Bloomberg Tax

Tax Management
International Journal™

'Cameco': Canadian Counterpart of 'E.I. Du Pont de Nemours'

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INTRODUCTION

A recent Canadian transfer pricing case, *Cameco Corporation v. the Queen*,[1] involving a Canadian parent and a Swiss-based distributor and trading subsidiary, brings to mind U.S.-based E.I. Du Pont de Nemours' losing battle with the IRS some 40 years ago over the prices it had charged a Swiss-based distributor subsidiary.[2] But unlike Du Pont, the Canadian Cameco (uranium) group prevailed in opposing government claims. The Tax Court of Canada, in a decision handed down September 26, 2018, rejected a nearly half-billion Canadian-dollar transfer pricing-related income adjustment the Canadian government sought for the 2003, 2005, and 2006 taxation years, based on the alternate grounds that the Swiss subsidiary was a sham and/or the arrangements triggered a specific transfer pricing transaction substitution rule[3] and/or the prices used for the intercompany transactions did not meet an arm's-length standard.[4]

This commentary will attempt to briefly highlight the significant aspects of this 293-page judgment and the bewildering array and blizzard of virtually endless facts, assertions, and opinions of the parties and the court that involved over 70 days of court hearings and testimony of countless persons, including several experts for the parties. And apart from the appeal of this judgment noted in the concluding comments, there are similar issues outstanding for several other years between the parties that bring the overall dispute to more than Can$2 billion of tax.

BACKGROUND

Cameco was privatized in 1987 by the Saskatchewan government to mine for and deal in uranium. Twelve years later it established a Swiss subsidiary and one in Luxembourg with a Swiss branch, which it subsequently transferred to the Swiss subsidiary to market the group's uranium production in Canada and the United States and to buy and sell third-party uranium. The structure, operations, and pricing arrangements and tax issues are examined in the next three sections.

STRUCTURE, OPERATIONS, AND ASSERTION OF SHAM

The government's basic view was quite simple. The Swiss subsidiary, referred to in the judgment as CEL or CESA or CESA/CEL, was a facade (para. 602) and an illusion (paras. 578 and 602) and the overall arrangement was a sham, so the profits of the Swiss subsidiary belong to the parent. This raises two interrelated questions: what is a sham in Canadian law, and do the facts comprising the structure and operations show there was or there was not a sham?

Justice Owen canvassed all the case law on sham, showing it variously has been said to be or described as or referred to as:

- "acts done or documents executed by the parties to the sham which are intended by them to give

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[1] 2018 TCC 195.

[2] *E. I. Du Pont de Nemours and Co. v. United States*, 221 Ct. Cl. 333 (1979).

[3] *Income Tax Act* (of Canada) ("*ITA*"), §247(2)(b), (d), detailed below.

[4] *ITA*, §247(2)(a), (c).

to third parties or to the court appearance of creating between the parties legal rights and obligations different from the actual legal rights and obligations (if any) which the parties intend to create.''[5]

- a situation where ''all the parties thereto must have a common intention that the acts or documents are not to create the legal rights and obligations which they give the appearance of creating'' (also from *Snook*).
- ''a transaction conducted with an element of deceit so as to create an illusion calculated to lead the tax collector away from the taxpayer with the true nature of the transaction, or, simple deception whereby the taxpayer creates a facade of reality quite different from the disguised reality.''[6]
- a transaction ''that does not have the legal consequences that it purports on its face to have''(also in *Stubart*).
- ''For a sham to exist, the taxpayers must have acted in such a way as to deceive the tax authority as to their real legal relationships. The taxpayer creates an appearance that does not conform to reality of the situation.''[7]
- a sham ''requires an element of deceit which generally manifests by a misrepresentation by the parties of the actual transaction taking place between them.''[8]
- ''It suffices that parties to a transaction present it as being different from what they know it to be.''[9]
- a sham gives a ''false impression of the rights and obligations created'' (also in *Antle*).

Justice Owen sums up as follows in paragraph 592:

> It can be seen from the foregoing authorities that a transaction is a sham when the parties to the transaction present the legal rights and obligations of the parties to the transaction in a manner that does not reflect the legal rights and obligations if any, that the parties intend to create. To be a sham, the factual presentation of the rights and obligations of the parties to the sham must be different from what the parties know those legal rights and obligations, if any, to be. The deceit is factual representation of the existence of legal rights when the parties know these legal rights either do not exist or are different from the presentation thereof.

And in paragraph 597: ''Accordingly, for a transaction to be a sham, the facts (assumed or proven) must establish that the parties to the transaction *presented their legal rights and obligations differently from what they know those legal rights, if any, to be*'' (emphasis added). Does it all come down to those 18 italicized words? In fact in the summation on sham in paragraph 670 (discussed below), Justice Owen relied upon them — the parties ''did not factually represent the numerous legal arrangements that they entered into in a manner different from what they knew those arrangements to be, nor did they factually represent the transactions created by those arrangements in a manner different from what they knew those arrangements to be.''

Now just what were the arrangements and transactions that the court said were not presented in a manner intended to be seen differently from what the parties intended them to be? This section deals with the arrangements (structure and operations), and the next two deal with the transactions (intercompany sale of product and sale to third parties). In arriving at his conclusion in paragraph 670 that ''the element of deceit required to find sham is simply not present'' and that therefore the arrangements were not, as the government contended, a facade or illusion, Justice Owen focused *inter alia* on the following key facts.

The Luxembourg and Swiss subsidiaries were properly constituted, with fully functioning boards of directors (para. 607),[10] and were expressly authorized by both the Swiss and European nuclear regulatory authorities to engage in the uranium industry (para. 608),[11] and each had at least one senior employee with extensive experience in the uranium industry as well as ''the assistance of a third party service provider'' (para. 609) and services provided under contract by Cameco (paras. 611 *et seq*.).[12] With respect to the *bona fides* of the individuals involved and their ac-

[5] The classic British case, *Snook v. West Riding Investments Ltd.*, [1967] 1 All E.R. 528.

[6] Canadian Supreme Court in *Stubart Investments Ltd. v. the Queen*, [1984] 1 S.C.R. 536.

[7] *Faraggi v. the Queen*, 2007 TCC 286.

[8] FCA in *Faraggi*, 2008 FCA 398.

[9] *Antle v. the Queen*, 2010 FCA 280.

[10] The *location* of that activity is, separately, fundamental to establishing, under Canadian case law, the place of residence of a corporation.

[11] In this respect, Justice Owen stated in paragraph 608 that ''it is beyond belief that this regulatory authority would authorize what the Respondent (the government) in substance alleges are fictitious transactions.''

[12] The role of service provider to augment employees in running a business — whether related or not — was accepted by the Supreme Court in the seminal case of *Stubart Investments Ltd. v. the Queen*, [1984] 1 S.C.R. 536, where the taxpayer transferred a profitable business to a related loss corporation but continued to run it under a service contract. But even years earlier, in *E.S.G. Holdings Ltd. v. the Queen,* 76 DTC 6158 (FCA), the courts ac-

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tivities, two paragraphs in the judgment appear particularly persuasive:

> [621] The uncontradicted evidence of Mr. Assie, Mr. Glattes and Mr. Murphy is that the terms of all contracts relevant to the Appellant, Cameco US and CESA/CEL were discussed and agreed to during the sales meetings held twice-weekly, or more frequently if the circumstances warranted. Mr. Wilyman and Mr. Mayers testified that discussions regarding the uranium market and potential sales to third parties did take place during the sales meetings and that Mr. Glattes and Mr. Murphy participated in those discussions. The terms of the sales to third parties in turn determined the terms of the back-to-back contracts between Cameco US and CESA/CEL.
>
> [622] Mr. Glattes and Mr. Murphy were both experienced participants in the uranium industry and in my view clearly had the knowledge and experience to understand and participate in the sales meetings, and to meaningfully contribute to those meetings. Mr. Newton, in cross-examination, spoke in glowing terms of Mr. Glattes' expertise and experience in the uranium industry, as did other witnesses. Even without such testimony, Mr. Glattes' résumé and years of experience speak for themselves. Mr. Murphy, for his part, had extensive relevant experience with the Cameco Group before he became the president of CEL. My clear impression of Mr. Glattes and Mr. Murphy is that they are both strong personalities and experts in the Uranium business carried on my (*sic*) the Cameco Group and that they would not and did not act as mere figureheads who simply followed the explicit directions of the Appellant.

The court also notes, at paragraph 121, the taxpayer's testimony respecting the choice of Switzerland:

> When it comes to Switzerland and uranium there are nuclear reactors in the country. It has a nuclear regulatory regime if you will. It is a western country. It's easy to get in and out of. It has laws that are established. It is a place that people do business. It fits and as I say compared to other jurisdictions in the world which may have many of the same things but do not have the nuclear history associated with it.

At paragraph 625, the court rejected the government's argument that sham could be seen in the facts that ''the Appellant continued to play an important role in the gathering of market intelligence and the administration of the various contracts entered into by CESA/CEL and because the decision making by CESA/CEL, the Appellant and Cameco US was collaborative rather than adversarial (and therefore) the overall arrangement was a deliberate deception of the Minister because the Appellant was doing everything'' in the following words:

> However there was nothing unusual about the way in which the Cameco Group operated. Carol Hanson (the taxpayer's expert witness on corporate governance) opined that it is common in an MNE such as the Cameco Group for administrative functions to be centralized and shared across the enterprise and that commercial integration across the MNE and the accountability of the parent company to investors and regulators requires cooperation and coordination across the entities forming the MNE.

Similarly, the court invokes the *Stubart* case (referred to in footnote 12 above) in rejecting the government's contention in paragraph 629 ''that little changed following the reorganization and that that supports a finding of sham'':

> In *Stubart* the taxpayer transferred its food production business to a related corporation that had losses'' (Grover). The taxpayer and Grover executed an agency agreement pursuant to which the taxpayer continued to carry on the transferred business for the benefit of Grover. In effect, nothing changed except the beneficial ownership of the transferred business, which, after the transactions, rested with Grover. The Supreme Court of Canada held that such an arrangement was not a sham because there was no false representation of the arrangements.

The manner in which the court rejected the government's contention that sham could be seen in some sloppy execution of certain arrangements (respecting five sales contracts by CESA/CEL out of 210 between March 1999 and the end of 2006) is also noteworthy (at para. 643): ''It defies logic and common sense to suggest that the relatively minor issues with these few contracts, establishes the existence of a sham from 1999 to 2006.''

The court also rejected the notion that sham should be seen in negotiating assistance provided to the

knowledged that a corporation can be said to carry on an active business (in that case for the purpose of qualifying for a low rate of tax applicable to private Canadian corporations not controlled by non-residents or public corporations) even though it has no employees and is run under service contracts by related parties. And the very same notion (running a business through a service contract with a related corporation that employs more than five full-time employees in running the business) is statutorily embedded in an exception to an element (''investment business'') of Canada's counterpart to U.S. ''Subpart F'' income, namely ''foreign accrual property income'' that may be attributed to a Canadian shareholder of a non-resident corporation.

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Swiss subsidiary by Cameco with respect to third-party uranium supply contracts. At paragraph 665: ‘‘Sham is focused on the existence of deception in the description of the legal rights and obligations of parties to arrangements, not on who negotiated the agreements creating those arrangements.’’

Finally the government sought to rely, in its sham argument, on a case, *Dominion Bridge Co. v. Canada*,[13] that treated an offshore subsidiary (Span) that purchased foreign-made steel and resold it at a markup to its Canadian parent, as an agent of its parent. Justice Owen rejected this on the basis that Dominion Bridge found agency not sham, and that subsequent case law makes the decision ‘‘of dubious relevance today’’ (para. 668). And at paragraph 669:

> even if *Dominion Bridge* is still good law in Canada, the factual circumstances found to exist in that case bear no resemblance to CESA/CEL’s and the Appellant’s factual circumstances. Span was literally an empty shell corporation, and its parent corporation, which was its only client, directed, controlled and carried out all its activities.

In light of the foregoing, it is not difficult to see how Justice Owen arrived at the following conclusion on sham at paragraph 670:

> In summary, I find as a fact that the Appellant, Cameco US and CESA/CEL did not factually represent the numerous legal arrangements that they entered into in a manner different from what they knew those arrangements to be, nor did they factually represent the transactions created by those arrangements in a manner different from what they knew those arrangements to be, consequently, the element of deceit required to find sham is simply not present.

TRANSFER PRICE-RELATED TRANSACTION SUBSTITUTION RULE

As noted above the government’s second line of attack was that a transfer price-related transaction substitution rule applied so that it could effectively reallocate all the Swiss subsidiary’s profits to the Canadian parent. The third line of attack, dealt with in the next section, is based on the straightforward arm’s-length pricing rule. For purposes of considering both sets of rules, the court categorized all the transactions as follows, at paragraph 709:

> Consistent with my interpretation of subsection 247(2), I have identified the following transactions or series of transactions:
>
> 1. The series of transactions comprised of the incorporation of CESA, the decision by the Appellant to designate CESA as the Cameco Group signatory to the HEU Feed Agreement, CESA’s execution of the HEU Feed Agreement and the Appellant’s guarantee with respect to CESA’s obligations under the HEU Feed Agreement (the ‘‘Tenex Series’’).[14]
>
> 2. The series of transactions comprised of the incorporation of CESA, the decision by the Appellant to designate CESA as the Cameco Group signatory to the Urenco Agreement, CESA’s execution of the Urenco Agreement and the Appellant’s guarantee with respect to CESA’s obligations under the Urenco Agreement (the ‘‘Urenco Series’’).[15]
>
> 3. The transactions consisting of the Appellant and CESA/CEL entering into the BPCs and the Appellant delivering uranium to CESA/CEL under the BPCs (the ‘‘BPC Transactions’’). In identifying each sale under the BPCs as a separate transaction, I am cognizant of the fact that I could classify the Appellant’s deliveries of uranium under each BPC as a series of transactions. However, I have concluded that the most effective way to test these deliveries against the arm’s length principle is to address each delivery separately. In my view, identifying each delivery as a separate transaction does not preclude an analysis of the terms and conditions of the BPCs having regard to all deliveries contemplated by those contracts since, in conducting any transfer pricing analysis, all the relevant circumstances must be considered.
>
> 4. The transactions consisting of the Appellant and CESA/CEL entering into the CC Contracts and CESA/CEL delivering uranium to the Appellant under the CC Contracts (the ‘‘CC Transactions’’).
>
> [710] I will refer to the Tenex Series and the Urenco Series, collectively, as the ‘‘Series’’ and to the BPC Transactions and the CC Transactions collectively as the ‘‘Transactions.’’[16]

[13] [1975] F.C.J. No. 316 (QL) (FCTD).

[14] This saw CESA buy uranium from third parties and resell to other third parties.

[15] Same as the Tenex Series.

[16] The taxpayer contended (see paragraph 711) that the first category were ‘‘events without tax attributes and therefore cannot be subject to the transfer pricing rules.’’ The court rejected that in paragraph 712 and found the rules can apply to the Tenex Series and the Urenco Series.

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The transfer price-related transaction substitution rule, added to the *Income Tax Act* in 1998 and inspired by the 1995 OECD Guidelines,[17] reads as follows:

> (2) **Transfer pricing adjustment —** Where a taxpayer or a partnership and a non-resident person with whom the taxpayer or the partnership, or a member of the partnership, does not deal at arm's length (or a partnership of which the non-resident person is a member and participants in a transaction or a series of transactions and
>
> [. . .]
>
> (b) the transaction or series
>
> (i) would not have been entered into between persons dealing at arm's length, and
>
> (ii) can reasonably be considered not to have been entered into primarily for *bona fide* purposes other than to obtain a tax benefit,
>
> any amounts that, but for this section and section 245, would be determined for the purposes of this Act in respect of the taxpayer or the partnership for a taxation year of fiscal period shall be adjusted (in this section referred to as ''an adjustment'') to the quantum or nature of the amounts that would have been determined if,
>
> [. . .]
>
> (d) where paragraph (b) applies, the transaction or series entered into between the participants had been the transaction or series that would have been entered into between persons dealing at arm's length, under terms and conditions that would have been made between persons dealing at arm's length.[18]

Although a different issue, it is apparent that in light of the manner in which Justice Owen came to his findings respecting the sham argument, the court would not have much difficulty in finding that the transactions would have been entered into by arm's-length persons so as to render this rule inapplicable — and it did not have much difficulty. That determination involved a two-step process. First the court found that the way in which to assess whether arm's-length parties would enter into a transaction (in this case, particularly, the Transactions — the category three and four transactions between Cameco and CESA/CEL above) is to determine if they were commercially rational. That is the criteria. Second, the court found that all four categories met that test and therefore §247(2)(b) and (d) had no application. Finally, although it was unnecessary in light of his finding on §247(2)(b)(i), Justice Owen expressed the view that the series arrangements were primarily tax driven within the meaning of §247(2)(b)(ii). But that alone was insufficient to trigger §247(2)(d).

As to the first step, what is the criteria, Justice Owen, clearly relying on and referring to paragraph 1.37 of the 1995 OECD Transfer pricing guidelines and paragraph 1.65 of the 2010 Guidelines, states unequivocally and at the onset that:

> [714] In my view, subparagraph 247(2)(b)(i) is not asking the Court to speculate as to what arm's length persons might or might not have done in the circumstances. Rather, the subparagraph is asking whether the transaction or series under scrutiny would have been entered into by arm's length persons acting in a commercially rational manner. The focus of the test is the commercial rationality (or irrationality) of the transaction or series, taking into consideration all relevant circumstances. The determination of whether a transaction or a series is commercially rational requires an objective assessment of the transaction or series, and that assessment may be aided by expert opinion.
>
> [715] If a transaction or series is commercially rational then it is reasonable to assume that arm's length persons would enter into the transaction or

[17] See text below.

[18] The court rightly emphasizes, at paragraphs 696 et seq., that contrary to prevalent inaccurate discussion, this (§247(2)(b) and (d)) is quite different from a transaction ''recharacterization'' rule. Justice Owen refers to the government identifying ''an alternative transaction or series'' and notes in paragraph 697 that the OECD distinguished between ''the recharacterization of a transaction and the use of an alternatively structured transaction as a comparable uncontrolled transaction'' and that only the latter approach is taken in §247(2)(d). That choice is explained in great detail by one of the chief draftsmen of the rule, Brian Bloom, in *Paragraph 247(2)(b) Demystified*, 1783 Tax Topics (CCH) 1-5 (May 11, 2006), who refers to ''re-constituting,'' ''substituting,'' or ''ignoring'' transactions which are *both* commercially irrational *and* ''have been structured in this commercially irrational manner in order to impede tax authorities' ability to determine an arm's-length price under 'normal' transfer pricing rules or to achieve some other tax benefit for the tested party.'' Bloom also points out the OECD examples and the difference between transaction recharacterization and transaction modification. The former would see a loan to an affiliated party that has substantial features of equity being recharacterized as equity with the effect of the denying interest deductions. The latter would see a current sale of future (developed) intangibles for a lump sum payment which is considered to be irrational being recast as a license of the future intangibles for commensurate royalty type payments. Bloom summarized the OECD-suggested approach to the matter as follows: ''If the transfer of [rights to such future] property is to be respected, but it is not rational to set a fixed price therefor currently, absent (knowledge of futures related developments), then it follows that arm's length parties would probably have agreed to the payment of a royalty by the transferee based on future revenues generated by the transferee from the resulting future property's exploitation.''.

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> series. The fact that the transaction or series is uncommon or even unique does not alter this assumption. If a transaction or series is not commercially rational then it is reasonable to assume that arm's length persons would not enter into the transaction or series.

The court then examines each of the four categories of transactions, under this test, and concludes that none were commercially irrational. In so doing the court made several interesting comments.

With respect to the first two categories (the "Series"), Justice Owen linked several factors. After citing, with apparent approval, (in paragraph 722) the U.S. Tax Court decision in *Merck & Co.*[19] that "a U.S. parent of a corporate group is free to establish subsidiaries and to decide which among its subsidiaries will earn income and that the mere power to do so cannot justify reallocating the income earned by that subsidiary" and indicating that "implicit in [that] view is that the behaviour of the parent corporation in establishing subsidiaries and placing business opportunities in those subsidiaries is not commercially irrational" and then stating that "I would go so far as to suggest that such behaviour is a core function of the parent of a multinational enterprise," Justice Owen infers a relationship (in paras. 723–725) thereof to the role of the Canada's foreign affiliate system in allowing "Canadian multinationals to compete in international markets through foreign subsidiaries without attracting Canadian income tax" (para. 725).[20] That leads him to state (in para. 725) that "[t]he tax plan conceived and implemented by the Appellant sought to take advantage of the foreign affiliate regime by having a contract with an arm's length non-resident person (Tenex) executed by a controlled foreign affiliate of the Appellant." The judge wraps this all up in paragraphs 726 and 730 as follows:

> There is nothing exceptional, unusual or inappropriate about the Appellant's decision to incorporate CESA and have CESA execute the HEU Feed Agreement. To the extent that the Appellant's implementation of the decision raises transfer pricing concerns, paragraphs 247(2)(a) and (c) address those concerns. The application of the extraordinary remedy in paragraphs 247(2)(b) and (d) is neither warranted nor appropriate in the circumstances.
>
> In light of the foregoing, I conclude that the Tenex Series is not described in subparagraph 247(2)(b)(i). The same analysis and conclusion applies to the Urenco Series.

With respect to category three, the long-term sale contracts from parent to the Swiss subsidiary, the court did not have much trouble, after examining the key contractual terms and industry norms and context and after noting (in paragraph 736) that the government's own expert witnesses "do not suggest that the Appellant's decision to sell its uncommitted uranium production to CESA/CEL was commercially irrational," coming to the following conclusion (in para. 737): "On the basis of the foregoing, I conclude that the BPC Transactions are not described in subparagraph 247(2)(b)(i)."

As far as the fourth category, the CC transactions comprising sales by the Swiss subsidiary to its parent, apart from the fact that any profit therefrom would have been deemed to be attributable passive income[21] the court (in paragraph 738) summarily dismissed any suggestion that they were commercially irrational.

Finally on §247(2)(b), as already noted Justice Owen did not have to comment but he did on the second branch of that rule — whether the Swiss subsidiary structure was primarily tax motivated. Of interest in his mixed conclusion – the first two categories (the "Series") were primarily tax motivated but the other two (the "Transactions") were not — was the statement in paragraph 742, that reads as follows:

> My finding that the principal purpose of the Tenex Series and the Urenco Series was to save tax must not to be taken as a condemnation of the Appellant's behaviour. For the reasons described above, any tax savings realized by the Appellant resulted from the application of the foreign affiliate regime in the ITA. In taking advantage of the foreign affiliate regime, the Appellant was simply utilizing a tax planning tool provided by Parliament. The foreign affiliate regime has clearly defined boundaries, as evidenced by the fact that CESA/CEL's income from selling uranium to the Appellant was subject to current taxation in Canada.

WERE THE PRICES ARM'S LENGTH?

Finally we come to the place where transfer pricing cases usually start (and end). Were the prices charged by Cameco to the Swiss subsidiary under the long-term contracts (the BPCs) for Cameco's uncommitted uranium production arm's-length prices? (There was also pricing of the service contracts and whether a fee

[19] *Merck & Co v. United States*, 24 Cl. Ct. 73.

[20] Under Canada's "foreign affiliate" system, Canadian MNEs are not taxed on earning business profits through foreign subsidiaries, nor on their distribution where tax treaty or TIEA jurisdictions are involved.

[21] *See* ¶742. This is a statutory rule (§95(2)(a.1) of the *Act*), comparable to the U.S. Subpart F foreign base company sales income rule.

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should have been charged for providing the Tenex and Urenco contracts — pricing for the inbound sales was irrelevant because of the deemed passive income rule.)

The short answer is that Justice Owen found that all the prices and all the other terms and conditions met the requirement of §247(2)(a) of being ''those that would have been made between persons dealing at arm's length.'' How he arrived at that conclusion can only be seen by considering more closely the law, a maze of facts, conflicting expert witness testimony, and intricate and nuanced analysis and findings by the court. The following deals with only some of the highlights of those elements.

On the law there are no statutory rules or statutorily mandated regulations to give meaning to §247(2)(a). There are non-binding views of the Canada Revenue Agency[22] that advocate reliance on the OECD transfer pricing guidelines, but where Justice Owen notes (in para. 745) they have been described by the Supreme Court in *GlaxoSmithKline*[23] as not governing like a Canadian statute. But yet they are dealt with throughout as if they were, particularly by the chief expert witnesses for both parties, U.S. transfer pricing economists: Deloris Wright for the government and Thomas Horst for the taxpayer.

In his testimony on behalf of the taxpayer, Horst opined that the prices charged by Cameco to the Swiss subsidiary could be supported by prices from comparable uncontrolled transactions (i.e., comparable uncontrolled prices (CUPs)) and offered 10 different CUPs in the context of a multi-phase analysis. He also tested his results with the resale method.

Wright, however, disagreed, in part because the CUPs were not of public record, and testified that a method that measures the Swiss subsidiaries' functions performed and management of risks but that does not focus on property ownership or risk of loss is more appropriate. Depending upon the extent of function performance, that would be the retail sales method or the transactional net margin method.[24] Note that the focus on functions, not ownership and risk bearing, by the government and CRA officials was heavily criticized by two other taxpayer experts, Alan Shapiro and Atulya Sarin,[25] and rightly so.[26]

Another government witness, Anthony Barbera, advocated a cost plus method, an approach normally associated with contract, not proprietary, manufacturers or commodity service providers but not with distributors.

In that context, what do we see in Justice Owen's analysis that runs 30 pages?

In paragraph 753, Justice Owen stated:

> With respect to the Series (i.e., the category one and two events above) the question to be addressed is whether arm's length persons in the same circumstances would have attributed value to the business opportunities. With respect to the Transactions, the question to be addressed is whether the pricing of the Transactions reflected arm's length pricing, having regard to all the circumstances and to objective benchmarks.

In paragraphs 754 and 755 the court notes Horst's reliance on the methods endorsed in the 1995 Guidelines — his selection of the CUP method and his effort to ''eliminate the effect of the differences between the Transactions and the comparable uncontrolled transactions'' that he had identified, as well as (in para. 756) that the ''proposed amendments following the completion of the OECD/G20 Base Erosion and

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[22] There is an Information Circular, IC 87-2R, and a series of transfer pricing memorandums.

[23] *Canada v. GlaxoSmithKline*, 2012 SCC 52 [2012] 3 S.C.R. 3.

[24] That reflected that paragraph 537 notes that Wright was asked by the government to assume three different factual scenarios: Cel performed no functions relevant to its purchase and sale of uranium, it performed some, or it performed all.

[25] They wrote, for example, in paragraph 455 as follows: ''Thus, to argue, as the CRA does, that the provision of administrative services to investors like CEL who supply risk capital is the equivalent of bearing the risks that capital is subject to is to denigrate the role of risk bearing while putting the engagement in routine functions on a pedestal. Simply put, it places the dinnerware on par with the meal.'' And they wrote in paragraph 456 as follows: ''In the case of CEL and CCO, the CRA believes that CCO monitored and managed CEL's price risk through Contract Administration, General Administrative, and Market Forecasting and Research Services, and that this means that CEL could not have borne the price risk. Even if the CRA's assertion that CCO monitored and managed CEL's price risk is true, this is irrelevant to the question as to who bore the price risk. The CRA confuses risk monitoring with risk-bearing. If an investor hires a broker who recommends stocks based on research performed by the broker's company, the investor is still the one who gains (or loses) if the stock price rises (or falls). The performance of brokerage functions does not shift investment risk from the investor to the broker. Similarly, an investor may buy gold from a company that also provides gold transfer and storage, but this logistics support does not shift investment risk, the investor still bears the risk. Likewise, a financial advisor may monitor and track the risk in an investment portfolio and prepare investment statements, but this does not change the fact that the investor bears the risk of the portfolio's investments rising or falling in value.''

[26] This is reminiscent of the OECD BEPS ''cash box'' initiative in actions 8–10 that wrongly would appropriate the profit of the property owner and award it to the property manager. It has been argued (see Nathan Boidman and Michael Kandev, *The OECD's Cash-Box Notion Is 'Fundamentally Flawed,' Writers Say*, Tax Notes Int'l (Aug. 15, 2016), and *BEPS Cash Box Inconsistent with all Canadian Tax Rules*, Canadian Tax Highlights, Vol. 24, No. 10 (Oct. 2016)) that the invalidity can be seen by considering that the world's greatest private equity managers get no more than a 20% ''carry.''

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Profit Shifting Project recognize the general appropriateness of using the CUP methodology to price commodities.''

Justice Owen appears to accept the latter and did so in part because he found (at para. 758) that the government's witnesses ''did not undertake the transfer pricing analysis required'' and ''their expert evidence is to a significant degree based on hindsight and on assumptions regarding the subjective views of the Appellant and Tenex at the time the relevant transactions occurred rather than on objective benchmarks as required by the traditional transfer pricing rules'' and (at para. 760) that they failed ''to address the legal substance of the Series and the Transactions'' but tried ''to fit the Series and the Transactions into a paradigm that ignores the economic reality of the actual legal arrangements.'' It would appear that underlying, at least in part, the latter concerns and others expressed by the court is one that is basic and expressed by Justice Owen in Paragraph 764 in the following words: ''I have therefore concluded that Doctor Barbera's opinions are in substance addressing the Respondent's position under paragraphs 247(2)(b) and (d) and not the factual issues raised by paragraphs 247(2)(a) and (c).''

In that respect Justice Owen then wrote in paragraph 765:

> Doctor Wright performed an analysis of various hypothetical scenarios involving the performance of various functions, but did not provide any transfer prices as such. Again, the hypothetical scenarios appear to be in support of the Respondent's position under paragraphs 247(2)(b) and (d).

Further support for Horst's position is found in the court's acceptance of a Horst's assertion that the cost plus method Dr. Barbera sought to use was ''in substance a CUP analysis'' (para. 813) but where the data he used did not provide comparability. As well the court found Barbera's alternate RPM analysis defective because, *inter alia*, it was based on the incorrect assumption ''that the contracts between CESA/CEL and Cameco US are in effect back-to-back with the purchases from the Appellant under the BPCs and thus place CESA/CEL in the same position vis-a-vis risk as a routine of a routine distributor'' (para. 819). But in fact, while Cameco US took a fixed small spread (when it purchased from the Swiss subsidiary and resold to the market), the Swiss subsidiary took the risk of a downturn in the market.

Separately the court accorded considerable analysis to and then rejected the government's assertion that Wright's analysis supported ''the position that the profit earned by CESA/CEL from the HEU Feed Agreement and from the BPCs should be attributed to the Appellant because the Appellant performed all the critical functions that earned the profit'' (para. 825). That of course is like double dipping as we have already seen above (in the discussion of sham) support for using service providers to run one's business and the reference above to the case of *Stubart* and of *ESG* — which is cited at this juncture in footnote 862 of the judgment. That point is affirmed by Justice Owen in paragraph 833 in the following words: ''As stated earlier, the law in Canada has long been that there is no distinction between a corporation carrying on an activity by using its own employees and a corporation carrying on an activity by using Independent contractors.''

But more fundamentally, the court rejects the inane notion that all or most profit should be allocated to the manager of property instead of to the owner who bears the risk of loss in the value of the property (see paras. 835 and 839). See discussion in notes 25 and 26.

At paragraph 841 et seq., Justice Owen revisits Horst's ''rigorous transfer pricing analysis'' and his use of ''three iterations of a CUP analysis'' and the backup RPM check, and Owen concludes at paragraph 848 that Horst's work ''provide(s) the most reliable and objectively reasonable assessment of those prices.''[27]

Justice Owen then reinforces those comments by specifically rejecting the government witnesses' criticisms of Horst's comparables as being based on conclusions as to relevant economic circumstances that were based on ''speculation as to the motivations'' of certain criteria relevant players in the industry (para. 849) and based on a faulty view of the effect of different markets and regions.

Finally the court Justice Owen rejects the contention that continual losses that Cameco showed meant the prices were suspect, with the comment in paragraph 854 that he has ''not been convinced that the Appellant knew or could have predicted with any degree of certainty that it would incur losses because of the BPCs.''

Justice Owen then sums up the main issue as follows, at paragraph 856:

> In conclusion, I accept the results of Doctor Horst's third CUP analysis as reflecting a reasonable assessment of the terms and conditions that arm's length parties would have reached in the same circumstances. The result of Doctor Horst's transfer pricing analysis is that the prices charged by the Appellant to CESA/CEL for uranium delivered in the

[27] Interestingly, paragraphs 844 and 845 reveal that Horst recommended certain income increases amounting to around Can$1.3 million and decreases amounting to Can$9 million.

ISSN 0090-4600

Taxation Years were well within an arm's length range of prices and that consequently no transfer pricing adjustment was warranted for the Taxation Years.

As to the category one and two items (the Series) and whether the Swiss subsidiary should have paid anything to Cameco for putting it into those third-party contracts, Justice Owen concluded in paragraph 788, with respect to the Tenex Series, and in paragraph 803, with respect to the Urenco Series, that there was ''no evidence warranting an adjustment.'' The reasons for this include the following.

The government argued that Cameco had positioned itself to enter into two profitable purchase (of uranium) contracts and that it would be consistent with arm's-length dealings for it be compensated when it assigned these opportunities to its Swiss subsidiary. The court, however, concurred with Horst's testimony — which was buttressed by Shapiro and Sarin — that there did not appear to be a likelihood of superprofits, tending therefore to negate the government's position. Furthermore, there was evidence that Cameco's interest in the contracts ''was the desire to control the sale of HEU feed to avoid it being dumped on the market thereby depressing the market price of uranium'' (para. 775) and not because these contracts would bring an economic windfall. Therefore in light of those and other evidence Justice Owen concluded in paragraph 786 that ''the economic benefits of participating in the HEU Feed Agreement was negligible at the time the parties executed the agreement in March 1999.''

That focused on the Tenex Series. Paragraph 789 indicates that although there were differences, the analysis of the Urenco Series was similar.

CONCLUDING COMMENT

That concludes this brief review of this massive 293-page judgment, and I leave it to the Federal Court of Appeal — to which an appeal was filed recently[28] — to wrestle further with this magnum opus. In the meantime, Justice Owen is to be commended for his tenacity and skill of keeping the massive array of facts, with which he was confronted and which he analyses and discusses, in a semblance of order.

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[28] On October 25, 2018, the Government filed an appeal to the Federal Court of Appeal seeking a reversal of the Tax Court's decision on the following grounds: 1. The Trial Judge erred in fact and in law in concluding that paragraphs 247(2)(b) and (d) of the *Act* did not apply. 2. The Trial Judge erred in fact and in law in concluding that paragraphs 247(2)(a) and(c) of the *Act* did not apply. 3. The Trial Judge erred in fact and in law by failing to properly apply the arm's-length standard as required by section 247 of the *Act*.

ISSN 0090-4600