The following is a summary of the agreed facts that I consider to be most material to that understanding:

A. The Debtor operated a restaurant between June 2000 and October 2015 [the Business] and had employees to whom it paid wages.

B. During the Debtor's 2013, 2014, and 2015 taxation years, the Debtor withheld, but failed to remit to the Canadian Revenue Agency [CRA], $74,518.17 in prescribed amounts under the *ITA*, the *Canada Pension Plan Act*, the *Employment Insurance Act*, and their regulations [collectively, Payroll Source Deductions]. $36,250.86 of the Payroll Source Deductions were for employee CPP/EI contributions and employee federal/provincial income taxes and were therefore subject to a deemed trust in favour of the Crown pursuant to sections 222 and 227 of the *ITA*.

C. In October 2015, the Debtor ceased operating the Business and sold it to an unrelated third party for $100,000.

D. The Bank provided banking services to the Debtor and its Director. The Debtor opened a business account with the Bank in 2004 [the Corporate Account], and the Director held a personal account with the Bank [the Personal Account]. The Debtor incurred overdrafts on the Corporate Account both before and after the sale of the

Business in October 2015 and until the account was closed in March 2016, making the Bank an unsecured creditor of the Debtor.

E. The Bank was unaware of the Debtor's failure to remit Payroll Source Deductions until it received notice from CRA on January 8, 2018.

F. The timeframe most material to the questions posed to the Court is October 13, 2015 to January 6, 2016:

    i. During this period, a total of 92 separate transactions were processed on the Corporate Account. In early October 2015, the sale of the Business netted the Debtor proceeds (after deductions) of $89,500.00 [the Proceeds]. At that time, the Bank had no knowledge of the Debtor's sale of the Business or the source of the Proceeds.

    ii. On October 13, 2015, the Director deposited the Proceeds into the Corporate Account and used those funds to pay the existing overdraft of $11,344.88. The Director then transferred $69,500.00 of the Proceeds to the Personal Account. After a series of transactions on October 13, 2015, the closing balance of the Corporate Account on that day was an overdraft of $6,450.19.

    iii. On October 15, 2015, the Director transferred $6,730.48 from the Personal Account to the Corporate Account to cover the overdraft of $6,450.19. The

balance of the Corporate Account at the end of the day on October 15, 2015, was $280.29.

iv. Between October 15, 2015 and January 6, 2016, the Bank advanced funds to the Debtor in the form of overdrafts and the Director transferred funds from the Personal Account to the Corporate Account to pay off the Debtor's overdrafts.

v. In total, the Bank received $37,595.07 from the Debtor between October 13, 2015 and January 6, 2016. None of these transactions were a result of any demand for payment by the Bank or the exercise of any form of security.

G. On January 8, 2018, CRA notified the Bank of its claim to $36,250.86 plus interest. The Bank did not pay the Crown, and the Crown commenced the within action.

## III. Issues

[6] The issues for the Court's determination are the two questions of law articulated earlier in these Reasons.

## IV. Analysis

### A. *Statutory provisions*

[7] The statutory provisions most relevant to the questions of law are subsection 227(4) and (4.1) of the *ITA*, which read as follows:

**Trust for moneys deducted**

**(4)** Every person who deducts or withholds an amount under this Act is deemed, notwithstanding any security interest (as defined in subsection 224(1.3)) in the amount so deducted or withheld, to hold the amount separate and apart from the property of the person and from property held by any secured creditor (as defined in subsection 224(1.3)) of that person that but for the security interest would be property of the person, in trust for Her Majesty and for payment to Her Majesty in the manner and at the time provided under this Act.

**Montant détenu en fiducie**

**(4)** Toute personne qui déduit ou retient un montant en vertu de la présente loi est réputée, malgré toute autre garantie au sens du paragraphe 224(1.3) le concernant, le détenir en fiducie pour Sa Majesté, séparé de ses propres biens et des biens détenus par son créancier garanti au sens de ce paragraphe qui, en l'absence de la garantie, seraient ceux de la personne, et en vue de le verser à Sa Majesté selon les modalités et dans le délai prévus par la présente loi.

**Extension of trust**

**(4.1)** Notwithstanding any other provision of this Act, the Bankruptcy and Insolvency Act (except sections 81.1 and 81.2 of that Act), any other enactment of Canada, any enactment of a province or any other law, where at any time an amount deemed by subsection 227(4) to be held by a person in trust for Her Majesty is not paid to Her Majesty in the manner and at the time provided under this Act, property of the person and property held by any secured creditor (as defined in subsection 224(1.3)) of that person that but for a security interest (as defined in subsection 224(1.3)) would be property of the person, equal in value to the amount so deemed to be held in trust is deemed

**(a)** to be held, from the time the amount was deducted or withheld by the person, separate and apart from the property of the person, in trust for Her Majesty whether or not the property is subject to such a security interest, and

**Non-versement**

**(4.1)** Malgré les autres dispositions de la présente loi, la Loi sur la faillite et l'insolvabilité (sauf ses articles 81.1 et 81.2), tout autre texte législatif fédéral ou provincial ou toute règle de droit, en cas de non-versement à Sa Majesté, selon les modalités et dans le délai prévus par la présente loi, d'un montant qu'une personne est réputée par le paragraphe (4) détenir en fiducie pour Sa Majesté, les biens de la personne, et les biens détenus par son créancier garanti au sens du paragraphe 224(1.3) qui, en l'absence d'une garantie au sens du même paragraphe, seraient ceux de la personne, d'une valeur égale à ce montant sont réputés

**a)** être détenus en fiducie pour Sa Majesté, à compter du moment où le montant est déduit ou retenu, séparés des propres biens de la personne, qu'ils soient ou non assujettis à une telle garantie;

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| **(b)** to form no part of the estate or property of the person from the time the amount was so deducted or withheld, whether or not the property has in fact been kept separate and apart from the estate or property of the person and whether or not the property is subject to such a security interest | **b)** ne pas faire partie du patrimoine ou des biens de la personne à compter du moment où le montant est déduit ou retenu, que ces biens aient été ou non tenus séparés de ses propres biens ou de son patrimoine et qu'ils soient ou non assujettis à une telle garantie. |
| and is property beneficially owned by Her Majesty notwithstanding any security interest in such property and in the proceeds thereof, and the proceeds of such property shall be paid to the Receiver General in priority to all such security interests. | Ces biens sont des biens dans lesquels Sa Majesté a un droit de bénéficiaire malgré toute autre garantie sur ces biens ou sur le produit en découlant, et le produit découlant de ces biens est payé au receveur général par priorité sur une telle garantie. |

B. *Principles of statutory interpretation*

[8] Both questions that the Court is required to answer in this motion turn on the proper interpretation of section 227 of the *ITA*. As with any statutory provision, this interpretation must employ a textual, contextual, and purposive analysis. *Rizzo & Rizzo Shoes Ltd (Re)*, 1998 CanLII 837 (SCC), [1998] 1 SCR 27 at paragraph 21, explains that the words of the statute are to be read in their entire context and in their grammatical and ordinary sense, harmoniously with the scheme of the statute, the object of the statute, and the intention of Parliament. As expressed in *Alberta (Treasury Branches) v. MNR*, 1996 CanLII 244 (SCC), [1996] 1 SCR 963 at paragraph 38, the words of the *ITA* should be given their plain and ordinary meaning in accordance with the structure and purpose of the statute.

[9] However, the Bank emphasizes that, in tax cases, the jurisprudence recognizes that, given the particularity and detail of many tax provisions, the construction of taxation statutes requires

an emphasis on textual interpretation (*Canada Trustco Mortgage Co v Canada*, 2005 SCC 54, [2005] 2 SCR 601 at para 11). As this point is described in *Canada v Loblaw Financial Holdings Inc*, 2021 SCC 51 at paragraph 41, the requirement for attention to the text, context and purpose of the statute continues to apply in the taxation context but, in determining the relative weight to be afforded to those components of the analysis, it is important that full effect be given to Parliament's precise and unequivocal words.

[10] I do not understand these interpretive principles to be in dispute between the parties.

C. *Do the deemed trust provisions in section 227 of the ITA apply to unsecured creditors?*

(1) Explanation of the question

[11] In *First Vancouver Finance v MNR*, 2002 SCC 49 [*First Vancouver*] at paragraph 3, the Supreme Court of Canada [SCC] provided a helpful summary of how the deemed trust in the *ITA* operates:

> 3. Section 153(1) of the *ITA* requires employers to deduct and withhold amounts from their employees' wages ("source deductions") and remit these amounts to the Receiver General by a specified due date. By virtue of s. 227(4), when source deductions are made, they are deemed to be held separate and apart from the property of the employer in trust for Her Majesty. If the source deductions are not remitted to the Receiver General by the due date, the deemed trust in s. 227(4.1) of the *ITA* becomes operative and attaches to property of the employer to the extent of the amount of the unremitted source deductions. As well, the trust is deemed to have existed from the moment the source deductions were made.

[12] The dispute between the parties in this case, which leads to the questions posed to the Court, focuses upon the operation of subsection 227(4.1). As is plain from the text of that subsection, in broad strokes, the deemed trust created thereby is imposed both upon property of the tax debtor and upon property held by any secured creditor of the tax debtor that, but for a security interest, would be property of the tax debtor.

[13] I pause at this point in my analysis to emphasize what is, and is not, in dispute between the parties. As the parties acknowledged at the hearing, the first question posed in this motion (whether the deemed trust provisions apply to unsecured creditors) is perhaps somewhat lacking in precision in identifying the nature of the dispute.

[14] The Bank acknowledges that if, for instance, it (as an unsecured creditor) and the Crown (as the beneficiary of the trust) were both claimants against a debtor that continued to hold particular property, the Crown would prevail against the Bank in a priorities dispute in accessing the value of that property to pay its claim. In that respect, the deemed trust provisions clearly apply to unsecured creditors, in the sense that they exclude unsecured creditors from, for instance, obtaining a judgment and executing that judgment against the debtor's property, to the extent the value of that property is impressed with the deemed trust. This result follows from the fact that the trust deems such property, to the value of the amount owed to the Crown, to be beneficially owned by the Crown rather than by the debtor.

[15] The dispute between the parties surrounds a situation where the debtor no longer holds its property. The Rule 220 questions are questions of law and are not formally rooted in the

particular facts of the dispute between the Crown and the Bank. However, those facts serve to illustrate the type of situation that the parties wish the answer to the question to address.

[16] The Debtor owned the assets of the Business, but it sold those assets to an arm's length third party. The Debtor received money for the sale. As I understand the Bank's position, consistent with the explanation above, it would accept that, as long as the Debtor continued to hold the money from the sale, that money was impressed with the deemed trust. However, the Debtor conveyed that money to the Bank, through a series of transactions in which the Debtor paid unsecured overdraft amounts on its Corporate Account. The Bank takes the position that, once the money was conveyed by the Debtor to the Bank, the deemed trust no longer applied. It is in a scenario of that sort that the Bank argues that the deemed trust provisions do not apply to unsecured creditors.

[17] In taking this position, the Bank relies on the nature of the deemed trust, which *First Vancouver* described as follows (at paras 4-5):

> 4 For the reasons set forth below, I find that the s. 227(4.1) deemed trust is similar in principle to a floating charge over all the tax debtor's assets in favour of Her Majesty. The trust arises the moment the tax debtor fails to remit source deductions by the specified due date, but is deemed to have been in existence from the moment the deductions were made. As long as the tax debtor continues to be in default, the trust continues to float over the tax debtor's property. Thus, at any given point in time, whatever property then belonging to the tax debtor is subject to the deemed trust.
>
> 5 Viewed in this way, it is clear that, as property comes into possession of the tax debtor, it is caught by the trust and becomes subject to Her Majesty's interest. Similarly, property which the tax debtor disposes of is thereby released from the deemed trust. This mutuality of treatment between incoming and outgoing property relating to the deemed trust is supported by both the plain language

> of the provisions as well as their purpose and intent. Most importantly, Her Majesty's interest in the tax debtor's property is protected because, while property which is sold to third party purchasers is released from the trust, at the same time, the proceeds of disposition of the alienated property are captured by the trust. Moreover, commercial certainty is promoted owing to the fact that third party purchasers are free to transact with tax debtors or suspected tax debtors without fearing that Her Majesty may subsequently assert an interest in the property so acquired.

[18] The Crown disagrees with the Bank's position, but it does not rely on an argument that the money remained impressed with the deemed trust after it had been conveyed by the Debtor to the Bank. Rather, the Crown relies on the language at the end of subsection 227(4.1), which requires proceeds of deemed trust property to be paid to the Crown. In a decision that will figure significantly in the analysis of the Rule 220 questions, my colleague, Justice Grammond, explained at paragraph 17 (in considering parallel provisions in section 222 of the *Excise Tax Act*, RSC 1985, c E-15 [*ETA*]) that this obligation is often referred to as a "statutory obligation", distinguishing it from the establishment of the deemed trust itself (*Canada v Toronto-Dominion Bank*, 2018 FC 538 [*TD Bank FC*], affirmed *Toronto-Dominion Bank v Canada*, 2020 FCA 80 [*TD Bank FCA*]).

[19] In short, the disagreement between the parties arises from the deemed trust being similar in nature to a floating charge, coupled with the statutory obligation to pay proceeds of trust property to the Crown. In that context, the Bank argues that the section 227 provisions do not apply to unsecured creditors to which a debtor conveys money that had been subject to the deemed trust. The Crown argues that the section 227 provisions do apply to such an unsecured creditor, because such money represents proceeds of trust property and the secured creditor that receives the money must therefore remit it to the Crown pursuant to the statutory obligation.

[20] At the hearing of the motion, the Court consulted counsel on whether the first of the Rule 220 questions should be reformulated to capture with more precision the legal point in dispute between the parties. However, counsel were content to leave the question as framed, on the understanding that the question did not necessarily require a "yes" or "no" answer, but rather could if necessary be answered in a nuanced manner that addresses the point in dispute.

[21] With the benefit of that explanation, I will set out the parties' principal arguments as to how a textual, contextual and purposive interpretation of subsection 227(4.1) favours their respective positions on the first Rule 220 question, taking into account existing jurisprudence that has interpreted this subsection.

(2) The Crown's arguments

[22] Noting the explanation in *TD Bank FCA* (at paras 42 and 48) that the evolution of legislation represents an important contextual factor in statutory construction, the Crown's argument begins by drawing the Court's attention to the legislative and jurisprudential history of subsections 227(4) and (4.1). Jurisprudentially, the Crown's submissions begin with the decision of the SCC in *Royal Bank of Canada v Sparrow Electric Corp*, 1997 CanLII 377 (SCC), [1997] 1 SCR 411 [*Sparrow*], which interpreted predecessors to those subsections, being respectively subsections 227(4) and (5), that read as follows:

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| **227** | **227** |
| […] | […] |
| **(4)** Every person who deducts or withholds any amount under this Act shall be deemed to hold the amount so deducted or withheld in trust for Her Majesty. | **(4)** Toute personne qui déduit ou retient un montant quelconque en vertu de la présente loi est réputée retenir le montant ainsi déduit ou retenu en fiducie pour Sa Majesté. |

**(5)** Notwithstanding any provision of the *Bankruptcy Act*, in the event of any liquidation, assignment, receivership or bankruptcy of or by a person, an amount equal to any amount

> **(a)** deemed by subsection (4) to be held in trust for Her Majesty, […]

shall be deemed to be separate from and form no part of the estate in liquidation, assignment, receivership or bankruptcy, whether or not that amount has in fact been kept separate and apart from the person's own moneys or from the assets of the estate.

**(5)** Malgré la *Loi sur la faillite*, en cas de liquidation, cession, mise sous séquestre ou faillite d'une personne, un montant égal à l'un ou l'autre des montants suivants est considéré comme tenu séparé et ne formant pas partie du patrimoine visé par la liquidation, cession, mise sous séquestre ou faillite, que ce montant ait été ou non, en fait, tenu séparé des propres fonds de la personne ou des éléments du patrimoine:

> **a)** le montant réputé, selon le paragraphe (4), être détenu en fiducie pour Sa Majesté;

[23] In *Sparrow*, the SCC found that the Crown's deemed trust was able to attach to a tax debtor's unencumbered property (*i.e.*, property not subject to a security interest) but did not oust a secured creditor's pre-existing security interest (at paras 98-99). However, the Court explained that it was available to Parliament to step in and assign absolute priority to the Crown through the deemed trust (at para 112). As described in *TD Bank FCA* (at paras 26, 27 and 48), Parliament then amended the predecessor legislation to section 227 of the *ITA* in response to this invitation in *Sparrow* to expand the application of the deemed trust provisions.

[24] As part of its contextual analysis (related to the parallel *ETA* provisions), *TD Bank FCA* also noted that, when the post-*Sparrow* amendments were announced in 1997, the government's press release referred to "absolute priority" to be given to the collection of unremitted GST, in exchange for the Crown waiving all other priorities in bankruptcy. *TD Bank FCA* explained at paragraph 45 that this reflected a policy decision by Parliament that, in exchange for the super-

priority ordinarily given to the deemed trust provisions of the *ETA*, the priority did not survive bankruptcy under the *Bankruptcy and Insolvency Act*, RSC 1985, c B-3 [*BIA*] or apply to arrangements under the *Companies' Creditors Arrangement Act*, RSC 1985, c C-36 [*CCAA*]).

[25] In the case at hand, the Crown notes that the *ITA* similarly creates limited exemptions from the super priority of the deemed trust, for the benefit of certain categories of unsecured creditors in the event of a bankruptcy or receivership under the *BIA*. This is accomplished through the parenthetical language, "(except sections 81.1 and 81.2 of that Act)", following reference to the *BIA* in the introductory wording of subsection 227(4.1).

[26] In reviewing the deemed trust amendments, *First Vancouver* explained the deemed trust provisions give the Minister of National Revenue [Minister] special priority over other creditors to collect unremitted taxes (at para 23) and described the post-*Sparrow* changes as representing a concerted effort by Parliament to broaden and strengthen the deemed trust in order to facilitate the collection efforts of the Minister (at para 29).

[27] Against that background of the legislative and jurisprudential history, which the Crown argues speaks to both the context and purpose of the current deemed trust provisions, its submissions turn to the text of the provisions. It argues that the grammatical and ordinary language of subsection 227(4.1) extends the deemed trust to two types of property: (a) "property of the person", the person being the tax debtor; and (b) "property held by any secured creditor … of that person that but for a security interest ... would be property of the person". The Crown submits that it is the reference to the first category of property, that of the tax debtor, that affords

the Crown priority over unsecured creditors, because the Crown has the benefit of the deemed trust over the tax debtor's property while unsecured creditors lack any proprietary interest in that property.

[28] Anticipating the Bank's arguments (as will be canvassed shortly) that the Court should favour its position because subsection 227(4.1) is replete with references to secured creditors and has no references to unsecured creditors, the Crown submits that this does not support a conclusion that the text does not afford the Crown priority over unsecured creditors. Rather, the express references to secured creditors are a function of the fact that secured creditors have proprietary interests in the tax debtor's property such that, per the analysis in *Sparrow*, these references are necessary to expressly override those proprietary interests. In contrast, it is not necessary for the text to expressly override the interests of unsecured creditors, as that is accomplished simply by the text applying the deemed trust to the property of the debtor.

[29] Against the background of those submissions, the Crown emphasized at the hearing of this motion that its position is based principally on the statutory obligation, embodied in the language at the end of subsection 227(4.1), that "… the proceeds of such property shall be paid to the Receiver General in priority to all such security interests."

[30] The Crown refers the Court to *Canada (Attorney General) v National Bank of Canada*, 2004 FCA 92 [*National Bank*], which considered the application of this language, albeit in a context involving a secured creditor. Relying on *First Vancouver* (at para 40), *National Bank* (at para 29) referred to the deemed trust as resembling a floating charge such that, once a tax debtor

alienates its property in the normal course of its business, the trust extends to the proceeds of sale or replacement property. When the secured creditor in that case received the proceeds of property subject to the deemed trust, it was obliged to pay them to the Receiver General (*National Bank* at para 40).

[31] *National Bank* involved a circumstance where the proceeds resulted from the forced sale of assets by the secured creditor. However, the Crown also refers to the analysis in *TD Bank FC*, which considered that authority and others in concluding that the same analysis applied where a debtor voluntarily sold its property and used the sale price to make payments to a secured creditor (at paras 24 to 31). As expressed in *TD Bank FC* at paragraph 31 (in the context of the parallel provisions of the *ETA*):

> 31 To summarize, the phrase "the proceeds of the property shall be paid to the Receiver General" in section 222(3) of the ETA encompasses proceeds flowing from the voluntary sale of the tax debtor's property. Upon such a sale, a tax debtor has an obligation to pay the proceeds to the Receiver General. If the tax debtor fails to do so and pays a secured creditor instead, that creditor has an obligation to repay the money to the Crown.

[32] As I will explain shortly, there are other portions of the decision in *TD Bank FC* that comment upon the position of unsecured creditors. The Crown argues that such comments are *obiter* and should not be relied upon. However, the Crown agrees with the conclusion in paragraph 31 of the decision and submits that the logic leading to the conclusions in *National Bank* at paragraph 40 and *TD Bank FC* at paragraph 31 apply equally to a situation where the sale of a tax debtor's property generates proceeds that are ultimately received by an unsecured creditor. The Crown argues that the tax debtor has an obligation to pay such proceeds to the

Receiver General and, if it fails to do so and pays an unsecured creditor instead, that creditor has an obligation to pay the money to the Crown.

[33] The Crown cites jurisprudence that it considers to favour this argument. It relies on *AG Canada (MNR) v GlassCell Isofab Inc*, 2011 ONSC 2660 [*GlassCell*], in which an unsecured creditor, claiming the cost of goods sold and delivered to a debtor, obtained a judgment against the debtor and, through a garnishment process, was paid funds obtained by the sheriff. Based on unremitted source deductions under the *ITA*, the Crown sought an order requiring the unsecured creditor to pay it those funds. The Ontario Superior Court of Justice held that, by virtue of the super priority created by the deemed trust provisions of the *ITA*, the Crown had priority over the claim of the unsecured creditor to the proceeds of the garnishment (at para 38).

[34] The unsecured creditor in *GlassCell* attempted to rely on the explanation in *First Vancouver* that, as a result of the floating charge nature of the deemed trust, the trust released property alienated by the tax debtor, because the trust then applied to the property received by the debtor in exchange, such that the trust was neither depleted nor enhanced (*First Vancouver* at para 42). The Court in *GlassCell* rejected this argument, finding at paragraph 37 that there had been no sale or disposition in the nature of a sale by the tax debtor of the sort to which *First Vancouver* applied.

[35] The Crown also relies on *Proman Ltd v RCL Operators Ltd*, 1993 CanLII 3328, (NB KB) [*Proman*], in which an unsecured judgment creditor argued that the subsection 224(1.2) of the *ITA* (which is worded similarly to subsection 227(4.1)) gave the Crown priority over secured

creditors but not unsecured creditors. The New Brunswick Court of King's Bench concluded that the statute made the money required to be paid to the Minister take precedence over all claims, notwithstanding that there may be a security interest. This did not give unsecured creditors a preferred position.

(3) The Bank's Arguments

[36] I will now canvass the Bank's arguments in response to those of the Crown. As anticipated by the Crown, the Bank relies on the importance of the statutory text in the construction of taxation provisions and emphasizes the repeated references to secured creditors in both subsections 227(4) and (4.1) and the lack of any references to unsecured creditors.

[37] The Bank invokes the principle that, in the absence of clear language to the contrary, a tax on one person cannot be collected out of property belonging to another (*Pembina on the Red Development Corp Ltd v Triman Industries Ltd*, 1991 CanLII 2699 (MBCA) and argues that, unlike in relation to the property of secured creditors, the language of subsection (4.1) does not speak of imposing the deemed trust upon the property of unsecured creditors. The Bank emphasizes the past conclusions of the SCC that the deemed trust provisions should not be interpreted to extend to the property of other parties in the absence of language to that effect (*Sparrow* at paras 39 and 112; *First Vancouver* at para 43).

[38] The Bank also takes issue with the Crown's argument that the legislative history supports its position. The Bank refers to the Crown's argument that the pre-*Sparrow* legislation already

extended the deemed trust to unsecured creditors and submits that there is no language in that legislation or in *Sparrow* that supports such a conclusion.

[39] In relation to the Crown's authorities, the Bank argues that this Court cannot be guided by *GlassCell* or *Proman*, because they are not binding on this Court, they did not undertake the required textual, contextual and purposive analysis of the legislation, and they did not take into account authorities from the SCC that the Bank considers to be instructive on the question now before the Court.

[40] The Bank first relies on *Canada v Canada North Group Inc*, 2021 SCC 30 [*Canada North*], which considered the priority between the Crown's deemed trust and priming charges incurred pursuant to the *CCAA* in connection with a plan of arrangement intended to avoid a company's bankruptcy. The Bank refers the Court to the SCC's comment (per Côté, J.) that the deemed trust created by the *ITA* has priority over only a defined set of security interests, not priority over all possible interests (at paras 4 and 60). Based thereon, the Bank submits that the trust does not extend to all creditors and does not extend to secured creditors.

[41] Similarly, the Bank notes that, in *Caisse populaire Desjardins de l'Est de Drummond v Canada*, 2009 SCC 29, [2009] 2 SCR 94 [*Caisse populaire*] at paragraph 10, the SCC identified that the scope of the deemed trust created by the *ITA* is to be defined in terms of the particular statutory definition of "security interest" adopted in the *ITA* itself.

[42] In relation to *Caisse populaire*, the Bank also raised an additional argument at the hearing of this motion. In that case, the SCC adjudicated whether agreements between the Caisse populaire [Caisse] and its customer, Camvrac Enterprises Inc [Camvrac], who was also a tax debtor, represented a "security interest" within the meaning of the *ITA* deemed trust provisions. The Crown argues that the premise of this dispute must have been that, if Caisse did not have a security interest, it would have been able to prevail against the Crown. In other words, the Bank submits that implicit in the SCC's adjudication of that dispute is an assumption that the deemed trust provisions do not apply to unsecured creditors.

[43] The Bank also refers the Court to comments in *TD Bank FC* on the application of the deemed trust provisions in the *ETA* to unsecured creditors. While the dispute in that case was between the Crown and a secured creditor, the decision also makes observations about the position of unsecured creditors. As explained earlier in these Reasons, in analysing the position of the secured creditor that was before the Court, it held that upon a sale of its property a tax debtor has obligation to pay the proceeds to the Receiver General and, if the debtor fails to do so and pays the secured creditor instead, that creditor has an obligation to repay the money to the Crown (at para 31). Following that finding, the Court observed that it was uncertain that the same logic would apply to unsecured creditors, although it was unnecessary for it to decide that issue (at para 32).

[44] At the hearing of this motion, the Bank emphasized that its position on the Rule 220 questions does not depend upon those observations in *TD Bank FC* (or upon other observations in that case as to the position of unsecured creditors, to which I will refer when considering the

second question later in these Reasons). The Bank argues that those observations are correct. However, the Bank's position is based principally upon its arguments surrounding the principles of statutory interpretation and the required focus on the text of the relevant taxation provisions, in conjunction with the SCC jurisprudence referenced above.

(4) Analysis

[45] As a preliminary point, I note that the parties' arguments, and therefore this analysis, are based on the English version of the relevant provisions. While the French version is equally authoritative, neither party argued that any ambiguity exists between the two versions. The argument and analysis in *TD Bank FCA* proceeded in the same manner (see para 32).

[46] I have considered the Bank's submissions surrounding the repeated references to secured creditors in subsections 227(4) and (4.1), the lack of any such references to unsecured creditors, the requirement for clear statutory language for the tax on one person to be collected out of the property of another, and the absence of any such language in the predecessors to subsections 227(4) and (4.1) or *Sparrow* to support a conclusion that the pre-*Sparrow* legislation already extended the deemed trust to unsecured creditors.

[47] In my view, these submissions do not engage with the Crown's position as to how subsection 227(4.1) applies in a situation where a tax debtor's property has been sold. The Crown does not argue that the deemed trust applies to the property of an unsecured creditor. Indeed, as explained above, it submits that such application would be unnecessary to grant the Crown the protection created by the deemed trust, as the trust need only apply to the property of

those parties that potentially have relevant property interests, *i.e.*, the tax debtor and any secured creditor. Rather, the Crown relies on the statutory obligation, embodied in the language at the end of subsection 227(4.1), that "… the proceeds of such property shall be paid to the Receiver General in priority to all such security interests."

[48] As previously explained, the parties' disagreement on the first Rule 220 question surrounds the circumstance where a tax debtor has conveyed trust property (in particular, money derived from the sale of other trust property) to an unsecured creditor. The Crown's position is that such circumstances engage the statutory obligation, as the money represents proceeds within the meaning of subsection 227(4.1), requiring the unsecured creditor to pay those proceeds to the Crown.

[49] I have also considered the Bank's reliance on *Canada North* and *Caisse populaire* and do not consider those authorities to assist the Bank on the subject of the parties' particular disagreement. I accept the principles that the deemed trust created by the *ITA* is not intended to afford the Crown priority over all possible interests (*Canada North* at paras 4 and 60) and that one must have recourse to the particular statutory definition in the *ITA* in determining the scope of the deemed trust (*Caisse populaire* at para 10). However, those authorities do not focus upon the scope or operation of the statutory obligation surrounding proceeds of deemed trust property.

[50] In relation to the Bank's additional argument based on *Caisse populaire* (that implicit in the SCC's adjudication of that dispute in that case is an assumption that the deemed trust provisions do not apply to unsecured creditors), it is necessary to review briefly the facts of that

case and the particular arguments before the SCC. Caisse had granted its customer Camvrac a line of credit, and Camvrac also lodged a term deposit with Caisse, pursuant to an agreement that allowed Caisse to withhold repayment of the deposit to the extent the line of credit remained owing (paras 1-4).

[51] As explained in the majority decision of Rothstein, J., the issue for the Court's determination was whether the Crown was the beneficial owner of Camvrac's term deposit as a result of the deemed trust provisions (at para 7). Caisse had argued that it did not hold a security interest, but rather that the terms of its agreement with Camvrac conferred upon it a contractual right to simply extinguish its own indebtedness to Camvrac (see para 26). Justice Rothstein rejected this position and held that Caisse's right of set-off or compensation did represent a "security interest" within the meaning of the deemed trust provisions (see para 17). The dissent by Deschamps, J. found that the right of compensation was not a security interest and that Caisse's contractual right could be set up against the Crown, because the Crown did not have any more rights than Camvrac had (at para 65).

[52] I am not convinced that *Caisse populaire* supports the Bank's submission that implicit in the SCC's adjudication of that dispute is an assumption that the deemed trust provisions do not apply to unsecured creditors. Rather, Caisse was arguing that its contractual rights allowed it to extinguish its debt to Camvrac, as represented by the term deposit, such that there was no asset of Camvrac to which the Crown's deemed trust could apply. Certainly, the decision in *Caisse populaire* did not turn on any analysis, or conduct any analysis, of the extent to which the

deemed trust or statutory obligation created by subsection 227(4.1) of the *ITA* applied to unsecured creditors.

[53] Nor am I prepared to place any significant reliance on the Crown's authorities, *GlassCell* and *Proman.* I agree with the Bank that neither case conducts a robust statutory interpretation. Also, neither authority analyses the application of the statutory obligation. Each of *GlassCell* and *Proman* treats the competing claims as a conventional priorities dispute involving creditors seeking access to the value of a debtor's assets.

[54] That approach by the Courts in those cases is perhaps not surprising. In *GlassCell*, the dispute related to three accounts owing to the debtor (a trade account and two bank accounts), each representing an asset of the debtor. By the time the dispute arose, the unsecured creditor had executed upon those assets through a garnishment process and had been paid the resulting funds. As such, I understand why the Crown argues the facts are somewhat comparable to those in the underlying dispute between it and the Bank, as the Court in *GlassCell* was addressing a situation where the unsecured creditor was already in possession of the funds. However, the Court did not analyse the parties' respective entitlements by recourse to the statutory obligation.

[55] Similarly, in *Proman*, the creditors (including unsecured creditors and the Crown) were asserting competing claims to funds that had been paid into court, pursuant to an order for interpleader relief, by the obligor under a labour and materials bond. Again, I understand the Crown's reference to this case, as the Court described the funds as proceeds of the bond. However, I read the decision as a conventional priorities analysis, based on the Crown's claim of

the deemed trust having priority to the claim of the unsecured creditor, not as an analysis of the application of the statutory obligation.

[56] The authorities that I find most instructive in considering the application of the statutory obligation are *TD Bank FC* and *TD Bank FCA*, both as informed by *First Vancouver*. I will turn shortly to the parties' respective submissions on the application of *TD Bank FC* and their disagreement as to whether certain portions of the decision, which comment on the rights of unsecured creditors, are *obiter*. However, I will first consider *TD Bank FCA*, which conducted the required textual, contextual and purposive analysis of the deemed trust provisions in the *ETA*, including the language surrounding the statutory obligation.

[57] Following its review of the text of the deemed trust provisions, the Federal Court of Appeal concluded that, when the bank in that case lent money to the debtor and took its security interests, the debtor's property to the extent of the tax debt was already deemed to be beneficially owned by the Crown pursuant to the deemed trust (at paras 33-36). The Court then concluded, based on the language of the statutory obligation portion of the deemed trust provision, that when the debtor's property was sold, the bank was under a statutory obligation to remit the proceeds received to the Crown (at paras 37-38).

[58] The Court explained that this grammatical and ordinary meaning of the language was confirmed when one looked to the purpose and context of the deemed trust provisions. The purpose was to protect the collection of unremitted tax, effected by granting priority to the trust in respect of property that was also subject to a security interest. The Court concluded that such

purpose was served by construing the deemed trust provisions such that a secured creditor is obliged to remit proceeds received from the disposition of a debtor's property that are impressed with a trust in favour of the Crown (at paras 39-41).

[59] In relation to the context of the deemed trust provisions, the Court explained at paragraphs 42 to 48 that the most important contextual factors were the evolution of the legislation and the provisions that reflected a policy decision by Parliament to afford the Crown a super priority, although with exceptions such that it did not survive bankruptcy under the *BIA* or apply to arrangements under the *CCAA* (all as explained earlier in these Reasons). The Court described the evolution of the legislation as evidencing Parliament's intention to enlarge the scope of the deemed trust provisions so as to ensure that unremitted source deductions were to be recovered in priority to all debts (at para 48).

[60] I find the application of the Federal Court of Appeal's interpretive conclusions to the case at hand to favour the Crown's position on the first Rule 220 question. In conducting its textual analysis, the Court explained that the effect of the text, including the creation of the deemed trust over the tax debtor's property being "…despite any security interest in the property or in the proceeds thereof", was that, when the bank lent money to the debtor and took its security interests, the debtor's property to the extent of the tax debt was already deemed to be beneficially owned by the Crown (at paras 35-36). Then, referencing the statutory obligation language, that "… the proceeds of the property shall be paid to the Receiver General in priority to all security interests", the Court concluded that, when the debtor's property was sold, the bank was under a statutory obligation to remit the proceeds it received to the Crown.

[61] I do not read any of this analysis as dependent on the fact that the bank was a secured lender with a security interest in the property. Rather, it was the fact that the provisions imposed a deemed trust over the debtor's property, combined with the statutory obligation, that required the bank to pay the proceeds to the Crown. The textual references to secured creditors and security interests simply preclude the secured creditor from escaping the application of these provisions by virtue of its security interest. Those references were not otherwise material to the analysis that favoured the position of the Crown in *TD Bank FCA*.

[62] The Federal Court of Appeal's purposive analysis similarly supports the Crown's position. *TD Bank FCA* at paragraph 40 describes the purpose of the deemed trust provision as the collection of unremitted tax and states that this purpose is effected by granting priority to the deemed trust in respect of property that is also subject to a security interest (my emphasis). I read this language as recognizing Parliament's intention to afford the Crown priority access to the value of the tax debtor's assets, notwithstanding the existence of a security interest. Again, that analysis is not dependent on the existence of the security interest. Rather, it applies despite the existence of a security interest. Applied to the question at hand, the purpose of the deemed trust provisions, being the collection of unremitted tax, favours the application of those provisions to require unsecured creditors, to whom a debtor pays proceeds of sale of trust property, to pay those proceeds to the Receiver General in the same manner as secured creditors.

[63] The contextual analysis also supports the Crown. Viewed in the context of the legislative evolution, the Federal Court of Appeal refers to the policy decision made by Parliament to afford the Crown priority in exchange for certain exceptions (at paragraph 45). As the Crown argues in

the case at hand, the exceptions in subsection 227(4.1) of the *ITA* include the effects of the statutory definition of security interest in subsection 227(4.2), as well as sections 81.1 and 81.2 of the *BIA*. Those *BIA* sections afford unpaid suppliers of goods the right to repossess goods in certain circumstances and afford a secured claim to certain categories of unpaid farmers, fishermen and aquaculturists.

[64] I agree with the Crown that the overall effect of these legislative provisions is to afford priority to certain categories of claimants, including some claimants that might otherwise be unsecured creditors. Consistent with the contextual analysis in *TD Bank FCA*, this reflects nuanced policy decisions by Parliament, not a blanket policy decision to favour the interests of all unsecured creditors.

[65] *TD Bank FCA* applied the construction of the *ETA* deemed trust provisions in the adjudication of certain issues (see para 19) raised on appeal from *TD Bank FC*. Those issues included the availability of the *bona fide* purchaser for value defence to secured creditors, to which I will turn shortly when considering the second Rule 220 question. In *TD Bank FC*, Justice Grammond articulated the issues he was required to adjudicate as including whether the deemed trust provisions of the *ETA* imposed on the bank an obligation to repay the amount it had received from its debtor after the debtor sold the property (at para 15). It does not appear that the bank raised that particular issue on appeal. As such, it is useful to review Justice Grammond's analysis of that issue.

[66] The similarity of the factual circumstances in *TD Bank FC* to the case at hand (apart from the bank in that case having been a secured creditor), as well as the similarity of the required analysis, are evident from paragraph 18 of the decision:

> 18 In this case, the Crown does not allege that the Bank held property in trust. The deemed trust covered Mr. Weisflock's house, despite the mortgage that the Bank held on the house. The Bank did not hold legal title to any property as a form of security, so the extension of the deemed trust to that category of property is not in play. Rather, the Crown alleges that the Bank has a "statutory obligation" under the final proviso of section 222(3), because it received the "proceeds" of the property, namely, part of the amount from the sale to a third party, when Mr. Weisflock reimbursed his loans.

[67] The bank in *TD Bank FC* argued that the statutory obligation applied only where the proceeds resulted from its enforcement of its security to sell the debtor's property to repay itself (see para 19). The Court rejected that argument, based on both statutory interpretation and precedent. While that argument is not raised in the case at hand, the Court's analysis led to the conclusion in paragraph 31 (reproduced earlier in these Reasons) that the statutory language encompassed proceeds flowing from the voluntary sale of the tax debtor's property. Upon such a sale, the debtor had an obligation to pay the proceeds to the Receiver General and, if it failed to do so and paid a secured creditor instead, that creditor had an obligation to repay the money to the Crown.

[68] While that analysis and conclusion related to facts in which the creditor held a security interest, I cannot identify any basis on which the analysis would not apply equally to an unsecured creditor.

[69] This brings me to the next paragraph of the Court's decision. Following the conclusion in paragraph 31 as to the application of the statutory obligation to secured creditors, Justice Grammond stated as follows (at para 32):

> 32. At the hearing, I asked counsel for the Crown whether the same logic would apply to unsecured creditors. He asserted that it did. I am not sure, however, that this is compatible with the wording of section 222(3), which requires proceeds of the property to be paid to the Crown "in priority to all secured interests." A contrary interpretation seems to have been adopted in *Canada (Attorney General) v Community Expansion Inc*, 72 OR (3d) 546 (Ont SCJ) at para 19, aff'd 2005 CanLII 1402 (Ont CA). It would also seem odd that Parliament provided a mechanism for the exemption of certain security interests in section 222(4), but not for the protection of unsecured creditors, if the latter are subject to the statutory obligation to pay. Given that the Bank was a secured creditor when it received the payment from Mr. Weisflock, and in light of my conclusion on the next question, it is not necessary for me to decide this issue.

[70] The Crown submits that the observations in paragraph 32 of *TD Bank FC* were made in *obiter*, and the Crown encourages the Court not to follow them. Given the explanation in this paragraph that the Court was not required to decide the issue related to unsecured creditors, I agree with the Crown that the paragraph is clearly *obiter*. However, while the principles of judicial comity may therefore not strictly apply, it is still useful to examine this analysis to assess whether it may have persuasive value.

[71] The Crown questions the relevance of the decision in *Canada (Attorney General) v Community Expansion Inc*, 72 OR (3d) 546 (Ont SCJ) [*Community Expansion*] upon which the observations in paragraph 32 of *TD Bank FC* rely. The Crown also argues that those observations do not take into account the purpose of the deemed trust provisions or their context, including

both their statutory evolution and the limited exemptions therein for certain unsecured creditors in the event of a bankruptcy or receivership under the *BIA*.

[72] Paragraph 32 suggests that the issue of the application of the statutory obligation to unsecured creditors arose as a result of a question posed by the Court during the hearing. This may mean that the Court did not have the benefit of full and considered submissions by the parties on the issue. Also, the paragraph relies to some extent on the decision in *Community Expansion* at para 19. As the Crown submits, a review of that decision demonstrates that it concluded that a landlord's exercise of its right to distrain against a delinquent tenant's property represented a security interest within the meaning of the deemed trust provisions. It did not analyse the application of the deemed trust provisions to unsecured creditors.

[73] In relation to *Community Expansion*, the Bank advances an argument similar to its submissions in relation to the decision in *Caisse populaire*. That is, it argues that the premise of the dispute must have been that, if the landlord did not have a security interest, it would have been able to prevail against the Crown. Unlike in *Caisse populaire*, the decision in *Community Expansion* does not clearly articulate the landlord's position as to how it would have benefited from a determination that it did not have a security interest. As such, the bank may be correct in its characterization of the landlord's position, and this may have been the reasoning underlying Justice Grammond's reference to *Community Expansion*. However, as in *Caisse populaire,* the decision of the Court in *Community Expansion* did not turn on any analysis, or conduct any analysis, of the extent to which the deemed trust or statutory obligation created by subsection 227(4.1) of the *ITA* applied to unsecured creditors.

[74] Finally, noting Justice Grammond's observation that it would seem odd that Parliament provided a mechanism for the exemption of certain security interests but not for protection of unsecured creditors, if the latter were also subject to the statutory obligation, I agree with the Crown's submission that this observation does not take into account the limited exemptions in the deemed trust provisions for certain categories of creditors, including some that might otherwise be unsecured creditors (as canvassed earlier in these Reasons). Again, this is likely the result of Justice Grammond not having the benefit of full and considered submissions by the parties on the issue of the application of the deemed trust provisions to unsecured creditors, as that issue was not before the Court. The Crown has satisfied me that I should decide (with respect) not to adopt the reasoning in paragraph 32 of *TD Bank FC*.

(5) Conclusion on first Rule 220 question

[75] Based on the foregoing analysis, I agree with the Crown's position on the first Rule 220 question. While I noted earlier in these Reasons that it may be necessary to provide a nuanced answer to the question, my analysis results in the conclusion that the question can simply be answered in the positive. As explained earlier, it is not in dispute that, if an unsecured creditor and the Crown were both claimants against a debtor that continued to hold particular property, the Crown would prevail in a priorities dispute and, in that sense, the deemed trust provisions apply to unsecured creditors. In the scenario that is in dispute, in which a tax debtor voluntarily sells its property that was subject to the deemed trust and pays the proceeds of that sale to an unsecured creditor, the deemed trust provisions apply to the unsecured creditor, as the statutory obligation requires it to pay those proceeds to the Crown.

D. *Can unsecured creditors rely on the* bona fide *purchaser for value defence to defend against a deemed trust claim?*

[76] I understand the Bank's position to be that, even if the answer to the first Rule 220 question is unfavourable to it, it can still prevail in its dispute with the Crown if the second question is answered in the affirmative. The Bank characterizes itself as a *bona fide* purchaser for value, when it engaged in the transactions with the Debtor that resulted in the extension of credit to the Debtor and the Debtor's subsequent repayment thereof, such that it has a defence to the Crown's claim under subsection 227(4.1) of the *ITA*.

[77] *TD Bank FCA* provided the following summary of the *bona fide* purchaser for value defence (at para 73):

> 73. First, in *i Trade Finance Inc. v. Bank of Montréal*, 2011 SCC 26, at paragraph 60, the Supreme Court quoted with approval the following explanation of the *bona fide* purchaser for value defence:
>
> > The full name of the equitable defence is 'bona fide purchase of a legal interest for value without notice of a pre-existing equitable interest.' The effect of the defence is to allow the defendant to hold its legal proprietary rights unencumbered by the pre-existing equitable proprietary rights. In other terms, where the defence operates, the pre-existing equitable proprietary rights are stripped away and lost in the transaction by which the defendant acquires its legal proprietary rights.
>
> (L. Smith, *The Law of Tracing* (1997), at p. 386 (footnote omitted; [underlining added]).)

[78] As the Bank submits, a defendant must establish two elements in order to take the benefit of this defence: (a) there must be a purchase for value; and (b) the defendant purchaser must

have had no notice of the pre-existing equitable interest (Mitchell McInnes, *The Canadian Law of Unjust Enrichment and Restitution*, 2nd ed (Toronto: LexisNexis Canada, 2022) ch 38, s 38.01). While not directly relevant to the answer to the Rule 220 question of law, the Bank argues that the second element of the defence is clearly met in its case, as it had no notice of the tax debt until January 8, 2018, after the transactions that gave rise to the Crown's claim.

[79] The Bank argues that the first element is also met, as courts have held that banks can be "purchasers of money repaid to them" and the defence applied in those circumstances. Justice Grammond addressed that point as follows in *TD Bank FC* (at paras 42-43):

> 42. The application of the *bona fide* purchaser for value defence in this case presents a conceptual difficulty. In ordinary parlance, the Bank did not purchase anything. It received money in repayment of the loan it made to Mr. Weisflock. For that reason, the Crown says that the defence is unavailable. It points to the fact that the buyers of Mr. Weisflock's house would be the *bona fide* purchasers for value in this case. The Bank, however, argues that it "purchased money." In my view, this is an awkward manner of saying that the defence does not apply merely to transactions which are properly called "sales," but also to transactions where a third party acquires property, be it chattels or money, that was initially part of the corpus of the trust, for some form of consideration.
>
> 43. I agree that the defence is not limited to "purchasers" who obtain property through a contract of sale. In *i Trade Finance*, the Supreme Court of Canada, quoting from Professor Ziegel, noted that a purchaser in equity is a person who acquires any interest in property, irrespective of the precise manner in which that interest is acquired (paras 62-66). In that case, a bank successfully argued that it was a *bona fide* purchaser for value in a situation where shares were pledged to it. A recent decision of the Ontario Court of Appeal, *Arrow ECS Norway AS v John Doe*, 2017 ONCA 664, also supports the proposition that the defence may be invoked by a person who received money for a valuable consideration, including the payment of an existing debt, and who was unaware that the money had been obtained fraudulently.

[80] In responding to the Bank's effort to invoke the application of this defence, the Crown argues first that, being an equitable defence, it is available only against equitable claims and not against legal claims based in common law or statute. The Crown relies on authorities that have rejected the application of equitable defences to common law and statutory claims, principally (but not exclusively) in the context of the defence of laches.

[81] However, in *TD Bank FC*, the Court addressed this argument directly in the context of the *bona fide* purchaser for value defence. Justice Grammond rejected the Crown's argument in that case that the deemed trust of the *ETA* and *ITA* was not governed by trust law at all, concluding that the deemed trust provisions incorporate the rules of trust law, although only to the extent they are compatible with the legislation. As such, the Court concluded that the bank could invoke equitable defences to claims based on the deemed trust, provided it met the conditions of such defences and provided the defence was not inconsistent with the scheme of the legislation (at paras 39-41).

[82] As previously noted, the Crown argues that Justice Grammond's observations on the application of the deemed trust provisions to unsecured creditors are *obiter* and should not be followed. I will address this argument shortly. However, the portion of *TD Bank FC* referenced above, which analyses the general availability of equitable defences, is relevant to the issue that was clearly before the Court, *i.e.*, the availability of the *bona fide* purchaser for value defence to secured creditors.

[83] In the result, as I will explain below, Justice Grammond concluded that the defence was not available, based on governing jurisprudence and the legislative intent behind the deemed trust provisions (see paras 44-46). As I will also explain below, my conclusion on the second Rule 220 question similarly turns not upon the Crown's argument on the general unavailability of equitable defences but rather upon the availability of that defence being inconsistent with legislative intent and the jurisprudence. As such, while the principle of judicial comity favours adoption of Justice Grammond's conclusion that the equitable defence is generally available, it is unnecessary for me to make a definitive finding on this point, as it is not determinative of the answer to the Rule 220 question.

[84] In arriving at his conclusion that the defence could not be invoked by a secured creditor in the context of the deemed trust provisions, Justice Grammond noted at paragraph 45 the explanation in *First Vancouver* that the deemed trust is akin to a floating charge, a mechanism that is generally consistent with the defence, because the subject matter of the trust changes over time. As trust assets are sold and replaced with property received in exchange, the trust is neither depleted nor enhanced (*First Vancouver* at para 42). However, Justice Grammond also noted the explanation in *First Vancouver* (at para 28) that the intent of the post-*Sparrow* amendments was to grant priority to the deemed trust with respect to property that is also subject to a security interest. Based on that premise, he reasoned that it would be inconsistent with Parliament's intent to allow secured creditors to invoke the *bona fide* purchaser for value defence (at para 46).

[85] The Federal Court of Appeal upheld this reasoning and conclusion. It found that it would be irrational for Parliament, in an effort to ensure that uncollected, unremitted GST was to be

recovered in priority to all debts, to intend the *bona fide* purchaser defence to be available so as to undo the Crown's pre-existing beneficial interest in the property of the deemed trust. As the Federal Court had found, this would eviscerate the deemed trust provisions (*TD Bank FCA* at para 74).

[86] The Court of Appeal also relied on the comment by the SCC in *First Vancouver* that, while *bona fide* purchasers for value were not caught by the deemed trust, secured creditors were (at paras 75-76), and (at para 77) it followed its own decision in *National Bank*, which concluded (at para 30) that lenders were "not comparable to third party purchasers. They are secured creditors and the property over which they asserted their security interest continued to be subject to the deemed trust and remains so at the time of sale."

[87] In my view, the reasoning underlying these decisions, in relation to secured creditors, applies equally to the position of unsecured creditors.

[88] As noted above in addressing the first Rule 220 question, *TD Bank FCA* at paragraph 40 describes the purpose of the deemed trust provision as the collection of unremitted tax. The Federal Court of Appeal states that this purpose is effected by granting priority to the deemed trust in respect of property that is also subject to a security interest. That purposive analysis recognizes Parliament's intention to afford the Crown priority access to the value of the tax debtor's assets, notwithstanding the existence of a security interest. However, the analysis is not dependent on the existence of the security interest. Rather, it applies despite the existence of a security interest. Applied now to the second Rule 220 question, it would be inconsistent with

Parliament's intent in enacting the deemed trust provisions to afford unsecured creditors recourse to the *bona fide* purchaser defence.

[89] I also consider this conclusion to follow from the explanation in *First Vancouver* of the manner in which the deemed trust operates, in the context of third party purchasers of trust assets, such that the trust releases property alienated by the tax debtor but then applies to the consideration given to the debtor for the purchase of that property. As the SCC expressed the point, the trust is neither depleted nor enhanced as a result of that sort of transaction (see para 42). However, analysed rigorously, the result would be different if the *bona fide* purchaser defence was afforded to unsecured creditors.

[90] Taking the example of the Bank's transactions with the Debtor in the case at hand illustrates this point. At the time the proceeds of sale of the trust property were applied to its line of credit with the Bank, the consideration given by the Bank in exchange for the receipt of those proceeds was simply the discharge of a portion of the Debtor's unsecured loan. Unlike a situation where trust property has been alienated to a purchaser, and the purchaser conveys money or another asset to the debtor in exchange for that property, the transaction between the Debtor and the Bank leaves the trust depleted, because the discharge of the Debtor's loan does not represent an asset that has value to the Crown that can be realized in satisfaction of the tax debt. As expressed in *National Bank* (at para 30), unsecured creditors are not comparable to third party purchasers.

[91] I recognize that this conclusion is inconsistent with the observations made with respect to unsecured creditors in *TD Bank FC*. After concluding that the *bona fide* purchaser for value defence was not available to secured creditors, Justice Grammond added at paragraph 47 that the defence remained available to unsecured creditors, such as suppliers, landlords or public utilities, who receive payments from a tax debtor, as denying the defence in those cases would have a general chilling effect on commercial transactions of the sort described in *First Vancouver* (at para 44).

[92] Justice Grammond also queried (at para 51) why Parliament would single out secured creditors in the deemed trust provisions. Although expressing that it might appear absurd to allow unsecured creditors to claim the *bona fide* purchaser defence, when secured creditors could not, Justice Grammond reasoned that this may have been a rational decision for Parliament to make, as security interests by their nature provide debtors with a very strong inducement to pay their secured creditors (at para 52).

[93] The parties disagree on whether these observations in *TD Bank FC* represent *ratio* or *obiter*. In my view, they are clearly the latter, as the factual matrix of that case involved a secured creditor only, and the comments related to the position of unsecured creditors do not form part of the critical path to the decision the Court was required to make. As explained in my analysis of the first Rule 220 question, the issue of the position of unsecured creditors arose as a result of a question posed by the Court during the hearing, which may mean that the Court did not have the benefit of full and considered submissions by the parties on the issue. As for the concern about a chilling effect on commercial transactions, I note that *First Vancouver* raised

those concerns in the context of assets sold by tax debtors to "ordinary consumers" (at para 44). As I have found that application of the relevant appellate authorities favour a conclusion inconsistent with the *obiter* observations in *TD Bank FC*, I respectfully decline to follow those observations.

[94] In so finding, I am conscious of the fact that the final portion of *TD Bank FCA* references briefly the position of unsecured creditors. In that portion of the Decision, the Federal Court of Appeal addressed policy arguments raised by an intervener, the Canadian Bankers' Association, including the following argument:

> It is anomalous and illogical that a secured creditor receiving proceeds of property of the tax debtor in the ordinary course is personally liable to pay the Crown the unpaid amount of GST when there is no such liability imposed upon a lender providing an unsecured credit facility, or any other unsecured creditor whose claim ranks subordinate to the secured creditor.

[95] *TD Bank FCA* concluded at paragraph 84 that the answer to the various policy concerns raised was that Parliament made a considered policy choice to prioritize protection of the fisc over the interests of secured creditors, although tempering the potential harshness of this choice by providing for prescribed security interests and by waiving the Crown's deemed trust rights in cases of bankruptcy and arrangements under the *CCAA*.

[96] While one of the intervener's policy arguments was premised on unsecured creditors being in a more advantageous position than secured creditors, I do not read the Federal Court of Appeal's resulting analysis as necessarily adopting that premise. Rather, the Court addressed the

point that was before it, *i.e.* that Parliament had made a policy decision that, while tempered by certain nuances, favoured the collection of tax debts over the interests of secured creditors.

[97] Based on the foregoing analysis, I agree with the Crown's position on the second Rule 220 question, which will be answered in the negative.

## V. Conclusion and Costs

[98] In the result, my Order will answer the first Rule 220 question in the positive and the second question in the negative.

[99] The parties have agreed that lump-sum costs of $1700.00 should be paid to the successful party in this motion. I consider the proposed amount reasonable and, as the Crown has prevailed on both Rule 220 questions, my Order will award it costs in the agreed amount.

**ORDER IN T-1841-21**

**THIS COURT'S ORDER is that:**

1. The answers to the questions of law posed in this Rule 220 motion are as follows:

    a. Do the deemed trust provisions in section 227 of the *ITA* apply to unsecured creditors? – Yes

    b. Can unsecured creditors rely on the *bona fide* purchaser for value defence to defend against a deemed trust claim? – No

2. The Defendant shall pay the Plaintiff costs of this motion in the lump-sum all-inclusive amount of $1700.00.

"Richard F. Southcott"
Judge

**FEDERAL COURT**

**SOLICITORS OF RECORD**

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|---|---|
| **DOCKET:** | T-1841-21 |
| **STYLE OF CAUSE:** | HIS MAJESTY THE KING v THE TORONTO-DOMINION BANK (TD CANADA TRUST) |
| **PLACE OF HEARING:** | VANCOUVER, BRITISH COLUMBIA |
| **DATE OF HEARING:** | FEBRUARY 22, 2024 |
| **ORDER AND REASONS:** | SOUTHCOTT J. |
| **DATED:** | MARCH 19, 2024 |

**APPEARANCES:**

| | |
|---|---|
| Aminollah Sabzevari | FOR THE PLAINTIFF |
| Christine Lonsdale<br>Anu Koshal<br>Almut MacDonald | FOR THE DEFENDANT |

**SOLICITORS OF RECORD:**

| | |
|---|---|
| Department of Justice<br>Vancouver, British Columbia | FOR THE PLAINTIFF |
| McCarthy Tétrault LLP<br>Toronto, Ontario | FOR THE DEFENDANT |