

Docket: 2012-481(GST)G

BETWEEN:

SUN LIFE ASSURANCE COMPANY OF CANADA,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on September 22, 2014, at Toronto, Ontario

Before: The Honourable Justice John R. Owen

Appearances:

Counsel for the Appellant: Justin Kutyan
Vern Vipul
Counsel for the Respondent: Khashayar Haghgouyan

JUDGMENT

The appeal from a reassessment made under the *Excise Tax Act* for the reporting period from January 1, 2006 to December 31, 2006 by notice number 071310187229G0002 dated May 1, 2009 is allowed, with costs to the Appellant, and the reassessment is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that Sun Life is entitled to additional input tax credits of \$1,279,180.49.

Signed at Ottawa, Canada, this 16th day of February 2015.

“J.R. Owen”

Owen J.

Citation: 2015 TCC 37
Date: 20150216
Docket: 2012-481(GST)G

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REASONS FOR JUDGMENT

Owen J.

I. Introduction

[1] This is an appeal by Sun Life Assurance Company of Canada (“Sun Life”) from a reassessment by notice number 071310187229G0002 dated May 1, 2009, issued under the *Excise Tax Act* (the “ETA”) for the reporting period of January 1, 2006 to December 31, 2006. The reassessment denied Sun Life’s claim for certain input tax credits (ITCs) in the amounts of \$1,279,180.49, \$53,700.33 and \$2,954.43. Sun Life objected to and then appealed the denial of the first amount of \$1,279,180.49 but did not object to or appeal the denial of the other two amounts. Accordingly, only Sun Life’s claim for ITCs in the aggregate of \$1,279,180.49 is in issue in this appeal. According to the Amended Reply to the Amended Notice of Appeal (the “Reply”), the \$1,279,180.49 comprises the following amounts: (i) ITCs of \$398,411.58 claimed for the reporting period ending December 31, 2006; (ii) ITCs of \$484,020.97 claimed by retroactive adjustment for the reporting period ending December 31, 2005; and (iii) ITCs of \$396,747.96 claimed by retroactive adjustment for the reporting period ending December 31, 2004.¹

II. Facts

¹ I note that these three numbers add up to \$1,279,180.51, so there is a very small rounding error.

[2] Sun Life called as a witness Mr. Stéphane Coutu. Mr. Coutu is a CA and a CPA and holds the office of Assistant Vice-President of Indirect Tax and Transfer Pricing at Sun Life. The Respondent called as a witness Mr. Gilles Lazure. Mr. Lazure is employed by the Agence du Revenu du Québec (the “Quebec Revenue Agency” or “Revenu Québec”) and has been responsible for auditing insurance companies since 1985. The Quebec Revenue Agency is responsible for administering the federal GST in the province of Québec. The parties also introduced into evidence a joint book of documents consisting of nine tabs and marked as Exhibit A-1 (the “Joint Book”).

[3] Sun Life is a corporation incorporated under the laws of Canada that operates as an insurance company. Sun Life sells a range of financial products and services that are primarily insurance-based but that also include wealth management products, such as investments and retirement products (collectively, the “Financial Products”). The Financial Products are sold through many different channels, including through independent contractors called sales advisers (“Advisers”). The sale of Sun Life’s Financial Products is considered to be the supply of a financial service that is an exempt supply by virtue of Part VII of Schedule V to the ETA.

[4] Sun Life maintains financial centres across Canada which focus on the sale of Financial Products. The financial centres house both employees of Sun Life and Advisers. The space occupied by the financial centres is leased from third party landlords and Sun Life pays GST on the rent it pays for each financial centre as well as on any leasehold expenditures associated with the financial centre.

[5] The rent paid by Sun Life to the third party landlords varies from location to location but is generally composed of a base rent, an additional rent and, in some cases, other charges. The base rent is stated as a dollar amount per square foot per annum. The additional rent is made up of Sun Life’s share of expenses incurred by the landlord, namely, building operating costs, property taxes, janitorial services, electricity costs, heating costs, air conditioning costs and such other costs as may be agreed. The amount of additional rent can be stated as a dollar amount per square foot per annum.

[6] A sample lease at Tab 7 of the Joint Book describes a lease of space in Brossard, Quebec consisting of 8,855 usable square feet and Sun Life’s share of common areas of 1,328 square feet, for a total area under lease of 10,183 square feet. The rent charged is composed of base rent of \$11.75 per square foot per annum and additional rent estimated to be approximately \$10 per square foot per

annum. The base rent and estimated additional rent are applied to the total area of 10,183 square feet to determine the amount payable by Sun Life. The lease has an addendum that increases the total leased space to 12,454 square feet, extends the term of the lease by three years and increases the base rent to \$12.15 per square foot per annum. No estimate is given for additional rent, but Sun Life's share of the landlord's costs that is incorporated into additional rent is stated to be 17.79 percent of those costs.

[7] A chart at paragraph 32. h) of the Reply, with which Mr. Coutu agreed, summarizes the information regarding the total space rented by Sun Life for financial centres (collectively, the "Leased Space") and the GST paid on the rent for the Leased Space, as follows:

	Space Rented by the Appellant (Square feet)	GST Paid by the Appellant
2004	742,298	\$1,298,125
2005	714,674	\$1,485,882
2006	712,789	\$1,303,551

[8] The Advisers are entitled to rent space in the financial centres from Sun Life but are not obligated to do so. Sun Life estimates that approximately 50% of the Advisers do rent space and that the space rented by the Advisers typically ranges from 100 to 140 square feet.

[9] The rental arrangement is implemented through a sublease agreement between the Adviser and either Sun Life or a predecessor of Sun Life. The financial terms of the sublease are set out in an e-mail to the Adviser, which is referenced in the body of the sublease agreement. Generally, the rent is calculated as the area of the Adviser's office in square feet times a monthly rate per square foot plus GST. The Adviser is also subject to a monthly charge for the telephone and ethernet connection in the rented office. In cross-examination, Mr. Coutu acknowledged that, although the Adviser was renting a specific office within the financial centre, under the sublease the Adviser would have full access to the financial centre and the building common areas and would access the financial centre through the same entrance as the employees of Sun Life.

[10] Tab 8 of the Joint Book contains a copy of a sublease agreement for an Adviser's office in the Brossard financial centre comprising 123 square feet leased at a rate of \$2.66 per square foot per month or \$31.92 per square foot per annum plus applicable tax. Mr. Coutu testified that the difference between the rate charged

to the Adviser of approximately \$32 per square foot per annum and the rate paid by Sun Life of approximately \$23 per square foot per annum reflected Sun Life's attempt to recover the effective cost of the office from the Adviser. Mr. Coutu also testified that if there was any discount in the rental charged to the Adviser as compared to Sun Life's effective cost of the office, it was minimal. In cross-examination, Mr. Coutu explained that the situation described in paragraph 20 of the Amended Notice of Appeal, which states that the consideration payable by Advisers to Sun Life was less than the consideration payable by Sun Life to its landlords, reflected the fact that Sun Life may not achieve full recovery of the effective cost of the space rented to Advisers but that "significantly all" of that cost is recovered.²

[11] A chart at paragraph 32. p) of the Reply, with which Mr. Coutu agreed, summarizes the information regarding the space rented by the Advisers in each year, as follows:

	Space Subleased by the Appellant to the Advisers (Square feet)	GST charged by the Appellant
2004	210,008	\$338,994
2005	207,804	\$351,605
2006	194,381	\$316,218

[12] Each financial centre houses one or more employees of Sun Life who are charged with the supervision of the financial centre and the providing of support for the Advisers. The task of recruiting Advisers falls on these employees and, as there is a high turnover of Advisers, a large portion of these employees' role is to recruit and support new Advisers. According to Mr. Coutu, the focus is always on the recruitment of Advisers, not on the renting of space to the Advisers.

[13] Mr. Coutu testified that Sun Life's model targets a ratio in each financial centre of one employee of Sun Life to eight Advisers. This ratio dictates the amount of space at each financial centre that is considered by Sun Life to be available to Advisers. On average, a portion of the space allocated to Advisers is vacant. A chart at paragraph 32. r) of the Reply, with which Mr. Coutu agreed, summarizes the information regarding the amount of vacant space in each year as follows:

² Transcript at pages 50 to 51.

	Vacant Office Space (Square feet)
2004	83,566
2005	82,924
2006	81,932

[14] Mr. Coutu testified that the vacant office space varies from financial centre to financial centre and represents space that is kept available for new Advisers who choose to rent space from Sun Life, so that the financial centres have the capacity to grow. The variability of the vacancy rate from financial centre to financial centre during 2004, 2005 and 2006 is shown in three charts at Tabs 1, 2 and 3 of the Joint Book under the column titled “Vacant Space As a % of Total Area under Lease”.

[15] In cross-examination, Mr. Coutu conceded that the vacancy rate could be as high as 50% if measured as a percentage of the area available for rent to Advisers instead of the total area under lease. Mr. Coutu further stated that the vacant space would not be rented to someone who was not an Adviser but that a vacant office could be used by an employee of Sun Life, at which point it would no longer be considered Adviser space. If the area of a financial centre is determined to be too large for Sun Life’s needs, the excess space may be returned to the landlord or it may be physically segregated and subleased. Mr. Coutu did not know whether this had occurred during the periods in issue.

[16] In filing its GST returns for the reporting periods from January 1, 2004 to December 31, 2004 and from January 1, 2005 to December 31, 2005, Sun Life claimed ITCs in respect of the space sublet to Advisers in an amount equal to the GST collected from the Advisers on the rent charged to the Advisers for space in the financial centres. Mr. Coutu explained that Sun Life did not have the information needed to claim higher ITCs and that using the GST collected was a “good floor” on which to claim some ITCs.³ Sun Life subsequently revised its ITC claim for 2004 and 2005 and applied the revised approach to 2006, resulting in the claim for additional ITCs of \$1,279,180.49 which is the subject of this appeal.

[17] With respect to the new method for calculating ITCs, in 2006, Sun Life started measuring the physical dimensions of some of its financial centres to obtain a clearer picture of the actual use of the space. Initially, Sun Life prepared diagrams for 11 financial centres, which divided the space into four categories and provided the floor area for each category (the 11 diagrams are reproduced at Tab 6

³ Transcript at pages 25 to 26.

of the Joint Book): (1) space used, or intended for the use of, Advisers (shown in yellow); (2) space used by Sun Life (shown in blue); (3) space used by both Sun Life and the Advisers (shown in pink); and (4) interior corridor and hallway space (shown in various ways in green). In addition to the four categories of coloured space, the building common areas such as elevators, stairways, washrooms and public hallways are shown without any colouring.

[18] The floor area for each category was determined and, in the case of the third and fourth categories and the public common areas, was allocated between the Advisers and Sun Life. The 11 samples were used to estimate the use of space in every financial centre for 2004, 2005 and 2006. Mr. Coutu testified that in subsequent years Sun Life measured every financial centre so that it did not have to rely on estimates.⁴

[19] Sun Life's revised methodology for the calculation of ITCs for 2004, 2005 and 2006 is found in worksheets reproduced at Tabs 1, 2 and 3 of the Joint Book and in supporting materials found at Tabs 4 and 5 of the Joint Book. Mr. Coutu provided an explanation of this methodology, using as an example the calculation of ITCs for the Toronto East financial centre for 2004, found at Tab 1, page 2 of the Joint Book:

- Column A, titled "Total Rent/Maintenance", sets out the total rent paid for the financial centre in 2004, which for Toronto East is \$520,188.
- Column B, titled "GST Paid on Rent Per GL", sets out the total GST paid on the rent in column A, which for Toronto East is \$33,279.15.
- Column C, titled "Leasehold Expense", sets out any other expenses that Sun Life incurred in respect of the financial centre, such as maintenance charges (Mr. Coutu was not certain of the details). The amount stated is \$741.
- Column D, titled "Leasehold Capital", was not explained, but appears to set out any capital expenditures made by Sun Life on leaseholds.
- Column E, titled "Total Leaseholds", was not explained, but is described under the heading as the sum of Columns C and D, which for Toronto East is \$741.

⁴ Transcript at page 42.

- Column F, titled “Calculated GST on Leaseholds”, was not explained, but is described under the heading as Column E times 7/115, which for Toronto East is \$45.10.
- Column G, titled “Total GST on Rent and Leaseholds”, sets out the total GST payable by Sun Life in respect of its lease of the financial centre. It is described under the heading as the sum of Columns B and F, which for Toronto East is \$33,324.25.
- Column H, titled “Square Footage under Lease”, sets out the square footage leased by Sun Life from the landlord as stated in the relevant lease, which for Toronto East is 16,550 square feet. No explanation was provided by Sun Life as to why this number differed from the 11,500 square feet stated on the diagram for that financial centre at Tab 6, page 22 of the Joint Book. Only the diagrams for Hamilton and Barrie also included a figure for the area under lease and in both cases it differed from the number in Column H – one being lower and the other being higher.
- Column I, titled “Square Footage Available for Rent to Advisors”, sets out the total space in the financial centre available to rent to Advisors, including any such space that is not occupied, which for Toronto East is 5,838 square feet. This is the space shown in yellow on the diagram of the Toronto East financial centre at Tab 6 of the Joint Book. The percentage of vacant space is indicated in an undesignated adjacent column titled “Vacant Space As a % of Total Area under Lease” as being 13.06%. Mr. Coutu acknowledged that there was a small discrepancy between the area stated in Column I of 5,838 square feet and the area stated on the diagram for Toronto East at Tab 6 of the Joint Book of 5,948 square feet. He suggested that the amount in Column I represented how much of the yellow space on the diagram was actually available to rent to Advisors.
- The undesignated column titled “Vacant Space As a % of Total Area under Lease” sets out the vacancy rate in the financial centre as a percentage of the total area under lease, which for Toronto East is 13.06%.
- Column J, titled “Square Footage of Specific Common Elements Attributed to Advisors”, sets out the portion of the space used by Sun Life and the Advisors (the space shown in pink on the diagram at Tab 6 of the Joint Book) that is allocated to the Advisors, expressed in square feet. The allocation was done on a room-by-room basis, but in the aggregate 65% of

the jointly used area was allocated to the Advisers, which in Toronto East represented an area of 534 square feet. For financial centres that were not measured, the aggregate jointly used space was assumed to be 664 square feet, which was the average amount of such space in the 11 financial centres that were measured. The amount allocated to Advisers was 65% of 664 square feet, or 431 square feet. The rationale for the allocation of the jointly used space is found at Tab 4 of the Joint Book, where it is stated:

Telecommunications Room – This room handles the equipment and services related in order to service the offices with their telecommunication needs. Using the average of advisor occupied space as a percentage of total occupied space.

Closing Room – This is a meeting room where the independent advisors meet with clients to finalize/close sales. This is allocated to the advisors at a 100% [sic]

Reception Area Seating – This area is allocated to the advisors using the average of advisor occupied space as a percentage of total occupied space.

Supply Room – Area for storage of stationary [sic] and supplies. This is allocated to the advisors at a rate of 50% rather than the average rate.

Kitchen – This area is allocated to the advisors using the average of advisor occupied space as a percentage of total occupied space.

Touch Down Station – An area for agents that do not occupy an office in the building. There is no consideration received for this space from the advisors. Therefore this area [sic] has been fully allocated to management.

- Column K, titled “Total measured footage attributed to advisors”, is the sum of Columns I and J, which for Toronto East is 6,372 square feet.
- An undesignated column titled “Common Area Gross-Up Based on Floorplan” sets out the interior corridor area as a percentage of the total measured area of the financial centre. In the case of Toronto East, the calculation is 2,176 square feet divided by 10,461 square feet, which yields 20.80%. This column is relevant only to the 11 financial centres that were measured. For the other financial centres, 12% is used, which, Mr. Coutu noted, was lower than the 26.02% average for the measured financial centres.

- Column L, titled “Interior common area Gross Up Factor”, is column K multiplied by a percentage that is intended to attribute a portion of the interior corridor area to the Advisers. The column’s description of the math is not correct but I have assumed from the numbers presented that it should read K multiplied by one plus either 12% or the percentage based on the actual measurements as determined in the immediately preceding column). The calculation of the gross-up percentage for the measured financial centres is described in more detail in Tab 5 of the Joint Book. The result stated for Toronto East is 7,697 square feet, which is 6,372 times 1.208.
- Column M, titled “Straight Ave Building Gross Up Factor” sets out as a percentage the ratio of the common building area attributed to Sun Life under the relevant lease to the useable floor area as set out in the lease. For example, the lease for the Brossard financial centre reproduced at Tab 7, page 27 of the Joint Book states in section 1.01 that the leased area consists of 8,855 square feet of useable area and an additional 1,328 square feet of building common area as described in section 8.01 g), for a total area under lease of 10,183 square feet. This yields a percentage ratio of 1,328 divided by 8,855 or approximately 15%. If the lease did not support such a calculation then, Mr. Coutu testified, 5% was used. The gross-up used for Toronto East is 12%. A note accompanying the column states:

The building gross-up factor is a specific factor provided by the landlord to account for building common spaces. In those instances where Sun Life office [*sic*] are located in storefronts, there is [*sic*] no building common spaces. However in these instances, there is typically additional interior common space. As a result Sun Life has found that the common space gross-up is insufficient and adds an additional 5% factor. Both the Interior Common Space and Building Grossup [*sic*] is [*sic*] included in the total area under lease.
- Column N, titled “Building Gross Up Footage”, sets out in square feet the result of multiplying column L by column M, which for Toronto East is 924 square feet.
- Column O, titled “Total footage with Building Gross up”, sets out the sum of column L and column N and is intended to represent the total floor area attributable to the Advisers. The result stated for Toronto East is 8,621 square feet, which is 7,697 plus 924.

- Column P, titled “% of Inputs Allocatable to Advisors”, sets out the result, as a percentage, of dividing column O by column H. For Toronto East, the calculation is 8,621 divided by 16,550, which yields 52.09%.
- Column Q, titled “GST Allocated to Advisors”, sets out the result in dollars of multiplying column P by column G. For Toronto East, the calculation is 52.09% of \$33,324.25, which for Toronto East is \$17,358.94.⁵

[20] In a nutshell, Sun Life determined what it considered to be the area acquired for the use of Advisors in each financial centre (including the area of any vacant space held for such use) and then grossed up that area by three factors intended to attribute to the Advisors their share of (1) the jointly used spaces within the financial centre, (2) the internal corridors and hallways of the financial centre, and (3) the building common areas attributed to Sun Life in the lease for the financial centre (for clarity, I will refer to these three areas collectively as the common-use space). The total so allocated to the Advisors was then divided by the total area under lease to provide the percentage of the GST paid by Sun Life on rent and leasehold expenditures that was attributable to the Advisors.

[21] Mr. Coutu testified that the foregoing methodology used for 2004 was also applied to the 2005 and 2006 periods. The calculations for these periods are found at Tabs 2 and 3 of the Joint Book, respectively. Mr. Coutu testified that for 2007 and subsequent years, Sun Life used actual measurements for each of the financial centres and that, as a result, the total ITCs claimed by Sun Life increased. According to Mr. Coutu, this was because of the conservative percentages used to take into account the common-use space. The actual percentages were on average higher, with the result that the percentage of the square footage under lease attributed to the Advisors was on average higher when using actual measurements for each financial centre.

[22] The witness for the Respondent, Mr. Lazure, testified that his on-site audit of the Brossard financial centre confirmed that the Advisors rented a specific office that was accessed through the main entrance of the financial centre and that the Advisors had access to the common-use space.

[23] Mr. Lazure testified that Revenu Québec had no issue with the measurements taken by Sun Life. The issue for Revenu Québec revolved around

⁵ Some of the numbers on the spreadsheets in Tabs 1, 2 and 3 of the Joint Book appear to reflect rounding by the software program that is not material.

the perceived attempt by Sun Life to claim ITCs in respect of space that was leased by Sun Life from a third party in order for Sun Life to carry on a financial services business. Specifically, the view of Revenu Québec is that the only evidence of a use of that space by Sun Life to provide a taxable supply is found in the subleasing of specific office space to Advisers. Any space that was not sublet to Advisers was being used by Sun Life in the course of its financial services business and not for the purpose of making taxable supplies and therefore it was unreasonable for Sun Life to claim ITCs in respect of any of that space.

A. The Appellant's Position

[24] Sun Life submits that the ITCs that may be claimed by it in respect of the receipt of taxable supplies from the third party landlords are not limited to the GST collected from the Advisers as a result of the taxable supply of office space made by it to the Advisers. Rather, the determination of the ITCs is based on a narrow independent purpose test that focuses on each particular supply in order to determine if it is being made in the course of a commercial activity and can be tracked to a particular input. The purpose of the particular input determines whether the input is in relation to the making of taxable or of exempt supplies. Where a registrant such as Sun Life acquires or uses inputs (the Leased Space) for the purpose of making both taxable supplies (subleasing a portion of the Leased Space to the Advisers) and exempt supplies (selling Financial Products), the ETA limits the claim for ITCs to reflect only the GST paid on the inputs acquired for the purpose of making taxable supplies. It is up to Sun Life, however, to determine an allocation method that is fair and reasonable and used consistently throughout the year. There is no rule that requires the use of a specific method, and once a fair, reasonable and consistent method has been chosen by Sun Life, the Minister is not entitled to replace that method with one of her own choosing simply because she believes it is a better method or even the best method.

[25] Sun Life submits that the method chosen by it was fair and reasonable because, to determine the amount of the ITCs, it relied on the area of the space acquired for the purpose of supply to the Advisers. The inclusion of the vacant space in the area acquired for the purpose of making taxable supplies was fair and reasonable for three reasons. First, Sun Life intended to sublet the vacant space to the Advisers. Second, the inclusion of that space on the basis of intended use was consistent with the text and context of subsections 169(1) and 141.01(2) of the ETA. Finally, the vacant space accounted for only 11% of the total space leased by Sun Life. The inclusion of the three gross-ups in the area acquired for the purpose of making taxable supplies was fair and reasonable because without these

adjustments the result would present an unrealistic view of how the property was being used by the Advisers. In addition, Sun Life submits that the gross-ups were consistent with the approach taken by the Tax Court of Canada in *Bay Ferries Limited v. The Queen*, 2004 TCC 663 and by the Federal Court of Appeal in *Ville de Magog v. The Queen*, 2001 FCA 210.

B. The Respondent's Position

[26] The Respondent states that the facts and the numbers in this appeal are not in dispute. The Respondent's position is simply that the method chosen by Sun Life is not a "fair and reasonable" method for determining the extent to which the acquisition of the Leased Space was for the purpose of making taxable supplies for consideration. The Respondent submits that the primary business of Sun Life is the rendering of financial services, which is an exempt supply under the ETA and does not give rise to ITCs. Sun Life also carries on a side business which consists of subleasing office space to Advisers.

[27] The Respondent submits that, while there is no doubt that the subleasing of the office space to Advisers is a taxable supply that entitles Sun Life to ITCs, the method chosen to determine those ITCs does not reflect the fact that Sun Life's efforts are focused not on the subleasing of the space but on the recruitment of Advisers, who may or may not sublease space from Sun Life. The intention to sublease the vacant space is thus secondary to the intention to recruit Advisers to sell Financial Products for Sun Life. The Respondent argues that the Advisers play two roles. The first is as tenants of Sun Life. The second is as workers helping Sun Life carry on its business of selling Financial Products. In the Respondent's view, the allocation of the common space to the taxable supply of space to the Advisers fails to recognize that the Advisers are using the common space not because they are tenants but because they are selling Financial Products on behalf of Sun Life. The Respondent says that this is most evident in the allocation of the closing room space to the taxable supply of space to the Advisers. When using that space, the Adviser is not acting as a tenant but as a seller of Financial Products for Sun Life.

[28] To support this position, the Respondent points to the fact that the percentage of vacant space is considerable when compared to the space actually subleased to the Advisers and that there was no evidence of any attempt by Sun Life to downsize the space rented by it from the third party landlords. As well, Sun Life admitted that it would not rent the vacant space to anyone other than an Adviser. The Respondent submits that this situation is therefore different from the case of a landlord who is in the business of subleasing space but has vacancies due

to economic conditions. The Respondent also states that Sun Life's assertion that all the vacant space is intended for Advisers ignores the possibility that the space could be used for another purpose, such as occupation by an employee of Sun Life.

III. The Law

[29] The statutory provisions of the ETA relevant to the issue in this case are as follows:

123(1)

“commercial activity” of a person means

(a) a business carried on by the person (other than a business carried on without a reasonable expectation of profit by an individual, a personal trust or a partnership, all of the members of which are individuals), except to the extent to which the business involves the making of exempt supplies by the person . . .

“exempt supply” means a supply included in Schedule V;

Schedule V, Part VII - Financial Services

1. A supply of a financial service that is not included in Part IX of Schedule VI.

“taxable supply” means a supply that is made in the course of a commercial activity;

165.(1) Imposition of goods and services tax — Subject to this Part, every recipient of a taxable supply made in Canada shall pay to Her Majesty in right of Canada tax in respect of the supply calculated at the rate of 5% on the value of the consideration for the supply.

169.(1) General rule for [input tax] credits — Subject to this Part, where a person acquires or imports property or a service or brings it into a participating province and, during a reporting period of the person during which the person is a registrant, tax in respect of the supply, importation or bringing in becomes payable by the person or is paid by the person without having become payable, the amount determined by the following formula is an input tax credit of the person in respect of the property or service for the period:

$$A \times B$$

where

A is the tax in respect of the supply, importation or bringing in, as the case may be, that becomes payable by the person during the reporting period or that is paid by the person during the period without having become payable; and

B is

...

(c) in any other case, the extent (expressed as a percentage) to which the person acquired or imported the property or service or brought it into the participating province, as the case may be, for consumption, use or supply in the course of commercial activities of the person.

141.01 [Allocation of input tax credits] - (1) Meaning of “endeavour” — In this section, “endeavour” of a person means

(a) a business of the person;

(b) an adventure or concern in the nature of trade of the person; or

(c) the making of a supply by the person of real property of the person, including anything done by the person in the course of or in connection with the making of the supply.

...

(2) Acquisition for purpose of making supplies [limitation on ITCs] — Where a person acquires or imports property or a service or brings it into a participating province for consumption or use in the course of an endeavour of the person, the person shall, for the purposes of this Part, be deemed to have acquired or imported the property or service or brought it into the province, as the case may be,

(a) for consumption or use in the course of commercial activities of the person, to the extent that the property or service is acquired, imported or brought into the province by the person for the purpose of making taxable supplies for consideration in the course of that endeavour; and

(b) for consumption or use otherwise than in the course of commercial activities of the person, to the extent that the property or service is acquired, imported or brought into the province by the person

(i) for the purpose of making supplies in the course of that endeavour that are not taxable supplies made for consideration, or

(ii) for a purpose other than the making of supplies in the course of that endeavour.

(3) Use for purpose of making supplies — Where a person consumes or uses property or a service in the course of an endeavour of the person, that consumption or use shall, for the purposes of this Part, be deemed to be

(a) in the course of commercial activities of the person, to the extent that the consumption or use is for the purpose of making taxable supplies for consideration in the course of that endeavour; and

(b) otherwise than in the course of commercial activities of the person, to the extent that the consumption or use is

(i) for the purpose of making supplies in the course of that endeavour that are not taxable supplies made for consideration, or

(ii) for a purpose other than the making of supplies in the course of that endeavour.

(5) Method of determining extent of use, etc. — Subject to section 141.02, the methods used by a person in a fiscal year to determine

(a) the extent to which properties or services are acquired, imported or brought into a participating province by the person for the purpose of making taxable supplies for consideration or for other purposes, and

(b) the extent to which the consumption or use of properties or services is for the purpose of making taxable supplies for consideration or for other purposes,

shall be fair and reasonable and shall be used consistently by the person throughout the year.

[30] The current version of subsection 141.01(5), contained in the Appellant's Book of Authorities, references section 141.02, and was enacted in 2010 effective for fiscal years that begin after March 2007. Section 141.02 sets out special rules for allocating the ITCs of financial institutions such as Sun Life. These rules were not applicable during the periods in issue in this appeal.

IV. Analysis

[31] The general scheme and purpose of the GST provisions of the ETA were explained by the Federal Court of Appeal in *CIBC World Markets Inc. v. The Queen*, 2011 FCA 270, [2013] 3 F.C.R. 3 as follows:

A. The statutory scheme: an overview

5 I shall begin with a broad, conceptual review of the general scheme and purpose of the GST provisions of the Act. This will provide context for interpreting the specific provisions at issue in this appeal.

(1) The purpose of the GST provisions of the Act

6 The GST is a consumption tax. The GST provisions of the Act show that it is meant to be paid by the final consumers of goods and services. An early technical paper issued by the Minister on the GST confirms this: Canada, Department of Finance, “Goods and Services Tax: Technical Paper” (Ottawa: Department of Finance, 1989).

(2) The key liability provision: subsection 165(1) of the Act

7 Subsection 165(1) of the Act sets out a general rule: those who receive services or property, such as goods, in the course of a commercial activity (known under the Act as a “taxable supply”) are liable to pay GST.

(3) Who is subject to GST

8 The general rule in subsection 165(1) of the Act applies to all, even those who are not final consumers.

9 In particular, each recipient of taxable goods and services is potentially liable to pay GST, even if it, as an intermediary, ultimately delivers those goods and services to others. For example, a wholesaler may supply goods to a retailer who supplies them to a consumer. The retailer is liable to pay GST under the general rule in subsection 165(1).

10 Were the matter left there, the GST would lose its character as a consumption tax imposed on the final consumers of goods and services. It would attach, full force, to each party in a chain of transactions culminating in the final receipt by consumers.

(4) Input tax credits: the general concept

11 One way in which the Act prevents this consequence is by giving parties credits for “inputs” that they receive.

12 For example, for the purpose of the selling of goods to consumers, a retailer might receive “inputs,” such as inventory. That “input” to the retailer is necessary in order for it to make a supply of the goods to the consumer. Depending on the particular business, there may be all sorts of necessary “inputs.”

13 Obviously, if, in the example above, the retailer were not given credit for the GST paid on inputs needed for the making of a taxable supply of goods to a

consumer, the GST would be imposed full force on it and, for that matter, on every intermediary in the chain of distribution. If that happened, the GST would lose its character as a consumption tax imposed on the final consumer of goods and services.

14 To achieve the purpose of taxing the final consumers of goods and services, the Act allows tax credits for inputs received by parties to make an onward taxable supply. These credits are called input tax credits.

15 The input tax credits, as explained above, ensure that the fundamental character of the GST as a consumption tax on final consumers is maintained. In the words of the Minister:

A fundamental principle underlying the GST/HST is that no tax should be included in the cost of property and services acquired, imported or brought into a participating province by a registrant to make taxable supplies...in the course of the commercial activities of the registrant. To ensure that a property or service consumed, used or supplied in the course of commercial activities effectively bears no GST/HST, registrants are generally eligible to claim an input tax credit (ITC) for the GST/HST paid or payable on such property or service. Consequently, the ITC enables each registrant to recover the tax incurred in that registrant's stage of the production and distribution process.

(Canada Revenue Agency, "GST Memorandum 8.1 — General Eligibility Rules" (May 2005) at paragraph 1.)

(5) Input tax credits: a further complication

16 A further complication needs to be mentioned. Some supplies under the Act are not taxable, because they do not fall under section 165(1) of the Act, or they are otherwise exempt under the Act.

17 A person may be a supplier of both taxable and exempt goods or services, but is entitled to input tax credits only for inputs relating to the taxable supplies.

18 Where a person is a supplier of both taxable and exempt supplies, a method must be found to limit the claim for input tax credits to reflect only goods and services acquired or used for making taxable supplies.

19 The Act solves this problem by allowing parties (in subsection 141.01(5)) to adopt a general allocation method.

20 Not all methods are acceptable. Subsection 141.01(5) provides that the method must be “fair and reasonable” and must “be used consistently by the person throughout the year.”

[32] The starting point in this case is subsection 169(1). For Sun Life to claim the ITCs in issue, the space leased from third party landlords to house the financial centres must have been acquired for consumption, use or supply in the course of commercial activities of Sun Life. The commercial activities of Sun Life include any business carried on by Sun Life, except to the extent to which the business involves the making of exempt supplies by Sun Life. The definition of “commercial activity” is worded in such a way that only the portion of any business that involves the making of exempt supplies is excepted from the definition. The provision of financial services by Sun Life is an exempt supply unless the service is included in Part IX of Schedule VI.

[33] Where Sun Life acquires property or a service for consumption or use in the course of an endeavour,⁶ as it has done here,⁷ subsection 141.01(2) deems it to have acquired the property or service for consumption or use in the course of commercial activities of Sun Life to the extent that the property or service is acquired by Sun Life for the purpose of making taxable supplies for consideration in the course of that endeavour. On the other hand, to the extent that the property or service is acquired by Sun Life (i) for the purpose of making supplies in the course of that endeavour that are not taxable supplies made for consideration, or (ii) for a purpose other than the making of supplies in the course of that endeavour, the property or service is deemed to have been acquired by Sun Life for consumption or use otherwise than in the course of commercial activities of Sun Life.

[34] Subsection 141.01(2) focuses on Sun Life’s purpose in acquiring property or a service. It is up to Sun Life to explain its purpose in acquiring property or a service, and that explanation must be neither improbable nor unreasonable (see, generally, *Canada v. Placer Dome Inc.*, [1997] 1 F.C. 780 (FCA) at paragraph 19).

⁶ An endeavour of a person is defined in subsection 141.01(1) to mean (a) a business of the person, (b) an adventure or concern in the nature of trade of the person, or (c) the making of a supply by the person of real property of the person, including anything done by the person in the course of or in connection with the making of the supply.

⁷ The endeavour in this case is the business of Sun Life. Although the definition of endeavour also includes in paragraph (c) the making of a supply of real property, the supply of the Leased Space in this case is part of Sun Life’s broader business so there is no need to rely on paragraph (c).

[35] Subsection 141.01(5) presupposes that a particular acquisition has more than one purpose and in such a case requires the person acquiring the property or service to determine the extent to which the property or service is acquired for the purpose of making taxable supplies for consideration or for other purposes. The method used to make this determination must be fair and reasonable and must be used consistently throughout the year. Subsection 141.01(5) thus requires that the method chosen by Sun Life to determine the extent to which a dual-purpose property or service is acquired by it for the purpose of making taxable supplies for consideration or for other purposes be fair and reasonable.

[36] One definition of the word “fair” in the *Oxford English Dictionary* (Second Edition) suggests that the approach taken by Sun Life must be equitable, honest and impartial (see “fair”, adverb, (definition) 4.), which in my view is an appropriate interpretation of the word as used in subsection 141.01(5). The use of the word “justes” in the French version of the provision supports this interpretation.

[37] The definition of the word “reasonable” in the *Oxford English Dictionary* (Second Edition) that is in my view most appropriate is A.2.a: “Having sound judgement; sensible, sane. . . . Also, not asking for too much.” The use of the word “raisonnables” in the French version of the provision supports this interpretation.

[38] The use of a reasonableness requirement in tax legislation has been considered in other contexts. In *Bailey v. M.N.R.*, [1989] T.C.J. No. 602 (QL), 89 DTC 416, the Court stated (at page 420):

What is “reasonable” is not the subjective view of either the respondent or appellant but the view of an objective observer with a knowledge of all the pertinent facts: *Canadian Propane Gas & Oil Limited v. M.N.R.*, 73 DTC 5019 per Cattanach J. at 5028.

[39] In *Maege v. The Queen*, 2006 TCC 117, the Court adopted the general approach to determining reasonableness set out in *Tsiantoulas v. Canada*, [1994] T.C.J. No. 984 (QL), where the Court stated at paragraph 11:

Reasonableness is a question of fact and requires the application of a measure of judgement and common sense.

[40] I can see no reason why the general approach to determining reasonableness in these cases would not also apply to determining whether a particular method is “fair and reasonable”. That is to say, what is “fair and reasonable” is a question of

fact and requires the application of a measure of judgment and common sense. The determination is not based on the subjective view of either the Appellant or the Respondent but is based on the view of an objective observer with knowledge of all the pertinent facts. It is also important to recognize that the tax authorities cannot simply substitute their approach for that of Sun Life and that there may be more than one method that is fair and reasonable in the circumstances (see *Ville de Magog v. The Queen*, *supra*).

V. Conclusion

[41] Mr. Coutu testified that one purpose for which Sun Life acquired the Leased Space was to rent a portion of that space to Advisers (that is, one purpose for acquiring the Leased Space was to make taxable supplies for consideration in the course of Sun Life's business). The objective facts support this stated purpose, as offices in the Leased Space were rented by Sun Life to Advisers who in turn used the space to conduct their own businesses, which included the sale of Financial Products. The evidence is that Leased Space was also acquired by Sun Life for the purpose of making exempt supplies in the course of its financial services business (that is, for the purpose of making supplies in the course of its business that are not taxable supplies made for consideration).

[42] The dual purpose for the acquisition of the Leased Space requires Sun Life to adopt a method for determining the extent to which the Leased Space was acquired for the purpose of making taxable supplies for consideration or for other purposes. The method chosen must be fair and reasonable and must be used consistently throughout the year. The consistency requirement is not in issue in this case.

[43] Initially, Sun Life claimed ITCs in respect of the portion of the Leased Space subleased to the Advisers on the basis of the rent paid by the Advisers for the subleased space. This resulted in a claim for ITCs by Sun Life essentially equal to the amount of GST collected from the Advisers on the rent. According to Mr. Coutu, the rent charged to the Advisers was grossed up to estimate the effective cost to Sun Life of the subleased space. Hence, this method did take into account the GST paid by Sun Life on a portion of the common-use space because the rent charged to the Advisers reflected a portion of the cost of that space to Sun Life. In other words, by including a portion of the cost of the common-use space in the calculation, the original method assumed that a portion of the common-use space was acquired by Sun Life for the purpose of making taxable supplies for consideration in the course of its business.

[44] The original method did not, however, take into account the GST paid by Sun Life on the vacant space that Sun Life says was reserved for the use of Advisers, nor did it take into account the GST paid by Sun Life on the portion of the common-use space that might be attributed to the use of that vacant space.

[45] Sun Life replaced this simple method for determining its ITCs with a more complicated method based on the total amount of Leased Space used by, or reserved for, Advisers and a gross-up that Sun Life says attributes an appropriate percentage of the common-use space to that space. The question is whether the new method is fair and reasonable.

[46] It is of note that both methods attribute to a portion of the common-use space the purpose of making taxable supplies for consideration in the course of Sun Life's business. The original method achieved this result because it was based on the rent charged to the Advisers for the subleased space, which in turn was set at a level that was intended to recoup "significantly all" of the effective cost of that space to Sun Life. The effective cost included a portion of the cost of the common-use space. The new method, on the other hand, used measurements and assumptions as to use in order to determine the purpose of acquiring the common-use space. The evidence was that the assumptions were conservative and did not overstate the purpose for acquiring the common-use space. The Respondent did not challenge the accuracy of the measurements used under the new method.

[47] The Brossard financial centre example lease and sublease suggest that the gross-up for common-use space implicit in the rent charged to the Advisers at that financial centre was approximately 1.391 (that is, \$32/\$23). The gross-up for the same space under the new approach was 1.394 (that is, 7,299 sq ft/5,236 sq ft) in 2004. Although Brossard is only one example, the difference is slight, so it is difficult to see how the inclusion of common-use space under the new method is not fair and reasonable if it was fair and reasonable under the original method. Both methods appear to yield ITCs commensurate with the GST on the true cost to Sun Life of the Leased Space that was sublet to Advisers.

[48] The Respondent argued, however, that the explicit allocation of the common-use space to the taxable supply of space to the Advisers that occurs under the new method fails to recognize that the Advisers are using the common-use space not because they are subtenants but because they are selling Financial Products on behalf of Sun Life. In my view, this argument fails to recognize that the Advisers are independent contractors and that their use of the subleased space

is in furtherance of their own business objectives, which include the sale of products other than the Financial Products.

[49] I also note that the Advisers cannot use the subleased space without also using the common-use space. From a practical point of view, it seems somewhat obvious that Sun Life would need to rent common-use space in order to be able to sublet office space to the Advisers, and therefore, attributing that purpose to a portion of the common-use space accords with common sense. The fact that the rent charged to the Advisers reflects the cost of essentially that same portion of the common-use space further supports this observation.

[50] The Respondent also argued that Sun Life's efforts were focused not on the subleasing of the space but on the recruitment of Advisers, which was admitted by Mr. Coutu. I have no doubt that the availability of space to rent would have aided the recruitment of Advisers. However, recruitment was a benefit derived from having space available to rent to Advisers and was not the direct purpose of the available space. In that regard, the situation is similar to that in *London Life Insurance Co. v. The Queen*, 266 N.R. 130 (FCA), where the Court distinguished between the direct purpose for the acquisition of property (supplying leasehold improvements to the landlord) and the indirect (or ultimate) purpose for the acquisition of property (leasing improved premises for a financial services business) and held that the direct purpose governed London Life's claim for ITCs. In this case, the direct purpose of the available space was to rent the space to Advisers and the indirect (or ultimate) purpose of having space available was to aid recruitment and to facilitate the sale of Financial Products.

[51] The major difference between the original method used by Sun Life and the new method is that the new method attributes the purpose of making taxable supplies for consideration to the vacant space reserved for the Advisers as well as to the portion of the common-use space attributable to that vacant space. The attribution of common-use space to the vacant space is not materially different in result from the attribution of common-use space to the subleased space under the original method. Hence, the only real distinction between the original method and the new method is the inclusion of the vacant space itself.

[52] I accept Mr. Coutu's uncontradicted testimony that the vacant space was reserved for the use of Advisers to accommodate the growth of the financial centres. In my view, attributing the purpose of making taxable supplies for consideration to the vacant space is fair and reasonable in the circumstances of this case because it accurately reflects Sun Life's purpose with respect to the direct use

of that vacant space. The attribution of common-use space to that vacant space in accordance with the new methodology is fair and reasonable for the reasons already stated in respect of the subleased space.

[53] The Respondent did suggest that the vacant space could be used for a different purpose, such as to house an employee of Sun Life. However, there was no evidence that this in fact occurred during 2004, 2005 or 2006. The evidence was that, if a change in use occurred, the particular vacant space (and its associated common-use space) would be removed from the pool of space reserved for the Advisers such that ITCs would no longer be claimed in respect of that space.

[54] The Respondent also pointed to the amount of vacant space as supportive of her position. However, the fact that there was a significant amount of vacant space reserved for the use of Advisers does not alter Sun Life's purpose in acquiring that space. The amount of vacant space that is required for rental to Advisers is a business judgment that is best left to Sun Life absent a sham or window dressing or similar vitiating circumstances, none of which are present here.

[55] For the foregoing reasons, the appeal is allowed, with costs to the Appellant, and the reassessment made for the reporting period from January 1, 2006 to December 31, 2006 is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that Sun Life is entitled to additional ITCs of \$1,279,180.49.

Signed at Ottawa, Canada, this 16th day of February 2015.

“J.R. Owen”

Owen J.

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