Docket: 2007-277(IT)G

BETWEEN:

ALBERTA POWER (2000) LTD.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on March 2, 2009, at Calgary, Alberta
By: The Honourable E.P. Rossiter, Associate Chief Justice

Appearances:

Counsel for the Appellant:	Al Meghji and Gerald Grenon
Counsel for the Respondent:	William L. Softley and Kim Palichuk

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JUDGMENT

The appeal from the reassessment made under the *Income Tax Act* for the 2001 taxation year is allowed, and the reassessment is referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with the attached Reasons for Judgment.

Costs are awarded to the Appellant.

Signed at Ottawa, Canada, this 21st day of August, 2009.

"E.P. Rossiter"

E.P. Rossiter

Citation: 2009TCC412
Date: 20090821
Docket: 2007-277(IT)G

BETWEEN:

ALBERTA POWER (2000) LTD.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

E.P. Rossiter A.C.J.

Introduction

[1] In the late 1990s the Province of Alberta ("Alberta") was moving from regulation of the electric energy sector to a deregulated environment. The Appellant was part of the ATCO Group ("ATCO") that owned and operated coal-fired electrical generation plants. As part of the deregulation process, Power Purchase Arrangements ("PPA") for each electrical producer's facility were established by Alberta including a PPA for ATCO's coal-fired plant known as the HR Milner Plant ("plant"). Each PPA was to be subject to auction but the PPA for the plant was pulled from its proposed auction by Alberta due to ATCO's concern as to the economic viability of the plant under its PPA. A Negotiated Settlement Agreement ("NSA") was concluded between ATCO and an Alberta authority ("Balancing Pool"). This NSA was effective December 20, 2000 and included an Operating Agreement ("OA") for the plant with ATCO for a period of time. On termination of the PPA, a payment was made effective January 1, 2001 to the Appellant, a subsidiary of ATCO, of approximately $59.7 million, purportedly for the termination of the PPA with the beneficial ownership of the plant being transferred to the Alberta authority. On January 1, 2001, ATCO entered into an Agreement of Purchase and Sale for the plant with the Appellant and transferred the plant to the Appellant by way of a tax deferred reorganization pursuant to section 85 of the *Income Tax Act* (the "*Act*"). The PPA for the plant was terminated

by Regulation on December 28, 2000 to be effective January 1, 2001. The plant was sold by the Alberta authority to a Third Party on October 30, 2003.

[2] The Appellant claimed the $59.7 million was a capital receipt which gave rise to proceeds of disposition on the basis that the plant and assets had been disposed of in the 2001 taxation year and as such was not profit to the Appellant. The Respondent rejected the position of the Appellant on the basis that the $59.7 million represented future profits surrendered and no beneficial interest was transferred to the Alberta authority, or in the alternative, the payment was a compulsory payment under subparagraph 12(1)(*x*)(iv) of the *Act*.

Facts

[3] ATCO was engaged in utility power generation among other enterprises in Alberta in the 1990s and owned and operated coal-fired generation plants including the plant. The plant was approximately twenty-five years old at the relevant time and had used an inferior quality of coal supply for years which was problematic in the plant operations leading to its continued economic viability being questionable by ATCO.

[4] In 1996 Alberta began the implementation of a plan to deregulate the electrical generation industry. Plants built pre-1995 had a different regime than plants built post-1995. The plants built pre-1995, of which the plant was one, were part of the Alberta regime which would result in total deregulation of different plants over a period of three to twenty years. To facilitate this gradual deregulation, Alberta caused PPAs to be established for each plant including a PPA for the plant. A PPA was a contract-like instrument between an owner of a power plant and a buyer. The owner makes the facility available to the buyer and all the output of the facility goes to the buyer. It allows the owner to recover the capital invested plus a return on the capital and certain other expenses. The buyer of the electricity, as a result, takes all of the risk on the price of the electricity.

[5] Each PPA was to be sold by auction. A Balancing Pool was established by Alberta for the purpose of collecting proceeds from a sale of the PPA at auction and if a PPA was not sold at auction, then the Balancing Pool acted as the PPA buyer. Normally, at the end of a PPA, the utility had a choice - it could decommission the plant and the costs would be covered by the Balancing Pool or they could operate the plant and all the revenues and expenses would go to the utility and all the decommissioning costs would be that of the utility. Under the PPA there was no provision for early termination except if the plant was destroyed

then ATCO would only get its net book value. The PPA for the plant was removed from auction after ATCO expressed strong concerns about the economic viability of the plant under the PPA. ATCO was concerned that the plant could not be economically viable under the PPA because of its poor quality of coal supply which was not recognized by the PPA and the questionable financial stability of the coal supplier for the plant (Smokey River), which was in receivership at the time. ATCO considered decommissioning the plant altogether and put pressure on Alberta to amend the PPA to address their concerns or they could close the plant.

[6] Alberta arranged for an Alberta authority ("Balancing Pool") under statute, which enacted the deregulation scheme, to enter into negotiations with ATCO to keep the plant operational for at least the short term, two to three years. The Balancing Pool undertook the negotiations on its own behalf and on behalf of consumers. The negotiations for the Balancing Pool were lead by Dale Hildebrand who was representing a group of consumers. These consumer groups included industrial institutions, municipal, governmental and residential consumers. These Alberta consumer groups or others, test applications before Alberta utility regulators and were not the actual utility regulator itself. The Department of Energy in Alberta had worked with the consumer groups in the deregulation process and Mr. Hildebrand took the lead in the negotiations with ATCO on behalf of the consumer groups. He had a background in energy generation and extensive experience with PPAs and PPA pricing. He had assisted Alberta in selecting a consultant to develop the PPAs and was part of an independent assessment team that developed the PPAs. He was also involved in the test of the PPAs before the utility board. He also assisted some buyers in analyzing the PPAs prior to their auction. He had never worked for the Appellant previously having primarily worked on the other sides of cases in regulatory proceedings dealing with ATCO. The negotiations between Mr. Hildebrand on behalf of the Balancing Pool and a Victor Post, a Vice-President of ATCO, on behalf of ATCO, resulted in the NSA and OA for the plant.

[7] In the course of negotiations ATCO tried to convince the Balancing Pool to go along with their suggestion for the decommissioning of the plant because of its poor future economic viability. The Balancing Pool was concerned that the plant might be closed in the short term which would result in lower supplies of electrical energy and higher cost of electrical energy to consumers. The Balancing Pool also had concerns that the PPA failed to recognize the capacity limitations of the Plant and its operational problems.

[8] Both negotiators, Mr. Hildebrand and Mr. Post, confirmed that there was no discussion at any time whatsoever about ATCO recovering loss of future profits and that discussions were only about the compensation to ATCO for return of their capital investment, or what is known in part as stranded costs. No calculations were conducted nor was any information exchanged by anyone for ATCO or the Balancing Pool in relation to loss of profits or loss of future stream of profits, nor was it ever considered by either party as an item to be recovered in the NSA by ATCO.

[9] In the OA there was concern with respect to the staff retention. The Balancing Pool wanted the plant to be run for a period of time and then auctioned off. The key to the operation of the plant was employees as they were a key asset and therefore there were certain payments to be made to them to ensure that they stayed at the plant. As a member of the operations committee, Mr. Hildebrand would receive a prepared report from ATCO at every meeting advising as to what transpired in the meantime. The report would include information such as costs, energy production, operational issues, health and safety, et cetera, and there was the committee, which managed the facilities and gave directions to ATCO on the operations of the facilities. The committee directed ATCO to operate the plant on 125 megawatts, not at its capacity of 145 megawatts and also directed ATCO as to how much capital was to be spent on the plant.

Brian G. Millen assisted Vic Post in the course of negotiations. He was familiar with the negotiations and confirmed all aspects of Post's evidence with respect to what the intent was of the parties in relation to the transaction and further prepared schedules to be part of the NSA showing the allocation of the proceeds and how the calculations are done. Both parties understood that they were selling the plant and ATCO was recovering its own invested capital. He also confirmed that the calculations were not consistent with treating the monies being paid as future lost profits. In fact, based on calculations presented, they were totally inconsistent with the suggestion that ATCO was recovering lost profits because the amount recovered was considered to be in excess of the lost profits, which could have been available.

[10] On behalf of the Balancing Pool and consumers group, Mr. Hildebrand had negotiated and agreed, all along, that ATCO would receive its capital investment and decommissioning costs, and that ultimately the decommissioning costs would be paid by the Balancing Pool. The $59.7 million was a return of net capital investment to be paid to ATCO. As a regulated utility, ATCO was given the right to operate the plant in a certain way. In exchange, they were allowed to invest in

capital expenditures once approved by the Alberta Utility Board and in return the consumers would receive their services at cost. The electrical rates were fixed by the utility board by looking at the investor's investment, operating expenses, return of capital investment and income tax implications. The Alberta Utility Board decides, after reviewing these considerations, as to what was appropriate and then set the rate of return and calculated the total revenue required. The investor receives a) its investment; b) return on capital investment if the capital investment was based upon depreciation rates over the operational life of the equipment; c) its operating expenses; and d) the income tax implications of the above. According to Hildebrand, the $59.7 million was not intended to be a payment for loss of future profits. There was no calculation done on this basis at any time and profits were totally irrelevant. The rates were based upon cost, not upon the future price or revenue. The consumers wanted to capture the residual value, that is, once the asset is taken out of regulation it would be owned by the consumers and therefore any value of the asset in the future was the residual value, i.e. generation of money or sales proceeds. The $59.7 million would not have been paid to ATCO if the residual value had stayed with them.

[11] In negotiations, the Balancing Pool was concerned with ensuring the residual value of the plant rested with them and that any credit which might arise in CCA to the benefit of ATCO in the transfer of beneficial interest to the Balancing Pool also go to the Balancing Pool and not remain with ATCO. The CCA pools were greater than the book value and therefore there would be a tax credit to ATCO and there had to be a provision in the NSA that this was part of the residual benefits and it was to flow to the Balancing Pool. In the course of negotiations, it was agreed to by ATCO, that the CCA credit would be paid by ATCO as they received the tax benefit, over a period of time to the Balancing Pool.

[12] Under the NSA, ATCO was to receive its outstanding capital investment of $59.7 million which was the net book value of the plant and its assets. It was the intent of both parties to conclude the NSA on the basis of net book value to ATCO.

[13] The collective effect of the NSA concluded by Hildebrand and Post was as follows:

1. The PPA would be terminated by a 2000 Regulation, effective January 1, 2001;
2. The legal title to the plant would remain with ATCO while all the beneficial interest in the plant would be transferred to the Balancing

Pool on January 1, 2001, including any entitlement of ATCO to a credit on the plant CCA.

3. ATCO would operate the plant for a limited period of time under direction of a sales committee made up of five people – four chosen by the Balancing Pool and one from ATCO, with the ATCO representative not having a vote on the plant operational issues. ATCO would be paid an annual management fee for its operation of the plant.
4. On the termination of the PPA on January 1, 2001, the Balancing Pool would pay the Appellant the sum of $59.7 million.
5. If the plant was not sold within a certain period of time, ATCO would have the option of decommissioning the plant within a certain period of time (one year) and if ATCO did decommission the plant within that period of time then the decommissioning costs would be paid by the Balancing Pool. If the plant was not decommissioned within the specified period of time, and ATCO continued to operate the plant, then ATCO would be responsible for any decommissioning costs that the plant incurred in the future.
6. The Balancing Pool would receive all the proceeds of the sale of the plant to a third party.

[14] On January 1, 2001 ATCO transferred the plant to the Appellant by way of a deferred reorganization pursuant to section 85 of the *Act* and under the NSA the Appellant received $59.7 million from the Balancing Pool “as compensation for the early termination of the PPA”.

[15] Under the terms of the PPA, ATCO was concerned about the required output of the plant over a period of time and the penalties it would have to incur if it failed to meet output targets set out in the PPAs; ATCO did not feel the plant would be profitable over the period of time specified in the PPA.

[16] The plant was sold to a third party by the Balancing Pool in October, 2003. All the proceeds of the sale of the plant became the property of the Balancing Pool. Between January 1, 2001 and the date of the sale to the third party, all the benefits, advantages and responsibilities of ownership of the plant rested with the Balancing Pool except the legal title which rested with ATCO. The legal title rested with ATCO during this interim period for three reasons:

1. The negotiations between ATCO and the Balancing Pool were rushed and there was not enough time to transfer all the permits and licenses of a legal owner to the Balancing Pool;
2. It was the plan all along to find a third party purchaser and it was not worth the cost and effort to have the title to the plant transferred and then transfer it to a third party because it was anticipated that the sale of the plant would occur much earlier than it eventually did to a third party; and
3. There was concern as to whether or not the Balancing Pool might not have been in a position to take ownership of the power plant under its terms of reference.

[17] When the plant was sold, the Appellant was a party to the sales agreement as vendor given that it held the legal title, but all other interests of the property had been held by the Balancing Pool.

[18] The NSA contained a number of particularly relevant articles, including:

1. Article 4(a)(i):

> This agreement and the parties' obligations hereunder shall be subject to:
> …
>
> (a) The making of regulations effective and in force January 1, 2001 which provide for the termination of the PPA; allow the BPA to execute this agreement for and on behalf of the power pool and allowed BPA to exercise such rights and authorities and assume such obligations and liabilities as given to or imposed on it for and on behalf of the power pool council pursuant to this agreement and allow the payments contemplated by this agreement to be made out of the Balancing Pool in accordance with the terms of this agreement …

2. Article 5(b):

> ATCO Electric shall receive payment of the termination compensation from the Balancing Pool as compensation for early termination of the PPA the lump sum amount shall be payable on January 1, 2001 …

3. Article 5(d):

> ATCO Electric agrees that amounts equal to the tax benefit accruing to ATCO Electric arrive from CCA pool surpluses attributable to the Plant shall be paid annually for the years 2001 to 2020, inclusive, to the Balancing Pool by ATCO Electric within ten days of its receipt …

[19] Schedule "A" of the NSA was entitled "Compensation for Early Termination of the PPA" and it states in part as follows:

> Compensation from the Balancing Pool of "book value" for early termination shall be based on a lump sum amount plus actual amounts, the 2000 capital cost additions and the 2000 year end coal inventory as shown below.

The lump sum amount of approximately $59.7 million was made up of approximately $54.8 million for the closing net book value of the plant assets, $2.1 million for the closing net book value for the corporate general administrative assets, and a variety of adjustments in respect to inventory with a further adjustment for decommissioning provision. There was no reference in Schedule A to monies for future profits surrendered; only references were made to net book values.

[20] Schedule G to the NSA was entitled "ATCO Electric Ltd., H.R. Milner U.C.C./Tax Calculation Allocation of Proceeds". Schedule G showed how the undepreciated capital cost was allocated given the purchase price and the applicable percentages to the applicable classes.

[21] In the NSA determination of "compensation" was defined to mean the sum of the lump sum amount and any additional amount (lump sum amount referring to the $59.7 million).

[22] The NSA also referred to the OA as Schedule "B" to the NSA with Schedule "B" being incorporated into and forming part of the NSA.

[23] In the OA preamble, ATCO was described as the owner of the plant.

[24] The OA contained a number of articles which are particularly relevant. Article 2.5(a):

> Upon termination of this agreement, except for … ATCO may continue with the ongoing operation of the Plants for its own use effective from and after the date of

termination of this agreement in which case it shall be entitled to receive all revenues and shall assume all liabilities and obligations resulting from the operation thereof …

Article 3.1:

During the term of this agreement, all revenue from the operation and ownership of the Plant and the Licensed Facilities shall be paid into the Balancing Pool. …

Article 3.2(a):

During the Term of this Agreement, ATCO Electric shall be entitled to receive payment from the Balancing Pool of all reasonably and necessarily incurred costs associated with the operation of the Plan, provided such costs are approved by the Operations Committee …

Article 4.1:

An Operations Committee shall be established consisting of four representatives of the BPA and one representative of ATCO Electric. The Parties shall appoint their respective representative(s) to the Operations Committee forthwith upon execution hereof. ATCO Electric and the BPA agree that two of the representatives appointed by the BPA shall be designated by the Consumers.

Article 7(a):

(a) ATCO Electric shall operate the Plant from and including January 1, 2001, under the terms of the operating agreement.

(b) The operating agreement shall be executed concurrently with the execution of this agreement.

Article 7.1:

ATCO Electric shall received additional payment of the Management Fee from the Balancing Pool. …

Article 9.2:

During the Term, ATCO Electric shall have legal title to the Plant and License Facilities subject to a beneficial interest in the Plant and Licensed Facilities in favour of the Power Pool for the full benefit and advantage of the Consumers.

[25] For the process of the sale of the plant to a third party, a sales committee was established to market the plant, made up of five persons, one from ATCO and four from the Balancing Pool. Only the members representing the consumers' interest (Balancing Pool) had a voting right. ATCO sat on the committee without a vote because:

1. The consumers wanted ATCO's assistance in selling the plant and providing assistance to the prospective buyers in doing their due diligence.
2. ATCO was concerned about the potential of residual liability in the plant therefore they wanted some input in the selection of a buyer. They did not want liability if the plant was decommissioned or if there was environmental liability and wanted to ensure that the purchaser would give ATCO an indemnity that they would not be responsible for any of the potential liabilities.

[26] On the sale to the third party, the Balancing Pool gave an indemnification to the Appellant because the third party did not have the financial wherewithal to provide an indemnity. On the sale of the plant the Appellant received nothing from the proceeds of the sale except a fee of $200,000 for assisting to facilitate the sale.

[27] Under the OA, an operations committee was to oversee the business and operations of the plant and to consider, evaluate and form a business strategy for the continued operation of the plant and licensed facilities in order to minimize costs and maximize the availability and benefits to the consumers. This committee also to give direction to ATCO with respect to the management of the plant, considered and approved any recommendations of ATCO based on ongoing operations of the plant and licensed facilities, and it also directed the Appellant to take or refrain from taking any action regarding the plant and licensed facility.

[28] As managers of the plant, the Appellant received a base fee of $750,000 made up of a minimum fee of $500,000 plus additional compensation if certain operational targets were met (a base fee plus incentives).

Issues

[29] 1. Was the lump sum payment of $59.7 million paid by the Balancing Pool to the Appellant a capital receipt or income receipt under section 9 of the *Act*?

2. Alternatively, if the payment was not income received under section 9 of the *Act*, was the payment a compulsory payment under subparagraph 12(1)(*x*)(iv) of the *Act*?

3. If the $59.7 million is a receipt under section 9 of the *Act*, under what year is the amount taxable, 2000 or 2001?

4. There were additional issues as to whether the current expenditures of $6,002,362 were properly deducted in computing the Appellant's profit for 2001; whether the adjusted current expenditures of $1,335,540 were properly deductible in computing the Appellant's profit for 2001 and finally whether the adjusted current dismantling expenditures of $225,888 were properly deductible in computing the Appellant's profits for the years. On these latter issues, there was agreement between the Appellant and Respondent, that of the $7,565,720 of repair and maintenance expenses, $4,539,430 were currently deductible in the 2001 taxation year and the remaining $3,026,288 were properly treated as additions to the undepreciated capital cost of the Appellant's capital cost allowance pools. This agreement will be reflected in the order coming from this particular Judgment.

Pleadings & Parties' Positions

[30] The Appellant filed an Amended Notice of Appeal on October 14, 2008 requesting the following relevant relief (save and except the relief which relates to the items agreed to). The Appellant requested that the appeal be allowed, with costs, and the reassessment for the taxation year ending December 31, 2001 be referred back to the Minister for reconsideration and reassessment on the following basis:

> (i) that the Lump Sum Payment in the amount of $59,737,728 under the NSA was a capital receipt and not profit; or alternatively, even if profit, was not properly included the Appellant's income in the 2001 taxation year;
>
> …
>
> 41.In Addition to the relief set out above, the Appellant requests that consequential to any adjustments made in respect of the items in the above paragraphs that the Appellant be permitted to recalculate its capital cost allowance, capital cost allowance recapture, resource allowance and earned

depletion allowance, and manufacturing and processing profits deduction for the taxation year.

42. In addition to the relief set out above, the Appellant requests that it be allowed to claim any unused permissive deductions, including but not limited to, CCA, CEC, non-capital losses from other years, net capital losses from other years and investment tax credits and such amounts as may be determined.

[31] The Respondent filed an Amended Reply on October 27, 2008 and separate and apart from what was agreed upon, related the following with respect to the ground relied upon and relief sought:

21. He submits that the receipt of $59M is properly treated as income and included in the Appellant's income in the 2001 taxation year in that:

a) the N.S.A. does not represent a sale purchase agreement for the Milner Plant. Rather, the $59M payment under the N.S.A. is payment of the termination compensation from the B.P. as compensation for early termination of the Milner Plan P.P.A. and represents future profits surrendered;

b) furthermore, under the N.S.A. there was no transfer of beneficial ownership in the Milner Plant within the meaning of paragraph 248(1)(*e*) of the *Act*. Nor was there a sale of the Milner Plan to B.P. for purposes of the *Sale of Goods Act*.

22. In the alternative, he states that the B.P. was required to compensate ATCO when the Milner Plan PPA was terminated, pursuant to the provisions of Regulation 170/99; 106/2000; and 331/2000. As such, the amount of $59M constitutes a compulsory payment that is taxable under paragraph 12(l)(*x*)(iv) of the *Act*, and is properly included in the Appellant's income in the 2001 taxation year in that ATCO received the $59M from a public authority as reimbursement for an amount that was included in the cost of property, or an outlay or expense, that was the Milner Plant and related properties.

[32] The position of the Appellant is that ATCO did not want to continue with the PPA; they wanted the PPA terminated and they wanted compensation for their investment in the plant and commenced negotiations in this regard. Negotiations were concluded with the result that all profits and losses from the plant (before the plant was sold to a third party by the Balancing Pool) went to the Balancing Pool. ATCO operated the plant pending the plant's sale and the proceeds paid to ATCO by the Balancing Pool were the proceeds of disposition of the plant and not income under s. 9 of the *Act*. The Appellant further argues that if the Appellant is in error,

then the $59.7 million paid under the NSA was income in 2000 and not in 2001. Under the accrual accounting principle, the amount was properly taxable in 2000 and not 2001. The Appellant disputes that there was no transfer of the beneficial ownership. Further the Appellant also says that there was not a compulsory payment under paragraph 12(1)(*x*) of the *Act*.

[33] The Respondent's position basically is that the amount paid to ATCO is compensation for a stream of lost future profits and therefore income under section 9 of the *Act* and further, that a beneficial interest was not and could not be transferred to the Balancing Pool because it did not have the capacity to hold such a beneficial interest and, in the alternative, the payment was a compulsory payment under subparagraph 12(1)(*x*)(iv) of the *Act*.

Applicable Statutes and Regulations

[34] There are numerous statutory and regulatory provisions which are relevant to the issues before the Court.

[35] Section 9 of the *Act* states:

> 9.(1) Subject to this Part, a taxpayer's income for a taxation year from a business or property is the taxpayer's profit from that business or property for the year.
>
> (2) Subject to section 31, a taxpayer's loss for a taxation year from a business or property is the amount of the taxpayer's loss, if any, for the taxation year from that source computed by applying the provisions of this Act respecting computation of income from that source with such modifications as the circumstances require.
>
> (3) In this Act, "income from a property" does not include any capital gain from the disposition of that property and "loss from a property" does not include any capital loss from the disposition of that property.

[36] Subparagraph 12(1)(*x*)(iv) of the *Act* states as follows:

> (iv) as a refund, reimbursement, contribution or allowance or as assistance, whether as a grant, subsidy, forgivable loan, deduction from tax, allowance or any other form of assistance, in respect of

(A) an amount included in, or deducted as, the cost of property, or

(B) an outlay or expense,

to the extent that the party amount

…

[37] Paragraphs 1(1)(*c*) and (*f*) of the *Electric Utilities Act*, R.S.A. 2000 c.E-5 ("EUA") *Balancing Pool Regulation)Regulation 169/99 states*:

…

(c) "balancing pool administrator" means the person or persons appointment under section 2(1)(c);

…

(f) "Council" means the Power Pool Council;

[38] Subsections 2(1), 3(1) section 4, subsection 5(1), sections 6 and 7 of the *EUA*, reads as follows:

2(1) The Council shall, before December 31, 1999,

(a) establish a separate financial account or accounts to be known as the balancing pool,

(b) establish the rules of the balancing pool, and

(c) appoint a qualified person or persons to act as the balancing pool administrator.

…

3(1) The balancing pool administrator must carry out its powers and duties in the name of the Council and all powers and duties carried out by the balancing pool administrator or a person referred to in subsection (2) are deemed to have been carried out on behalf of the Council.

…

4 The balancing pool administrator shall carry out the following powers and duties in accordance with the Act, the regulations and the rules of the balancing pool;

(a) sign contracts, agreements and other instruments in respect of the balancing pool;
(b) make and maintain banking arrangements in respect of the balancing pool;
(c) borrow money from any person or enter into overdraft or line of credit arrangements with a bank, treasury branch, credit union, loan corporation or trust corporation for the purpose of meeting obligations of the balancing pool as they become due, and give security for the loan, overdraft or line of credit;
(d) draw, make, accept, endorse, execute or issue promissory notes, bills of exchange or other negotiable instruments in respect of the balancing pool;
(e) hire employees, consultants and advisors required in connection with the administration of the balancing pool and the performance of the powers and duties of the Council and the balancing pool administrator and determine the duties, terms of engagement and remuneration of the employees, consultants and advisors;
(f) determine the amount of any obligation or expenditure payable out of the balancing pool under section 7(1)(h);
(g) carry out any other duties that are necessary to administer the balancing pool.

5(1) The balancing pool administrator shall carry out the following powers and duties in accordance with the Act, the regulations, the rules of the balancing pool and any arrangement:

(a) oversee the payment into the balancing pool of the amounts referred to in section 6;
(b) oversee the payment out of the balancing pool of the amounts referred to in section 7;
(c) determine the amounts of any balancing pool credits and balancing pool charges;
(d) allocate balancing pool credits directly to customers or indirectly to customers through
(i)retailers
(ii)wire service providers,
(iii) the power pool administrator;
(e) levy balancing pool charges directly against customers or against customers through
(i)retailers
(ii)wire service providers,
(iii) the power pool administrator;
(f) offer for sale to the public an arrangement held by the balancing pool administrator as a party to the arrangement;

(g) offer for sale to the public any derivatives created by the balancing pool administrator pursuant to the *Power Purchase Arrangements Regulation* (AR 170/99);

(h) exercise any powers and perform any duties that accrue to the balancing pool administrator as a party to an arrangement or to the balancing pool under an arrangement;

(i) exercise or assign to a third party the right to exchange electric energy through the power pool that arises as a result of the balancing pool administrator being a party to an arrangement;

(j) on receipt of notice in respect of an extraordinary event from a party to an arrangement or otherwise, assess and verify the occurrence of the extraordinary event and the need for any payment to be made into or out of the balancing pool by or to a party under the provisions of the arrangement, and participate in any dispute resolution proceedings under an arrangement pursuant to subsection (3);

(k) where clause (j) applies, commence making payments set out in the arrangement until the matters in question under clause (j) have been resolved, whether by agreement or in dispute resolution proceedings under subsection (3);

(l) make, defend, settle and withdraw claims and counterclaims against the balancing pool relating to an arrangement that the balancing pool administrator holds as a party to the arrangement;

(m) make, defend, settle and withdraw claims and counterclaims against retailers, wire service providers, customers and any other persons relating to the payment of balancing pool credits or charge.

….

6 The following amounts must be paid into the balancing pool

(a) any payment, fee, charge or other amount that is required by the Act or the regulations to be paid into the balancing pool;

(b) any payment, fee, charge or other amount that is required by an arrangement to be paid into the balancing pool, including any payment that is required to be made as a result of the occurrence of an extraordinary event or as the result of the resolution of a dispute referred to in section 5(3);

(c) any balancing pool charge payable, directly or indirectly, by a customer pursuant to billing;

(d) any money borrowed for the purpose of meeting the obligations of the balancing pool;

(e) any principal, income, dividend or other amount received in connection with investments made pursuant to section 8;

(f) any amount received by the balancing pool administrator in respect of an arrangement held by the balancing pool administrator as a party to the arrangement;

(g) any fine imposed by the Council in accordance with section 9.5(1)(c) of the Act;

(h) any amount approved by the Board as payable into the balancing pool for any period prior to an arrangement taking effect;
(i) any other amount received in the course of the administration of the balancing pool, except an amount that is specified by the Minister as not being payable into the balancing pool.

7(1) The following amounts must be paid out of the balancing pool:

(a) any payment, fee, charge or other amount that is required by the Act or the regulations to be paid out of the balancing pool;
(b) any payment, fee, charge or other amount that is required by an arrangement to be paid out of the balancing pool, including any payment that is required to be made as a result of the occurrence of an extraordinary event or as the result of the resolution of a dispute referred to in section 5(3);
(c) any balancing pool credit owing, directly or indirectly, to a customer pursuant to billing.
(d) any principal or interest to be paid or repaid in connection with an amount borrowed for the purpose of meeting the obligations of the balancing pool;
(e) money payable as the purchase price for investments made pursuant to section 8;
(f) any amount payable by the balancing pool administrator in respect of an arrangement held by the balancing pool administrator as a party to the arrangement;
(g) any amount approved by the Board as payable out of the balancing pool for any period prior to an arrangement taking effect;
(h) any other obligation or expenditure incurred in the course of the administration of the balancing pool, except those that are specified by the Minister as not being payable out of the balancing pool.

(2) For the purposes of subsection (1)(*h*), no amount may be paid out of the balancing pool relating to obligations or expenditures incurred in the course of the administration of the power pool.

(3) Nothing in the *Act*, the regulations or an arrangement is to be construed so as

(a) to relieve an insurer from its obligations under a policy of insurance, or
(b) to require an amount otherwise recoverable under a policy of insurance to be paid out of the balancing pool.

[39] Paragraphs 8(1), 8(2), 8(4)(c) of the EUA *Power Purchase Arrangements Regulation* (Regulation 170/99) state:

8(1) Where

(a) no acceptable bids are received for a power purchase arrangement at an auction (other than a power purchase arrangement referred to in section 26 of the General Units Regulation (AR 72/99)),
(b) a power purchase arrangement is converted to a financial instrument under section 45.94(2)(b) of the Act, or
(c) a power purchase arrangement is sold to a purchaser at an auction and the power purchase arrangement terminates other than pursuant to section 15.2 of the power purchase arrangement,

the power purchase arrangement

(d) is deemed to have been sold to the balancing pool administrator at an auction, and
(e) is to be held by the balancing pool administrator in the capacity of a purchaser for all purposes of the Act, the regulations made under the act and the power purchase arrangement.

(2) Where subsection (1) applies, the balancing pool administrator shall immediately become entitled to the rights and be bound by the obligations of a purchaser and, from that time, the power purchase arrangement has effect in accordance with its terms and conditions, as amended from time to time in accordance with the arrangement, subject to the following:

(a) sections 4.3(j), 7.3, 14.6, 15.3, 15.4 and 17.4 of the power purchase arrangement are deemed to be deleted;
(b) sections L3.1, L3.2(a), (c), (e) and (f), L3.4, L3.5 and L4.1 of Schedule L of the power purchase arrangement are deemed to be deleted;
(c) section 14.4 of the power purchase arrangement is deemed to be replaced with the following:

14.4 During any period in which the Owner's obligation to perform or comply with an obligation under this arrangement is suspended, the Monthly Capacity Payment shall be the same amount as the Provisional Capacity Payment, notwithstanding any other provision of this arrangement.

…

(4) Where subjection (l) applies, the balancing pool administrator may, notwithstanding the terms and conditions of the power purchase arrangement, terminate the power purchase arrangement if the balancing pool administrator

…

> (c) pays to that owner or ensures that the owner receives an amount equal to the remaining closing net book value of the generating unit, determined in accordance with the power purchase arrangement as if the generating unit had been destroyed, less any insurance proceeds.

[40] Paragraphs 2(4), 2(5) and 6 of the EUA, *Power Purchase Arrangement Auction Regulation*, (Regulation 85/2000) state:

> 2(4) Only power purchase arrangements that apply to thermal units may be offered for sale at the auction.
>
> (5) A power purchase arrangement must be offered for sale at the auction for the entire term of the power purchase arrangement, as set out in the power purchase arrangement.
>
> …
>
> 6 The Minister may adjourn or suspend the auction at any time.

[41] Paragraphs 1 and 2 of the EUA *Power Purchase Arrangements Amendment Regulation*, (Regulation 106/2000) state:

> 1 The Power Purchase Arrangements Regulation (AR 170/99) is amended by this Regulation.
>
> 2 Section 6 is repealed and the following is substituted.
>
> 6(1) In this section, "derivatives", in respect of a power purchase arrangement that applies to a Part 1 unit, means partial financial rights, interests and obligations derived from the power purchase arrangement where the underlying commodity is electricity or electricity services, but does not include a transfer of the power purchase arrangement in whole or in part to the buyer of the derivative.
>
> (2) Notwithstanding section 45.93(1) of the Act, a power purchase arrangement that applies to a hydro unit and the power purchase arrangement that applies to the H.R. Milner generating unit
>
> > (a) are not to be offered for sale to the public at an auction, but are deemed to have been sold to the balancing pool administrator at an auction, and
> >
> > (b) are to be held by the balancing pool administrator in the capacity of a purchaser for all purposes of the Act, the regulations made under the Act and the power purchase arrangements.

(3) A power purchase arrangement that is held by the balancing pool administrator under this section has effect in accordance with its terms and conditions.

(4) The balancing pool administrator who holds a power purchase arrangement under this section

(a) may create derivatives and offer those derivatives for sale to the public, and
(b) may offer the power purchase arrangement that applies to the H.R. Milner generating unit for sale to the public.

(5)The regulations referred to in section 45.93(3) of the Act may establish rules relating to the creation and sale of derivatives.

(6) Section 45.94 of the Act does not apply in respect of

(a) the sale of derivatives under this section, or
(b) the sale of the power purchase arrangement that applies to the H.R. Milner generating unit under this section.

[42] Paragraphs 1, 2, 3, 4 and 5 of the EUA, *H.R.Milner Generating Unit Negotiated Settlement Implementation Regulation* (Regulation 331/2000) state:

1 In this Regulation,

(a) "ATCO means"

(i)ATCO Electric Ltd., or
(ii) an affiliate of ATCO, as defined in the Milner Power Purchase Arrangement, to which ATCO Electric Ltd. Has the right pursuant to the negotiated settlement agreement to assign that agreement;

(b) "balancing pool administrator" means the person or persons appointed under section 2(1)(c) of the Balancing Pool Regulation (AR 169/99);

(c) "Milner Power Purchase Arrangement" means the power purchase arrangement that applies to the H.R. Milner generating unit;

(d) "negotiated settlement agreement" means the agreements relating to the H.R. Milner generating unit dated December 20, 2000 and made between

(i) ATCO and the balancing pool administrator, or

(ii) the balancing pool administrator and entitles described in the agreement as consumers,

and any amendments to those agreements that the Minister consents to.

2(1) The balancing pool administrator has the power to carry out any duty or function described in the negotiated settlement agreement as a duty or function of the balancing pool administrator.

(2) The balancing pool administrator must make the payments and carry out the other obligations described in the negotiated settlement agreement as being obligations of the balancing pool administrator.

3 ACTO must make the payments and carry out the other obligations described in the negotiated settlement agreement as being obligations of ATCO.

4 The Milner Power Purchase Arrangement is terminated on January 1, 2001.

5 For the purpose of ensuring that this Regulation is reviewed the ongoing relevancy and necessity, with the option that it may be repassed in its present or an amended form following a review, this Regulation expires on December 31, 2005.

[43] Paragraphs 2(1) of the EUA *Balancing Pool Regulation*, (Regulation 158/2003) state:

2(1) The Balancing Pool must carry out the following powers and duties in accordance with the Act, the regulations and any arrangement:

(a) oversee the payment into the balancing pool accounts of the amounts referred to in section 4;
(b) oversee the payment out of the balancing pool accounts of the amounts referred to in section 5;
(c) offer for sale an arrangement held by the Balancing Pool as a party to the arrangement;
(d) create and offer for sale derivatives in respect of arrangements held by the Balancing Pool and enter into financial and other transactions and agreements relating to those derivatives, arrangements and the Balancing Pool;
(e) exercise any powers and perform any duties that accrue to the Balancing Pool as a party to an arrangement or to the Balancing Pool under an arrangement;

(f) exercise, authorize a third party to exercise or grant or assign to a third party any right, entitlement, interest, term, condition or obligation that arises as a result of the Balancing Pool being a party to an arrangement;
(g) on receipt of notice in respect of an extraordinary event from a party to an arrangement or otherwise,
(i) conduct any investigation the Balancing Pool determines appropriate, and
(ii) participate to the extent determined appropriate by the Balancing Pool in any dispute resolution process between parties to the arrangement;
(h) when clause (g) applies,
(i) agree with the parties to the arrangement that the extraordinary event has occurred and that there is a need for a payment to be made to or by the Balancing Pool, or
(ii) assess and verify the occurrence of the extraordinary event and the need for any payment to be made by or to a party under the provisions of the arrangement, and participate in any dispute resolution proceedings under an arrangement pursuant to subsection (2);
(i) on receipt of notice under clause (g), begin making payments as set out in an arrangement until all matters arising pursuant to clauses (g) and (h) are agreed to or resolved;
(j) make, defend, settle and withdraw claims and counterclaims against the Balancing Pool relating to an arrangement that the Balancing Pool holds as a party to the arrangement;
(k) carry out any other powers or duties that are necessary for the administration and operation of the Balancing Pool.

Analysis

Issue No. 1

Was the lump sump payment of $59.7 million paid by the Balancing Pool to the Appellant a capital receipt or income receipt under section 9 of the *Act*?

[44] The Appellant argues that the central question is whether the $59.7 million represents future profits surrendered; if this is the question, one must look to the intent of the parties as what was the commercial deal between the parties. The Respondent takes a different approach and says that it is all about the statutory framework, that is, the statutory intention and the way in which the agreements were made and were to work. The transaction, regardless of the intention, must be technically correct and right in law in order for the Appellant to be successful.

[45] Regardless of which approach is taken, I must deal with both issues. First of all, what is the commercial deal between the parties and then once that is

determined, does that fit within the confines of the *Act* and the regulatory regime in place?

[46] What is the law in determining whether or not the financial exchange is return of capital investment, or payment for future profits surrendered? In *Tsiaprailis v. Her Majesty the Queen*, 2005 SCC 8, the Supreme Court of Canada looked at the "surrogatum principle". Madame Justice Charron, on behalf of the majority, stated at paragraph 7:

> **7** In my view, this conclusion runs counter to the principle that awards of damages and settlement payments are inherently neutral for tax purposes. My colleague takes no issue with this principle. As she explains, in assessing whether the monies will be taxable, we must look to the nature and purpose of the payment to determine what it is intended to replace. The inquiry is a factual one. The tax consequences of the damage or settlement payment is then determined according to this characterization. In other words, the tax treatment of the item will depend on what the amount is intended to replace. This approach is known as the *surrogatum* principle. As noted by Abella J., it was defined in *London and Thames Haven Oil Wharves, Ltd. v. Attwooll*, [1967] 2 All E.R. 124 (C.A.), and subsequently adopted in a number of Canadian cases: see P. W. Hogg, J. E. Magee and J. Li, *Principles of Canadian Income Tax Law* (4th ed. 2002), at pp. 91-93; and V. Krishna, *The Fundamentals of Canadian Income Tax* (8th ed. 2004), at pp. 413-15.

At paragraph 15, the Court went on to state, in part:

> a. The determinative questions are: (1) what was the payment intended to replace? And, if the answer to that question is sufficiently clear, (2) would the replaced amount have been taxable in the recipient's hands? In this case, the evidence of what the amount was intended to replace is clear and cogent. …

[47] Further, in *Charles R. Bell Ltd. v. Her Majesty the Queen*, 92 DTC 6472 (F.C.A.) Mr. Justice Letourneau, on behalf of the Federal Court of Appeal, stated in part as follows:

> … There was ample evidence on which the Trial judge could base his findings. He correctly applied the legal principles relevant in such cases. He looked at the purpose intended by the parties when the negotiated payment of $300,000 was made in compensation for the cancellation of an exclusive distribution to, or impairment of, the trading structure of the appellant.

[48] Further, in *Pe Ben Industries Company Limited v. Her Majesty the Queen*, 88 DTC 6347, Mr. Justice Strayer of the Federal Court (Trial Division), in dealing with a capital gain or income at page 6349 stated:

> I do not consider that the question of whether the payment was simply "on termination" or was "for termination" and thus liquidated damages, is determinative of whether that payment is capital or income in the hands of the recipient. One must look to see what loss was encompassed, that of capital or that of income …

The Courts are saying that basically you must look and see what hole was the payment intended to fill, that is, is the hole one in relation to capital or in relation to profits. What did the parties intend to do?

[49] To use the words of the Supreme Court of Canada in *Tsiaprailis v. Her Majesty the Queen*, an application of the surrogatum principle on the evidence before me as to what the amount was intended to replace, is clear and cogent.

[50] The two individuals who were leading the negotiations on behalf of their respective clients/employer and who concluded the agreement between ATCO and the Balancing Pool which resulted in the payment of $59.7 million from the Balancing Pool to the Appellant were *ad idem*, that the monies paid were not payment for future profits surrendered but rather, the parties clearly were of the understanding and in agreement that ATCO was receiving payment compensation for its capital investment in the plant. The evidence was clear and uncontradicted, that ATCO had a PPA for the plant but wanted to terminate the PPA because they expected to lose money on the plant's operation under the PPA. ATCO wanted to close the plant. The Respondent says that even though ATCO wants out of the PPA and to close the plant, someone is going to pay them $59.7 million as payment for future profits surrendered. This is not the evidence before this Court. This is not the evidence from the persons who negotiated the NSA, the Vice-President of ATCO, Victor Post and Dale Hildebrand representing the Balancing Pool and consumers. All negotiations and discussions in relation to the commercial objective before the NSA was executed in December, 2000, show that the agreement was specific as to what ATCO was getting paid for; there was no dispute or disagreement as to what ATCO were getting paid for or what the Balancing Pool was going to receive for the $59.7 million. ATCO was going to receive its capital investment in the plant as they would in a regulatory world. The negotiations were really about how to keep the plant open in the short term. The Balancing Pool and consumers needed ATCO to keep the plant operational to meet the Balancing

Pool's objective of keeping the cost of electricity low for a short period of time until they were able to sell the plant to a third party. The representative for the Balancing Pool and creditors saw that ATCO was going to have a certain indemnity if the transfer was made to the Balancing Pool and that was its capital investment in the plant.

[51] All the beneficial interest in the plant was transferred to the Balancing Pool, save and except legal title. I agree with the submission of the Appellant that everyone knew that the $59.7 million was going to result in a capital cost allowance credit to the benefit of ATCO and the only way this credit could occur was if the Balancing Pool was paying for an asset that the capital cost allowance related to, otherwise the capital cost allowance credit was irrelevant. This understanding is inconsistent with the suggestion that the $59.7 million was payment for surrender of future profits. This scenario results in the payment being out of section 9 of the *Act* as it is for a capital receipt not income receipt. In addition to this understanding as per Post and Hildebrand's *viva voce* evidence, in the course of negotiations and discussions of the commercial nature of the transaction, there are the agreements themselves and what they say about the proceeds of the sale, capital disposition and lost profits. In the NSA, there are condition precedents to the close of the transaction, including the termination of the PPA, the allowance of the Balancing Pool to execute the agreement for and on behalf of the Power Pool Council and allowing the Balancing Pool to exercise its rights and authorities and assume its other obligations and liabilities, to give to it or impose on it, for and on behalf of the Power Pool and allow the payments contemplated by the agreement to be made out of the Balancing Pool. Although the NSA provided at paragraph 5(b) that ATCO was to receive payment from the Balancing Pool as compensation for early termination of the PPA, the termination compensation was to be a lump sum amount. Lump sum amount is defined as the lump sum amount in Schedule A attached to the NSA. Schedule A of the NSA is entitled "Compensation for Early Termination of PPA". Notwithstanding the reference to "compensation for early termination of the PPA", when one looks at Schedule A, clearly the lump sum payment is made on the basis of the net book value for the plant assets, the closed net book value for the corporate, general and administrative assets, the closing balance for the unamortized amounts in the reserve for injuries and damages, and the closing net book value for spare parts and inventory plus reference to capital cost, year-end inventory. There is absolutely no reference to the phrase "profits" or "loss or surrendering of profits" or anything of that nature. Further, in paragraph 5(b) of the NSA there is reference to ATCO agreeing that the amounts equal to the tax benefit accruing to ATCO arise from the CCA pool surplus attributable to the plan, should be paid annually for the years

2001 to 2020 inclusive to the Balancing Pool by ATCO. This provision is totally inconsistent with the suggestion that the payment was for surrender of future profits. Also, attached as Schedule G to the NSA, is the plant's UCC/tax savings calculation allocation of proceeds which reviews, in detail, the undepreciated capital cost allowance, the breakdown of the proceeds of disposal in the Schedule A figures: this schedule is totally inconsistent with the suggestion that the Appellant was receiving the payment as compensation for surrender of future profits.

[52] Incorporated into the NSA is an OA which was executed concurrently with the NSA. The OA is also consistent with the position taken by the Appellant and inconsistent with the position taken by the Respondent. The OA is an extension of the NSA and refers to the obligations of the parties with respect to the operation of the plant once the benefit interest in the Plant (as will be described later) was transferred to the Balancing Pool. The fact that there is an OA for the Appellant to operate the plant post the transfer of its beneficial interest in the plant (save and except legal title) to the Balancing Pool, and receiving payment as a management fee plus incentive fees, is inconsistent with the position taken by the Respondent.

[53] The several key documents, that is, the PPA, the NSA and the OA, taken with the *viva voce* evidence of Mr. Post as Vice-President of ATCO and Mr. Hildebrand, as negotiator on behalf of the Balancing Pool and the consumers, both of whom were well experienced and familiar in the regulatory regime in existence in Alberta at the time and the intent of the government to de-regulate the electrical generation industry, are very consistent with the plan put in effect and ultimately concluded between the parties on the following basis:

1. ATCO was the owner of the plant;
2. The plant was an inefficient operation. It was difficult to operate on an economically viable basis because of the poor quality of the coal supply and was basically worn out with little prospects of operating on a positive economic basis in the future;
3. Alberta imposed a PPA upon ATCO for the plant. ATCO was of the view that this PPA would not allow it to operate the plant on an economically viable basis and it would likely result in ATCO losing money on the plant operations and suffering significant penalties if they failed to meet certain PPA output targets;
4. As a result of its views with respect to the plant PPA, ATCO wanted to close the plant and entered into discussions with Alberta in this regard. Alberta then brought in the Balancing Pool and consumers to negotiate an

agreement with ATCO, for the continued operation of the plant in the short term and the transfer of the plant's ownership ultimately to a third party;

5. In order to facilitate the concerns of ATCO with respect to the economic viability of the operation of the plant and the concerns of the Balancing Pool and consumers that the plant must operate on a short term basis to ensure that electrical rates would not go higher than they were at the time and therefore more costly to the consumer, Alberta would terminate the PPA, upon agreement being reached between ATCO and the Balancing Pool whereby the beneficial interest in the plant in question would be transferred to the Balancing Pool and ATCO would enter into an OA for the plant for the short term. The OA would provide that ATCO would operate the plant in the short term, under the direction of the sales operations committee, controlled by the Balancing Pool until the Balancing Pool had an opportunity to dispose of the plant to a third party. ATCO was to operate the plant for a certain period of time and if it was not transferred to a third party within that period of time, ATCO could decommission the plant within one year in which case the decommissioning costs would be borne by the Balancing Pool. If ATCO did not decommission the plant within the one year time period, then the decommissioning costs would be the responsibility of ATCO.

[54] The foregoing is the essence of the agreement between the parties such that ATCO was going to receive back its capital investment of $59.7 million, the net book value of its capital investment; that was what it was going to receive back, nothing more, nothing less. There were no discussions, talks, negotiations, calculations or communications whatsoever by anyone with respect to compensation being paid to ATCO for surrender of future profits on the termination of the PPA.

[55] The Respondent suggests that the payment was for surrender of future profits and that there were some phrases or wording in agreements or other documentation during the course of negotiations or post-conclusion of agreements to support this view. Both Mr. Post and/or Mr. Hildebrand rejected this suggestion repeatedly in their *viva voce* evidence. I refer to the following phrases or wording in documents referenced by the Respondent on this point:

1. In the NSA (Exhibit A-1, Tab 1), paragraph 5(b):

> … compensation for early termination of the PPA.

I have already commented on this provision in the NSA.

2. Schedule A to the NSA: “Compensation for Early Termination of the PPA” I have already commented on this particular phrase.

3. The reference in the recitals of the OA (Exhibit A-1, Tab 2). “Whereas ATCO Electric is the owner of the plant”. This particular statement is not inconsistent with the position of the Appellant, since it clearly states in article 9.2 of the OA, that ATCO shall have legal title to the plant and licensed facilities subject to the beneficial interest in the plant and licensed facilities that is in favour of the Balancing Pool for the full benefit and advantage of the consumers. It was my view that the phrase owner is not inconsistent with the fact that ATCO Electric was to continue to have legal title to the plant in question under article 9.2 of the OA.

4. The phrase “termination compensation” in article 1.1(nn) in the OA is not inconsistent with what is contemplated in the NSA because it states that “termination compensation”, as defined under article 1.1(oo) of the NSA, means lump sum amount and the additional amount; lump sum amount is the lump sum amount in Schedule A attached thereto. Schedule A clearly shows in my view that the lump sum amount is for a return of a capital investment. It consistently refers to net book value throughout and capital cost allowance and does not make any reference whatsoever anywhere in the document to a surrender of future profits.

5. The e-mail of May 2, 2000 (Exhibit A-1, Tab 4) refers to the fact that the consumer group, as represented by Mr. Hildebrand, reached an agreement that ATCO should receive their capital investment and decommissioning costs and that the consumer group wants to capture any residual value of the facility in this site. This was all explained in Mr. Hildebrand’s evidence, which was consistent completely with Mr. Post’s evidence. The largest component of costs to be recovered was going to be the capital investment but this is all broken down quite clearly in Schedule A of the NSA which was how the lump sum payment was calculated. Again, with respect to the plant negotiations between the Balancing Pool and ATCO, it clearly stated that ATCO was to receive its outstanding investment in the plant and was being paid its remaining book value. This e-mail is consistent with what the parties negotiated and what was in evidence.

6. Minutes of a Meeting of ATCO’s Board of Directors of December 14, 2000 (Exhibit A-1, Tab 39) in relation to approving agreements affecting the plant by ATCO’s Board of Directors. Reference was made to the following:

> In principle, the parties have agreed to give the Balancing Pool administrative (BPA) and the consumers an irrevocable option to sell the H.R. Milner Plant.

This is, in effect, what happened. Although the phrase irrevocable option was used, in fact the beneficial interest is transferred to the Balancing Pool and the capital investment in the plant is paid to ATCO with legal title to remain in ATCO. This was expanded upon in more detail further in the recitals before the execution of the NSA by the officers of ATCO.

7. Paragraphs (1) and (2) of the recital in the Minutes of the Meeting of ATCO's Board of Directors of December 14, 2000 (Exhibit A-1, Tab 39) before the resolution by the Board authorizing the execution of the NSA and the OA reads in part as follows:

> WHEREAS the Board of Directors of ATCO Electric Ltd. passed a resolution December 14, 2000 authorizing ATCO Electric Ltd. To execute the following described agreements in connection with H.R. Milner Station ("Station"):
>
> (1) A Negotiated Settlement Agreement with the Balancing Pool Administrator (the "BPA"), for and on behalf of the Power Pool Council, and the major consumers groups of Alberta (collectively the "Consumers") whereby:
>
> (d) the PPA for the Station will terminate effective January 1, 2001;
> (e) the Balancing Pool will pay ATCO Electric Ltd. The net book value of the Station estimated at $62.7 million with the major payment of $59.7 million payable on January 2, 2001 with the balance of approximately $3.0 million for final adjustments, payable on January 31, 2001.
> (f) ATCO Electric Ltd. The Consumers and the BPA will endeavour to sell the Plant to a third party purchaser during the following described Term with the sale proceeds payable to the Balancing Pool failing with TCO Electric Ltd. Will have the option to decommission the Station or continue to operate it, as a merchant plant.
>
> (2) An Operating Agreement with the Purchasers wherein ATCO Electric will operate the Station on behalf of the Consumers and the BPA from January 1, 2001 for an initial term of 21 months ending September 30, 2002 which may be extended by the consumers and the BPA for a further 12 months.

This recital is consistent with what was negotiated and agreed to between the parties. Attached to these minutes was a statement as to the overall purpose and intent of the agreement and again, although some of the phrases are not the exact same wording as is in the agreements, the overall intent from the document taken with the other documents, could only lead one to believe that the payment to ATCO was not compensation for surrender of future profits.

[56] After the NSR and OA had been executed, a variety of what appears to be press releases or communiqués by the Balancing Pool were issued, none of which have any legal authority and all of which do not derogate or take away from the *viva voce* evidence or other supporting documentation which are clear, cogent evidence as to what was the true intent of the parties in terms of the commercial transaction. [The statement by the Balancing Pool in December, 2001 in relation to the sale of the plant (Exhibit A-1, Tab 12); an information brochure on the sale of the plant in May, 2001 (Exhibit A-1, Tab 14); an information release by the sales committee of the Balancing Pool of May 22, 2001 (Exhibit A-1, Tab 31); further information released by the sales committee of the Balancing Pool on February 28, 2003 (Exhibit A-1, Tab 32); an information release by the Balancing Pool in April, 2003 (Exhibit A-1, Tab 17)].

[57] The Balancing Pool had an annual meeting on April 29, 2004. In a presentation at the meeting, reference was made to the sale of the plant. (Exhibit A-1, Tab 16, page 11): “Over a 3 year operating period, BP received over $50 million in cash flow from plant operations to offset the payout to ATCO”. The reference to payout to ATCO only has the connotation which would be given to it based upon the intentions of the parties in concluding the commercial transaction already described.

[58] The Annual Reports of the Balancing Pool (Exhibit A-1, Tab 11) were all available to ATCO for the years 2000 to 2003, and there is nothing therein inconsistent with the intention of the parties in terms of what the $59.7 million payment was for, that is, compensation for capital investment as opposed to surrender of future profits. The financial statements are consistent with the position taken by the Appellant. For example, at Exhibit A-1, Tab 11, the Financial Statements at page 26 state:

> Thermal Generation Assets
> The balance relates to the power generating rights of the H.R. Milner Plant for the period January 1, 2001 to September 30, 2002 with a right of renewal for a further

> year. The purchase price also includes the estimated costs of decommissioning the plant at the end of the contract period.

This would lead one to believe, that, consistent with the intent of the parties, the Balancing Pool received all of the benefits of the plant post-January 1, 2001 including the right to sell the plant and reap the proceeds. In the Annual Report of the Balancing Pool 2003, (Exhibit A-1, Tab 8, page 12) under Property, Plant and Equipment, it states in part as follows:

> Throughout 2003, management actively sought a buyer for the H.R. Milner plant. This plant was purchased from ATCO Power Ltd. under the Negotiated Settlement Agreement signed in 2001 for cash of $62.7 million and the assumption of the reclamation and abandonment liability which was estimated at $13 million. The Balancing Pool fully depreciated the plant by September, 2003. A purchase and sale agreement was signed in October and the sale was finalized in early 2004. The operations of the plant are disclosed in discontinued operations.…

[59] In the same Annual Report, at page 24 of the financial statements, the Balancing Pool included the plant as follows:

> Thermal generation asset
> The thermal generation asset (H.R. Milner) is recorded in the accounts at cost less accumulated amortization. The asset was amortized in a straight-line basis over a 33 month period ending September 30, 2003. The asset was subsequently sold in 2004 and therefore is disclosed as a discontinued operation.

And finally, at the IPPSA Conference in March, 2003, widely attended by industry officials, in the Balancing Pool update presentation, the Balancing Pool was described as the beneficial owner of three thermal PPAs and the H.R. Milner plant.

[60] The sale of the plant to a third party was subject to an Asset Sale Agreement of October 30, 2003 in which the Appellant was described as vendor. The purchaser was a partnership and the Balancing Pool was also named as a party to the agreement. It is obvious from a review of the agreement that the Appellant, was named as Vendor because it was the Appellant that still retained legal title to the lands on which the plant was situate. It is also equally clear that the beneficial interest in the plant and all other aspects of the beneficial interest in the plant rested with the Balancing Pool. There would be no reason for the Balancing Pool to be a party to the agreement, unless they were owners of the beneficial interest of the plant as described in the NSA. The purchase proceeds on the closing went to the Balancing Pool, not the Vendor. The purchaser assumed the liabilities of the

Balancing Pool. The purchaser was agreeing to purchase and accept the assets from the Vendor and the Balancing Pool consented to the sale of the assets by the Vendor to the purchaser. This description of the transfer would have been used because the legal title rested with the Vendor while the beneficial interest rested with the Balancing Pool. This agreement of purchase and sale was consistent with the entire intent associated with the commercial transaction from the beginning. The key clauses in the purchase and sale agreement, including the purchase consideration, goods and services tax, liabilities and closing adjustments clearly show that the key parties to the agreement were the Balancing Pool and the Third Party. In fact, the Balancing Pool provided a separate indemnity to the Appellant at the same time as the Agreement of Purchase and Sale (Exhibit A-1, Tab 22). As indicated in the NSA and OA, the Balancing Pool wanted the Vendor to operate the plant so that they could provide due diligence to a prospective third party buyer. This is what occurred under the Agreement of Purchase and Sale whereby through the transition, between the Agreement of Purchase and Sale and the time of closing, the Vendor was to provide plant operational information to the Third Party. When one looks at the representations and warranties by the Vendor in the Agreement of Purchase and Sale, these representations and warranties, taken with the Indemnity Agreement provided at the same time by the Balancing Pool to the Appellant, show that the Appellant was simply the conduit for legal title in the plant to pass to a Third Party. Recitals in the Indemnification Agreement refer to the fact that the Appellant required on the sale of the plant, certain indemnifications and other provisions on the basis that the Appellant should not be left with any residual liabilities or obligations with respect to the plant and the licensed facilities after the sale of the plant for which they did not have a satisfactory indemnity or security from a third party purchaser of the plant and the licensed facilities.

[61] As noted, the lead argument of the Respondent was whether the monies received by ATCO was in compensation for a surrender of future profits or return of a capital investment and property. Key to this position was whether or not there was a beneficial ownership transfer of the plant to the Balancing Pool by the Appellant. The Respondent takes the position that it is all about statutory framework and intention and the way in which the agreements were made and were the work, while the Appellant states that the beneficial ownership of the plant went to the Balancing Pool.

[62] Nothing in the Act defines the concept of “beneficial ownership”. However, in *Williams v. R.*, 2005 CarswellNat 2316, 2005 TCC 558, [2005] 4 C.T.C. 2499 , 2005 D.T.C. 1228, 18 E.T.R. (3d) 239, a case regarding whether a taxable capital gain was

realized by the taxpayer when he transferred property to a trust of which he was a beneficiary, Woods J. of this Court stated the following regarding “beneficial ownership”:

> 32 The term "beneficial ownership" is not defined in the *Act* and, although much has been written about its meaning, there are surprisingly few judicial decisions that are of assistance. In accordance with well-known principles, the term "beneficial ownership" should be given its ordinary meaning consistent with the scheme of the *Act* (*Bell ExpressVu Ltd. Partnership v. Rex*, [2002] 2 S.C.R. 559 (S.C.C.)).
>
> . . .
>
> 38 The ordinary meaning of "beneficial ownership" as defined in the most recent edition of *Black's Law Dictionary* is extremely broad and supports the meaning suggested by the taxpayer. The relevant extracts are:
>
> > *Beneficial owner*. 1. One recognized in equity as the owner of something because use and title belong to that person, even though legal title may belong to someone else; esp., one for whom property is held in trust. [...]
> > *Beneficial ownership*. 1. A beneficiary's interest in trust property. [...]

[63] In *Matchwood Investments Ltd. v. R.*, 1998 CarswellNat 1486, [1998] 4 C.T.C. 2492, a case regarding a taxpayer who took a mortgage in order to claim a capital gains reserve but was subsequently found not to have obtained beneficial ownership of the property until the deed was registered, McArthur J. of this Court stated the following regarding was is a “beneficial owner”:

> 10 The Minister submits that the Appellant who was the mortgagee in possession in 1994 did not obtain beneficial ownership of the property until the execution and registration of the Quit Claim Deed to him in April 1995. In paragraph 12 of the Reply to the Notice of Appeal the Respondent uses the word "interest" rather than "ownership" as provided for in the Act. These reasons may be different if the word "interest" was correct. In this regard I refer to the definition of "beneficial interest" in the Mozley and Whiteleys Law Dictionary and to the Dictionary of Canadian Law, Carswell Second Edition. I will deal with the words "beneficial ownership". While the Appellant re-acquired possession of the property in 1994 it did not obtain title or ownership until 1995 when it was granted a Quit Claim Deed. It is unfortunate this Deed was not available to be placed in evidence. While it is agreed that it was registered in 1995 there was no evidence as to when it was executed, although it would appear that it was also executed in 1995. The Dictionary of Canadian Law, Second Edition defines "beneficial owner" in part:

> ... the real owner of the property even though it is in someone else's name they quote *Csak vs. Aumon (*1990) 69 DLR at 567 and at 570 Lane J. stated: 'A person who has the right to drill into a unit of minerals and produce therefrom oil and gas or potash ...'

[64] Again, in *Larose (M.) v. M.N.R.*, 1991 CarswellNat 730, [1992] 2 C.T.C. 2339, 92 D.T.C. 2055, [1992] 1 C.T.C. 2667, 92 D.T.C. 2045, where the taxpayer sold property but was found to not have relinquished beneficial ownership of the properties, Tremblay J. of this Court stated:

> 47 (…) Thus, the concepts of "legal ownership" and "beneficial ownership", need it be recalled, are not germane to the property rights regime contained in the Civil Code. (…) the English version of subsection 248(3) (paragraph 4.03.2) clearly establishes that the concept of "beneficial ownership" is closely bound up with the abusus held in respect of a property, which is to say the right to dispose of the property as the holder sees fit. The predominance of this attribute of ownership in terms of the definition of beneficial ownership is evident. A property is deemed to be beneficially owned when one person assesses the three attributes of the ownership of property (*usus*, *fructus*, *abusus*) or when a property is subject to a usufruct, an emphyteutic lease or a servitude.
>
> 48 In other words, the owner who possesses the three attributes of ownership (full owner), the bare owner in cases of the creation of a usufruct or emphyteutic lease, and the owner who agrees to encumber his property with a servitude are deemed to be the holders of the beneficial ownership of the property in question.

[65] The Appellant quite correctly states there is nothing in the "OA that says that the legal and beneficial ownership in the plant stays with ATCO. Article 9.2 of the OA states as follows:

> During the term, ATCO Electric shall have the legal title to the plant and licensed facilities subject to a beneficial interest in the plant and licensed facilities in favour of the power pool for the full benefit and advantage of the consumers.

[66] Article 9.2 of the OA recognizes that while ATCO may retain legal title, the beneficial interest passed to the Balancing Pool. Three reasons were given in evidence by Victor Post of ATCO as to why ATCO would retain legal title and not transfer the legal title at the same time as the beneficial interest to the Balancing Pool:

(a) Negotiations were rushed, and they were trying to get the transaction completed and as such they did not think there was time to transfer the title;

(b) They did not think there was time to transfer all the licenses and permits which would also be required if the legal title passed even though ATCO was to operate the plant under the OA; and

(c) There was some question as to whether or not the Balancing Pool could take legal title to the plant at the time.

[67] In *Her Majesty the Queen v. Prévost Car Inc*., 2009 FCA 57 (F.C.A.), the Federal Court of Appeal considered the meaning of beneficial interest in a tax treaty with the Netherlands. There was no definition of beneficial interest in the tax treaty. The Court noted that in searching for the meaning of the term, the trial judge examined the ordinary meaning, the technical meaning and the meaning that they might have in common law, Quebec civil law, Dutch law, and in international law, and relied *inter alia* on the OECD commentary for article 10(2) of the model convention and an OECD document that was issued subsequent to a 1977 commentary. The Court of Appeal stated at paragraph 13 and 14 in part as follows:

> [13] In the end the Judge determined, at par. 100 of his reasons, that "the "beneficial owner" of dividends is the person who receives the dividends for his or her own use and enjoyment and assumes the risk and control of the dividend he or she received". …
>
> [14] The Judge's formulation captures the essence of the concepts of "beneficial owner", "bénéficiaire effectif" as it emerges from the review of the general, technical and legal meanings of terms. Most importantly, perhaps, the formulation accords with what is stated in the OECB Commentaries and in the Conduit Companies Report.

[68] The Appellant listed a variety of factors or elements in the NSA and OA which show that the beneficial ownership of the plant passed to the Balancing Pool, including:

1. The Balancing Pool paid all costs and received all revenues from the operation of the plant;
2. The Balancing Pool paid for the insurance coverage of the plant;
3. The Balancing Pool made the operation and management decisions of the plant;
4. ATCO did not have a vote in the sales committee which oversaw the sales process and the operations of the plant;

5. On the expected sale of the plant, the Balancing Pool received all of the proceeds;
6. In the event that decommissioning of the plant became necessary or desirable the Balancing Pool was responsible for all decommissioning costs and mention of the OA would have been unnecessary given that it was not in accordance with commercial practice if ATCO had been made the beneficial owner; and
7. The parties specifically referred to the $59.7 million as proceeds of disposal of long term assets in Schedule G of the OA.

[69] At the end of the day, what ATCO had left was really the fees to operate the plant pursuant to the OA and if it was not sold and did not operate on its own, it would decommission the plant at its own cost. All the benefits, and all the burdens that arise from the ownership rested throughout, from January 1, 2001 onward with the Balancing Pool. The Balancing Pool had all the decision making power with respect to all operations of the plant, how it was to be operated, what expenditures were to be made, what the output was going to be, to whom and when it was going to be sold, and what the selling price would be to a third party. There were certainly some clauses in the agreement of sale with the third party which tied in the Appellant, but that was because a) the Appellant was still the legal title holder of the plant and b) the Appellant operated the plant to and for the benefit of the Balancing Pool The conduct of the parties throughout also show that the beneficial owner of the plant was the Balancing Pool. The Balancing Pool even showed the plant as an asset in its financial statements, treating it differently than it did PPAs.

[70] The Respondent takes a very different approach with respect to beneficial interest.

[71] The Respondent first of all states that the general law does not support the transfer of beneficial ownership to the Respondent by the Appellant, with the Appellant retaining legal title. There was no reference to any law to support this proposition. I think it all goes back on to what was the original intent of the parties and the original intent of the parties clearly shows, as by the documentation, as to who was going to hold legal title and who was going to have the beneficial interest. This is consistent with the *viva voce* evidence and very consistent as explained, with all the documentation which was executed at the time, that is the NSA and the OA and the subsequent documentation including e-mails, et cetera, developed in the course of negotiations and thereafter explaining the status of the property over

a period of time until sold to a Third Party under an Agreement of Purchase and Sale. The Respondent referred to paragraphs 7 through 14 of the Respondent's written representations but I do not believe that the authorities referred to by the Respondent support the position of the Respondent. For example, reference is made to "Kathy Brown, Symposium, Beneficial Ownership and Income Tax Act" where it is thought, the authorities indicate, that the determination of the beneficial ownership of the property is one which requires the presence of indicia of a sufficient transfer of possession, risk and use, such that it can be truly said that someone is a beneficial owner by virtue of being one recognized in equity as the owner of something because use and title belong to that person even though legal title may belong to someone else. Reference was also made to *Csak v. Aumon*, 69 D.L.R. (4th) 567 at 570 where the Ontario Supreme Court stated in part as follows:

> … A beneficial owner is one who is the real owner of property even though it is in someone else's name. The minimal owner has legal title to the property but the real owner can require the nominal owner to convey the property to him and transfer legal title to him. …

[72] These references fit specifically in the circumstances with which we are concerned in this case.

1. Legal title rests with ATCO.
2. The Balancing Pool received what was described as the beneficial interest;
3. In receiving the beneficial interest, the Balancing Pool received all the right, interests, benefits and liabilities that went with the plant;
4. The Balancing Pool received the proceeds of the sale of the property;
5. The Balancing Pool controlled the direction, the use, the operation and management of the property, in all aspects.
6. The Appellant had nothing to do with the plant once it received the $59.7 million from the Balancing Pool other than to operate the plant at the direction of the Balancing Pool per the OA.
7. Given the facts, it can only be said that the real owner of the plant at the relevant time was the Balancing Pool and this is consistent with the authorities referred to by the Respondent.

[73] The Respondent also takes the position that the statutory framework, the *Act*, does not allow the transfer of such assets to the Balancing Pool. The Respondent asserts that the new de-regulation regime did not encompass a transfer of ownership of the plants to the Balancing Pool, and that the intent was to separate

generation, transmission and distribution in the *Electric Utilities Act*. The Respondent was correct in the assertion that the general overall intent was for the Balancing Pool to facilitate a short term transition from 1996 to 2020, to take the industry from regulation to de-regulation. The PPAs were done initially to deal with the transfer of output of existing generation units to the Balancing Pool if not sold otherwise. The Balancing Pool would then deal with the output of the plants on the basis of recovery of the so-called stranded cost of each unit. Stranded costs were the original cost minus claimed depreciation at that point in time and basically that was the amount that was paid here - the net book value. Here there was no sale of the PPA for the plant therefore the Balancing Pool became the counter party on behalf of consumers and negotiated the NSA and OA with ATCO for the recovery by ATCO of basically the stranded costs.

[74] What occurred in this case, however, was a one-off situation, that is an anomaly in terms of deregulation in Alberta. The PPA for the plant was put in place but it was such that it did not make the plant economically viable. If Alberta wanted this plant to continue to generate power in the short term, it had to accommodate the concerns of ATCO who were otherwise going to decommission the plant. The Respondent referred to a variety of language in the preambles in the plant PPA. This language is really irrelevant, because it was in existence well before the NSA and OA. The whole commercial arrangement between ATCO, the Appellant and the Balancing Pool was to avoid the implementation and reliance upon the PPA, for the reasons already described.

[75] The Respondent reviewed in detail a variety of Regulations related to deregulation of the electric energy sector in Alberta. In argument the Respondent stated, in effect, that the whole matter comes down to whether or not the Balancing Pool had the authority, the ability and the mandate to accept any beneficial interest in the plant. The Respondent asserts that the Balancing Pool did not have in its own mandate, power and authority to accept a beneficial interest in the plant, even if it wanted to. In other words, you cannot sell or buy what you do not have the capacity to sell or buy. I am in agreement that the Balancing Pool, through the Balancing Pool Administrator, must act in accordance with its statutory/regulatory mandate with the powers and rights in respect to all its transactions.

[76] The Balancing Pool was established, in Regulation 169/99 and its specific authorities, duties and powers are provided in section 4 thereof (see paragraph 38 hereof). These powers were, however, expanded by Regulation 331/2000. Article 2 of that Regulation states as follows:

> 1. The balancing pool administrator has the power to carry out any duty or function described in the negotiated settlement agreement as a duty or function of the balancing pool administrator.
>
> 2. The balancing pool administrator must make the payments and carry out the other obligations described in the negotiated agreement as being the obligations of the balancing pool administrator.

I believe that this particular regulation (331/2000) expands the power of the Balancing Pool to be able to carry out all those duties and functions necessary to give effect to the intent, and spirit, of the NSA. As noted earlier, incorporated by specific reference in the NSA was the OA. The OA specifically states that legal title of the property remains with ATCO while the beneficial interest of the property is transferred to the Balancing Pool. This was the spirit and intent of the commercial arrangement between the two. Given the intent was basically dictated, in whole or in part, by a government authority that is the Balancing Pool, and given that the Lieutenant Governor in Council of the Province of Alberta enacted Regulation 331/2000, and given the fact that Alberta is the entity which established the Balancing Pool in the first place, under the *Electric Utilities Act*, I believe the Balancing Pool had all the appropriate powers, mandates, rights and privileges it required to carry out the mandate which was dictated to it when it was initially established, and as expanded by Regulation 331/2000 and within the statutory/regulatory framework, certainly had the authority, power and capacity to receive the beneficial interest of the plant in question.

[77] One issue which arose in the course of argument by the Respondent was whether the subsequent regulation, that is, Regulation 331/00 can be such as to expand upon the powers given the Balancing Pool by prior regulation without a repeal of the prior regulation.

[78] Ruth Sullivan in *Statutory Interpretation*[1] states that once legislation is enacted, it continues to form part of the law until it expires or is repealed. Therefore, regulations are presumed to be valid unless shown to be invalid. Repeal occurs when a law declares another law to be invalid.

[79] If several regulations are enacted, then they must not be interpreted as repealing each other (unless the new regulations specifically state so). Instead, new

[1] Ruth Sullivan, *Statutory Interpretation* (2nd ed.), Irwin Law, 2007, p. 22

regulations must be read to render a previously enacted regulation inoperative in case there is any conflict[2]:

> Since a legislature cannot bind its successors, in the event of a conflict between two provisions, the more recent expression of the legislature's will prevails over the earlier one. Implied repeal is sometimes considered a method of actual repeal rather than a rule of paramountcy. It is certainly possible to analyze it this way: by enacting a provision that is inconsistent with the existing legislation, a legislature impliedly expresses an intention to repeal the existing law and replace it with something else.
>
> (…) In Canada, however, we have a well-established convention of explicit formal repeal. When a legislature wants to introduce new law, it actively reviews the existing statute book and prepares an express repeal of each provision that is judged to be inconsistent with the new law. If anything is overlooked by the legislature at this point, it is likely to be noticed and corrected in the next statute revision. Given these practices, it is better to treat implied repeal as a rule of paramountcy rather than a method of repeal. On this approach, a subsequently enacted provision renders a previously enacted provision inoperative to the extent of any conflict. However, the inoperative provision remains valid law and will become applicable again if for any reason the conflict disappears.

[80] Therefore, in order for the regulation to give the Balancing Pool the power to hold and be beneficial owner of the plant, prior regulations do not have to be repealed since the newest regulations must be read as trumping the prior ones.

[81] Based on this analysis, the Regulations seem to give the Balancing Pool the authority to hold the plant in light of the NSA and the OA. Section 2 of the *Alberta Regulation*[3] provides:

> **2. (1)** The balancing pool administrator has the power to carry out any duty or function described in the negotiated settlement agreement as a duty or function of the balancing pool administrator.
>
> **(2)** The balancing pool administrator must make the payments and carry out the other obligations described in the negotiated settlement agreement as being obligations of the balancing pool administrator.

[82] The Balancing Pool is a party to the NSA, which gives the Balancing Pool the power to hold the Plant:

> 4. Conditions Precedent

[2] Ruth Sullivan, *Statutory Interpretation* (2nd ed.), Irwin Law, 2007, p. 311
[3] Alberta Regulation 331/2000, Alberta Gazette, Part II, January 15, 2001

a) This Agreement and the Parties' obligations hereunder shall be subject to:

i) the making of regulations effective and in force January 1, 2001 which: provide for the termination of the PPA; allow the BPA to execute this Agreement for and on behalf of the Power Pool Council and allow the BPA to exercise such rights and authorities and assume such obligations and liabilities as given to or imposed upon it for and on behalf of the Power Pool Council pursuant to this Agreement, and allow the payments contemplated by this Agreement to be made out of the Balancing Pool in accordance with the terms of this Agreement; and

ii) The obligations of the BPA hereunder are subject to the satisfaction of the conditions contained in section 10.16 of the Operating Agreement.

b) These conditions precedent may not be waived by any Party.

[83] The OA specifically provides that the Balancing Pool shall acquire beneficial interest:

9.2. Beneficial Interest

During the Term, ATCO Electric shall have legal title to the Plant and Licensed Facilities subject to a beneficial interest in the Plant and Licensed Facilities in favour of the Power Pool for the full benefit and advantage of the Consumers.

[84] The OA also provides that the Pool shall have authority to acquire such an interest, according to the provincial legislation:

10.6. Governing Law

This Agreement shall be governed by and construed in accordance with the laws of the Province of Alberta and the Parties submit to the jurisdiction of the Courts in the Province of Alberta.

[85] The NSA and the OA give the Pool authority to acquire an interest in the Plant as per the authority granted to it by the provincial legislation. The legislation (and associated regulations) does grant the Balancing Pool authority to acquire an interest in the Plant. In addition, previous regulations need not be repealed in order to grant such authority. Therefore, the Balancing Pool does have the power to hold and be beneficial owner of the plant.

[86] The third reason given by the Respondent for the suggestion that the beneficial ownership did not transfer to the Balancing Pool from the Appellant was that the variety of agreements (NSA, OA and Third Party Agreement of Purchase and Sale) in place between ATCO, the Appellants and the Balancing Pool, do not support this assertion. The Respondent suggests that the agreements show that ATCO retains incidents of ownership. I have reviewed the agreements in detail, in particular the NSA, the OA and the third party agreement of purchase and sale and the specific clauses or phrases referred to therein by the Respondent in support for the proposition that there was not a beneficial ownership transfer to the Balancing Pool by the Appellant. What seems to be lost upon the Respondent is the fact that in order to determine what the nature of the commercial transaction was in the case at hand, one has to look at the intent of the parties and the intent of the parties is drawn from a) the activities which occurred before the agreements were signed, that is, the negotiations; b) the actual agreements themselves; c) the subsequent course of conduct of the parties and any collateral information or events which took place to reinforce or help the parties carry out their intent. As I indicated earlier, there is no question in my mind about what the intent of the parties was in this overall commercial transaction. When one looks at the course of negotiations, the documents produced with respect to same; the evidence of the negotiating parties which has not been rebutted or contradicted; the position of Alberta, and how it enacted regulations to facilitate the agreements which were entered into between the parties; the NSA, OA and the Agreement of Purchase and Sale with a Third Party, I do not believe I could reach any other reasonable conclusion other than the transaction was as I described. The events after the execution of the NSA and the termination of the PPA leads me to conclude that the essence of the commercial arrangement was as follows:

1. Alberta wanted to move from a regulated to a de-regulated energy generation industry;
2. To facilitate the non-regulation of the electrical energy industry in relation to those plants which are built pre-1995, PPAs were to be placed upon the owners of electro-generation plants to ensure the continued operation during the de-regulation phase.
3. PPA for the plant was such that the plant could likely not be operated on a economical basis and would likely end up losing money because of its history of using a poor quality coal supply resulting in ATCO’s decision to decommission the plant.
4. ATCO entered into negotiations with Alberta, for the purpose of decommissioning the plant, but Alberta wanted to keep the plant open and therefore caused the Balancing Pool to enter into negotiations

with ATCO, on behalf of consumers, to ensure that the plant was operated on a short term basis (two to three years) to allow ATCO to recover its capital investment in the plant.

5. The NSA was concluded after negotiations between two separate parties with separate interests, which provided *inter alia* (via the OA) that: (1) the legal title of the plant would remain with ATCO; (2) the beneficial interest in the plant would be transferred to the Balancing Pool; (3) the Balancing Pool would pay ATCO $59.7 million which was the net book value of the assets of the plant; (4) ATCO would enter into an OA with the Balancing Pool to operate the plant, for and on behalf of the Balancing Pool, and under the direction and control of the Balancing Pool at all times for a certain period of time and after the completion of this period of time, if the plant was not sold to a third party, ATCO could decommission the plant within one year and decommissioning costs would be paid for by the Balancing Pool, or it could continue to operate the plant after the termination of the one year, in which circumstance, it would be responsible for the decommissioning costs.
6. When the plant was sold by the Balancing Pool to the Third Party, all of the purchase price proceeds, would go to the Balancing Pool and ATCO would provide the Third Party, on behalf of the Balancing Pool, with information which the Third Party would require for the continued operation of the plant, including, helping the Third Party carry out its due diligence, because it had operated the plant from the time of the transfer of all beneficial interest, save the legal title, to the Balancing Pool.

[87] These are, in essence, the key points in the commercial transaction as between ATCO and the Balancing Pool. There is no question that one can read one particular clause or phrase, in the agreements in isolation which might lead one to some sort of belief that the compensation paid to ATCO was other than for a return of the capital investment, but when you review the entire evidence, in particular the negotiations between the parties, and the documentation which supports the negotiations, the only conclusion I can reach and I do reach and find as a fact, is that the commercial arrangement between the parties was, as stated aforesaid.

[88] The final suggestion by the Respondent that the beneficial ownership was not transferred to the Balancing Pool, was based upon published reports after the NSA and OA were executed. These reports do not, in my view, support such a view.

[89] The Respondent acknowledged that the wording in these reports were at best, ambiguous and it shows some confusion or lack of decision as to what was being described. In the course of examination of Mr. Post, the Respondent made references to December 14, 2000 Board of Directors of ATCO's meeting minutes, numerous information brochures and statements by the Balancing Pool, the Balancing Pool annual meeting report of April 29, 2001, the annual reports of the Balancing Pool for 2000 and 2003. These documents themselves were not the documents which were founding documents of the commercial arrangement between the parties. The information brochures and statements by the Balancing Pools, were basically public relation documents prepared, presumably, by someone in the public relations department of the Balancing Pool and would not necessarily use the legal wording reflected in the agreements. None of the phrases or wording in the documents indicate in any manner whatsoever that the compensation received by ATCO from the Balancing Pool was for a surrender of future profits. I see nothing prejudicial in these documents to the position taken by the Appellant, and in fact, in some of the documents there is wording which is consistent with the position taken by the Appellant. For example, in the Balancing Pool's Annual Report of 2003, it was stated in part under Property, Plant and Equipment:

> … throughout 2003, management actively sought a buyer for the H.R. Milner Plant. This plant was purchased from ATCO Power Ltd. Under a negotiated settlement agreement signed in 2001 for cash of 62.7 million and the assumption of the reclamation and abandonment liability which was estimated at 13 million. The balancing pool fully depreciated the plant by September 2003. A purchase and sale agreement was signed in October and the sale was finalized in early 2004. …

This is a more complete characterization of the deal than possibly other descriptions presented by the Respondent. At page 24 of the same report, the Plant was reported by the Balancing Pool as an asset at cost less accumulated amortization. At a public conference where a presentation was made by the Balancing Pool in March, 2003, the Balancing Pool was described as the beneficial owner of the plant.

[90] I find that the information in the published reports post-transaction is not inconsistent, with the intent of the parties in relation to the commercial transaction.

[91] Having reviewed all of the evidence adduced, paying particular attention to the documentation produced in relation to the negotiations between ATCO and the Balancing Pool, and to the *viva voce* evidence of both Mr. Post and Mr.

Hildebrand, being the persons who negotiated the agreements, having reviewed the agreements, the NSA, the OA and the third party agreement and the explanations provided in the evidence presented with respect to same, I find that the intent of the parties was to enter into a commercial transaction as described herein and, more specifically, that the intent of the parties was for a payment by the Balancing Pool to the Appellant of $59.7 million as compensation for the capital investment of the Appellant in the plant in question, and not as payment for loss of surrender of future profits.

Issue No. 2

If the payment was not income received under section 9 of the *Act*, was the payment a compulsory payment under subparagraph 12(1)(*x*)(iv) of the *Act*?

[92] Paragraph 22 of Amended Reply states as follows:

> 22. In the alternative, he states that the B.P. was required to compensation ATCO when the Milner Plant PPA was terminated, pursuant to the provisions of Regulation 170/99; 106/2000; and 331/2000. As such, the amount of $59 M constitute a compulsory payment that is taxable under paragraph 12(l)(*x*)(iv) of the *Act*, and is properly included in the Appellant's income in the 2001 taxation year in that ATCO received the $59 M from a public authority as reimbursement for an amount that was included in the cost of property, or an outlay or expense, that was the Milner Plant and related properties.

[93] The Appellant asserts that the damage payments or settlement payments are not reimbursements under subparagraph 12(1)(*x*)(iv). They refer to *Westcoast Energy Inc. v. Her Majesty the Queen*, 91 D.T.C. 5330 (F.C.T.D.). In that case a lawsuit was instituted by a taxpayer for the purpose of putting it in the same position as if a party who had been retained to construct a pipeline had built the pipeline according to the original contract specifications. The action was for damages, the object of which was to give the taxpayer compensation for the damages or losses it had suffered and therefore the amount received by the taxpayer was a settlement which constituted damages and did not form or fall within the ordinary meaning of the word "reimbursement" contained in paragraph 12(1)(*x*) of the *Act* and thus was not required to be included in computing the taxpayer's income. At page 5341 the Denault, J. stated in part as follows:

> … It is my conclusion that reimbursement does not include damage awards. It is not based on the evidence to say that the plaintiff received a reimbursement as

> defined in paragraph 12(1(x). The ordinary and legal meaning of the word does not contemplate an award of damages. …
>
> (emphasis added)

This decision was upheld in *Her Majesty the Queen v. Westcoast Energy Inc.*, 92 D.T.C. 6253 when the Federal Court of Appeal stated, in part, as follows:

> We are in agreement with the interpretation the learned trial Judge has placed in the term reimbursement in paragraph 12(1)(*x*)(iv) of the *Income Tax Act* …

In the case before the Court, we have settlement payments from the Balancing Pool to the Appellant for the capital investment not reimbursement they had in the plant upon termination of the determination of the PPA and, in effect, removing the plant from the possession and ownership of the Appellant.

[94] It was argued that paragraph 12(1)(*x*) of the *Act* deals with a situation where a party has already received funds into income because they have already expended them. In the facts before the Court, ATCO was never forced to pay an amount that was someone else's liability in any manner. *In Canada Safeway v. Her Majesty the Queen*, 98 D.T.C. 6060 (F.C.A.), the Federal Court of Appeal at page 6303 said, in considering the meaning of the word "reimbursement":

> It is apparent from the decision of Denault, J. in *Westcoast Energy Inc. v. Her Majesty the Queen* that the term as used in paragraph 12(1)(*x*)(iv) is limited by the context of that provision. In that case, the Court found that it does not include the compensation received by a taxpayer for the damage or loss it had suffered. The case makes it clear, contrary to what the Appellant argues, that it is not every payment or repayment that can and will qualify as a reimbursement within the terms of subparagraph 12(1)(*x*)(iv).
>
> In addition, Denault, J. reviewed the Parliamentary debates surrounding the enactment of that provision, examples of reimbursement in different legal relationships as well as the situation that the provision intended to remedy:
>
> > Examples of the word reimbursement in different legal relationships were cited. First, there is a compulsory payment. This is a situation where a person has been compelled by law to pay and pays money for which another is ultimately liable. The Payer can make a claim for reimbursement from the latter individual. …

What is contemplated is a situation where one party is forced to pay an amount that is properly the liability of another party and is therefore entitled to be reimbursed

the funds from the second party. This is not the case before the Court. ATCO was never compelled by law to pay any money to anyone, and therefore never has had any right to be reimbursed with respect to any monies it was compelled to pay. ATCO was being paid the $59.7 million, not as a compulsory payment but as part of a NSA between two competing interests.

[95] According to Stikeman's *Canada Tax Service*[4], the purpose of paragraph 12(1)(*x*) is to bring into income all amounts received by a taxpayer in the course of earning income from a business or property as an inducement to do something.

[96] According to the *Canadian Encyclopedic Digest*[5], damages received by the taxpayer may be on account of income or capital. According to the surrogatum principle, the characterization of damages is determined by the character of the item for which the compensation is intended to substitute. For example, compensation received for loss of profit from non-performance of business contracts is characterized as a receipt of income. Compensation for loss of capital property, goodwill, or a source of business is generally on account of capital. The situation was the same for reimbursements under common law until paragraph 12(1)(*x*) was introduced in 1985. Paragraph 12(1)(*x*) requires that all reimbursements, inducements, grants and subsidies received in respect of the acquisition of an asset or the incurring of a deductible expense be included in income unless the amount ahs already reduced the cost of the property or the amount of the expense. Paragraph 12(1)(*x*) was introduced to clarify the tax treatment of tenant inducements which in some cases the courts had considered to be tax-free.

[97] The Department of Finance's Technical Notes (November 2006) state that paragraph 12(1)(*x*) provides that certain inducements, reimbursements, contributions, allowances and assistance received by a taxpayer in the course of earning income from a business or property must be included in income "to the extent that" the particular amounts have not otherwise been included in income or reduced the cost of a property or the amount of an outlay or expense.

[98] In the present case, it is clear that the payment was not for any type of reimbursement or funding. The payment was for the sale of the Plant itself. If such a payment was to be included in 12(1)(*x*), then every sale of assets would also have to be included under this provision. Based on the Department of Finance's technical comments, above, this was clearly not the Minister's intention.

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[4] Stikeman, *Canada Tax Service, Volume 2*, Section 12(1)(x), Carswell, 2009
[5] *Canadian Encyclopedic Digest (Ontario), Third Ed.* Volume 15A, Title 76, Para 553, Carswell, 2009

[99] Paragraph 12(1)(*x*) of the *Act* was not enacted, in my view, for circumstances where someone has a legal obligation to make a payment, if the legal obligation arises from the course of legitimate negotiation. If that was the case, then any amount paid pursuant to any negotiations, for the purpose of settling any disputes regardless of their nature, would be awards obligated by law, to be included as income under paragraph 12(1)(*x*).

[100] Finally, even if the $59.7 million was described in subparagraph 12(1)(*x*)(iv), the application of paragraph 12(1)(*x*) would be excluded by the application of paragraphs 12(1)(*v*) and 12(1)(*viii*) which ensure that the amounts can be taxed under paragraph 12(1)(*x*) only. To the extent that the particular amount in 12(1)(*v*) was not otherwise included in computing the taxpayer's income or deducted in computing, for the purpose of this *Act*, any balance of undeducted outlays, expenses or other amounts for the year or a preceding taxation year, or (*viii*) may not reasonably be considered to be a payment made in respect of the acquisition by the payor or the public authority of an interest in the taxpayer or the taxpayer's business or property.

[101] The Appellant asserts is that all they have to establish here is an "interest" and "in respect of" and suggests these are very wide words. Also, the phrase "may not reasonably consider" was considered in *Canada Trustco v. The Queen*, 2005 SCC 54. After consideration of the words "may reasonable consider" the Supreme Court of Canada concluded that a taxpayer failed to meet a "may not reasonably be considered" threshold only where the opposite conclusion … cannot reasonably be entertained.

[102] Given the wording in the pre-sale documents, the course of negotiations; the evidence of the negotiating parties in the course of negotiations; the actual wording in the NSA and the OA, the sale agreement to the third party, and the fact that the proceeds of the sale to the third party were going to the Balancing Pool, all would lead one to conclude that an interest in the plant may reasonably be considered to have passed to the Balancing Pool.

[103] The Respondent takes the position that the Balancing Pool had not acquired any interest in the property and if they did acquire an interest in the property the exclusion of the inclusion does not apply, because according to *CCLC Technologies Inc. v. Her Majesty the Queen,* 96 D.T.C. 6527, the rights must be lasting property rights in order to be exempt from the inclusion.

[104] I disagree with this proposition. The Appellant did hold some security, some interest in the property, even if just for a short period of time. ATCO held the plant for a different purpose and for a different period of time. Also, *CCLC Technologies Inc*. case precedes *Canada Trustco* and the test set down there as to what was meant by "may reasonably be considered" considering the section 85 rollover which resulted in the Appellant being the vendor.

[105] I conclude that paragraph 12(1)(*x*) of the *Act* does not apply as the monies paid by the Balancing Pool to the Appellant, were not a reimbursement under paragraph 12(1)(*x*) and I do not believe that this paragraph deals with the situation, because neither ATCO nor the Appellant was ever forced to pay an amount that was somebody else's liability. Further, the amount here was removed from ATCO's CCA pool and therefore paragraphs 12(1)(*v*) and 12(1)(*viii*) takes it out of play. Also, I find that *CCLC Technologies* case does not apply to the case before the Court.

Issue No. 3

If the $59.7 million is a receipt under section 9 of the *Act*, under what year is the amount taxable, 2000 or 2001?

[106] Based upon my conclusions with respect to the issues, it is not necessary for me to consider what year the 59.7 million is to be considered as income to the Appellant.

[107] In summary:

The answer to Issue No. 1 is the lump sum payment of $59.7 million paid by the Balancing Pool to the Appellant was a capital receipt and not an income receipt under section 9 of the *Act*.

The answer to Issue No. 2 is the lump sum payment was not a compulsory payment under subparagraph 12(1)(*x*)(iv) of the *Act*.

Having answered Issues No. 1 and 2 in the manner answered, I need not and will not deal with Issue No. 3.

[108] The appeal is allowed, with costs awarded to the Appellant.

Signed at Ottawa, Canada, this 21st day of August, 2009.

"E.P. Rossiter"

Rossiter A.C.J.

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