Tax Notes

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PERSONAL TAX SEASON PREVIEW

— Maureen Vance, CPA, CA, Tax Software Consultant, Wolters Kluwer

As we enter the New Year, many tax practitioners will start to ramp up for yet another personal tax season and I am reluctant to admit it (even to myself), but this will be my 33rd tax season.

Just over a year ago, in an article entitled "The Evolution of Personal Tax Preparation" (Tax Topics 2283, December 10, 2015), I described some of the changes to personal tax preparation that I have seen over the years. For the upcoming tax season, we will see even more changes, including new e-services from the CRA. Here are some of the highlights we can expect to see this season.

Principal Residence Exemption

The change that is generating the most buzz amongst preparers appears to be related to dispositions of a principal residence. Proposed changes will modify the calculation of the principal residence exemption by effectively eliminating the "one plus" year in the calculation of the principal residence exemption ("PRE") for non-residents (for more information on the impact of this proposed change, see the article "A Primer on the New Principal Residence Rules" in Tax Topics 2332, November 17, 2016). However, it is a change in administrative practice that will affect the most tax returns.

Up until 2016, it has been CRA administrative practice that where an individual taxpayer disposed of their principal residence and no gain was taxable because the property was his or her principal residence during each year of ownership, the disposition did not have to be reported on their tax return.

However, starting with the 2016 tax year, all dispositions of a principal residence must now be reported in the tax year in which the property was sold, even if the property was the taxpayer's principal residence during each year of ownership. Schedule 3 has been revised for 2016 to add a new section in which the taxpayer must indicate any dispositions of a principal residence. The good news is that while the CRA is asking for the address (understandably) and the proceeds of disposition, they are not asking for any cost information, just the year of acquisition. So provided the property is fully exempt, there is no need to worry about taxpayers that have long since lost their purchase documentation!

It is important to note that the PRE will only be available if the sale is reported in the tax return in the year of disposition. If the sale is not reported, the taxpayer can request an amendment, but as the PRE is an election, any late-filed election may be subject to a penalty under subsection 220(3.5) of up to $8,000. However, the CRA has stated that for 2016, they will only assess a late-filing penalty in the most excessive cases.

Tax preparers should take note that this reporting requirement also applies to deemed dispositions, for example, when there has been a change in use.

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Home Accessibility Tax Credit

This tax credit was announced in the 2015 federal Budget. A non-refundable credit of 15% may be claimed on up to $10,000 of expenditures for home renovations to an eligible dwelling that improve accessibility, safety, or security for a senior or person with disabilities. The credit is similar to provincial credits already in place in Ontario, BC, and NB for seniors. The federal credit, however, is also available to persons with disabilities regardless of their age, and for 2016, the BC credit has been similarly expanded.

The credit will be reported on Schedule 12 (resurrected from the 2009 Home Renovation Tax Credit) and a provincial version of Schedule 12 is already in use for the aforementioned provincial credits. It is not only available to homeowners that are qualifying individuals (i.e., a senior or disabled person), but also to their family members if the qualifying individual resides with the family member.

Of course, as the CRA may ask for receipts to validate the claim, this could be a challenge for preparers, as many eligible families may not have been aware of the credit and therefore may not have obtained the necessary receipts.

Eligible Educator School Supply Tax Credit

This credit was introduced in the 2016 federal Budget. It provides a refundable tax credit of up to $150 for teachers and early childhood educators that purchase supplies out of their own pocket for use in the classroom or regulated day care. However, not only may the CRA ask for receipts to substantiate the credit, but the legislation includes a provision whereby the CRA may also request a written certificate from the taxpayer's employer certifying the eligibility of the expenses.

Tax Credits Reduced and Eliminated

The Family Tax Cut, which allowed for a limited form of income splitting, has been eliminated for 2016. The maximum fees for the children's arts amount is reduced from $500 to $250 and the maximum fees eligible for the children's fitness tax credit is reduced from $1,000 to $500 for 2016. Both credits will be eliminated in 2017.

The Overseas Employment Tax Credit which, starting in 2013, has been reduced each of the past three years, is now completely eliminated for 2016.

Tax Rates and Charitable Donations

Practitioners that prepare returns for high income earners will most likely already be aware of the introduction of the new 33% federal tax bracket for taxable income in excess of $200,000. What may be less well known is the related change to the calculation of the tax credit for charitable donations. The tax credit now allows for a credit of 33% for donations over $200, but only to the extent that the taxpayer is subject to the 33% tax rate (i.e., the taxable income in excess of $200,000). However, donations carried forward from 2015 or prior years only give rise to a 29% credit.

Changes to Auto Fill My Return

Some additional data will be available to download via Auto Fill My Return ("AFR") for 2016 returns. Data on a T1204 Government Service Contract Payment slip has been added as well as PRPP contribution receipts, and for T3s, T5s, and T5018s, the beneficiary code has been added to the list of fields downloaded — which should make it easier to identify slips relating to joint accounts.

T1 software will also be able to download an indicator of whether a T1135 for Foreign Property was filed in the prior year (which will be helpful for new clients) and EFILE software will be able to download new indicators, including whether or not another preparer had accessed the client's account.

In addition, the CRA is going to allow preparers to continue to download slip information for late-filed 2015 returns, although non-slip data, such as RRSP information and instalments, will only be available to download for the current tax year. Preparers will need to access My Account through Represent a Client in order to view this information for a prior year.

Note that the foregoing only describes changes to the data available from the CRA. *Personal Taxprep* users will also find a number of software enhancements with respect to AFR, including the identification of slips added since the last download, as well as a form for reconciling consolidated T3 slips to the CRA T3 data.

Multi-Jurisdiction Returns

Starting with the 2016 tax year, the CRA is going to allow the electronic filing of returns that are reporting income from more than one province or jurisdiction (i.e., multiple jurisdiction returns). These returns will therefore be subject to the rules for mandatory electronic filing. However, the EFILE restrictions on returns claiming foreign tax credits from more than 3 countries, or reporting on more than 6 rental properties, will still apply.

Electronically Filing Amended Tax Returns (ReFILE)

Starting in February 2017, the CRA will allow the electronic filing of an amended T1 using EFILE certified software, similar to what can already be done for amended T2 returns. And while representatives with Level 2 authorization (i.e., the authorization to make changes to a return) have been able to submit adjustment requests online through Represent a Client, this new service, called ReFILE, will simplify the process, as it will allow you to transmit the amended return from within your tax software.

Represent a Client

The CRA has indicated that starting in February 2017, the Represent a Client ("RAC") portal will be enhanced with the addition of a Represent a Client "Report Card" which will display the T1 assessment status of each client, including whether or not the return was assessed as filed. The CRA has also announced that representatives will be notified if tax slips are added to clients' accounts after filing.

For representatives of businesses, the CRA has indicated that the current RC59 form will be revised in May to only apply to authorizations where online access to information is not requested. In order to obtain online access to information, representatives will have to submit their request for a business authorization online through the Represent a Client portal.

Pre-Authorized Debit Agreements

For several years taxpayers have been able to set up a pre-authorized debit ("PAD") agreement with the CRA to pay instalments, etc. Now preparers can also offer taxpayers the ability to create an agreement as part of their T1 transmission. This may be useful for taxpayers that don't use online banking, but will have to be used with caution, as the PAD can require up to 5 business days for processing.

Express Notice of Assessment

For taxpayers preparing their own returns using NetFile software, if they have signed up for Online Mail (i.e., they no longer receive a paper copy of the notice of assessment), the CRA is planning to offer a new service, called Express Notice of Assessment, which will allow them to download their notice of assessment ("NOA") to their tax software once the return has been assessed, provided this service is supported by their software. While a similar service may be available in some EFILE software, it is not anticipated that this will be widely used by professional tax preparers, as the service will require re-assessing data files after the return has been accepted, then downloading and reviewing the NOA. Most preparers will find it easier to use the new RAC "Report Card" to identify clients whose NOA requires follow-up, then download the NOA directly through RAC if needed. In addition, for professional preparers, the Express NOA option will only be available if the client has signed new Part C on the T183, in which case the taxpayer will not receive a paper copy of the NOA unless the CRA is mailing a cheque to the taxpayer.

Conclusion

While this year's changes are perhaps not as dramatic as in some prior years (e.g., when electronic filing was first introduced), it still demonstrates that practitioners have to be aware of not only the legislative and form changes, but also of new CRA e-services. Something as simple as the promised Represent a Client "Report Card" could be a huge time saver if it means that you no longer have to review the NOA to check if the return was assessed as filed and/or rely on the client to inform you if there are any differences. And wouldn't that be nice?

CURRENT ITEMS OF INTEREST

2016 Meal and Vehicle Expense Amounts Released

The CRA released the 2016 dollar amounts for using the simplified method to claim meal and vehicle expenses. With respect to meal expenses, the amounts remain the same as previous years: $17 per meal to a maximum of $51 per day. The per kilometre amounts with respect to claiming vehicle expenses in the various provinces have all changed from that of 2015 and can be found in the news release: CCH Tax > Federal Income Tax > Past News > Government and Agency Documents > Canada Revenue Agency > Other [CCH-FIT-20170105-3945 - CCH-FIT-20160218-2294]> Meal and vehicle rates used to calculate travel expenses for 2016 and previous years.

2017 Automobile Deduction Limits and Benefit Rates

The Department of Finance recently published the prescribed amounts for automobile deduction limits and business expense benefit rates. All but one of the limits and rates are remaining the same as they were in 2016. The rate used in computing the taxable benefit to employees with respect to the personal portion of automobile operating expenses paid for by an employer is reduced by 1 cent to 25 cents per kilometre. The rate for those employed principally in the business of selling or leasing automobiles is also reduced by 1 cent to 22 cents per kilometre. All of the other unchanged amounts can be found in the full news release: CCH Tax > Federal Income Tax > Past News > Government and Agency Documents > Department of Finance Canada >News Releases [CCH-FIT-20170105-803 - 2015-004] > 2016-162 — Government Announces the 2017 Automobile Deduction Limits and Expense Benefit Rates for Business.

FOCUS ON CURRENT CASES

This is a regular feature examining recent cases of special interest, coordinated by John C. Yuan and Christopher L.T. Falk of McCarthy Tétrault LLP. The contributors to this feature are from McCarthy Tétrault LLP, Montreal, Toronto, Calgary, and Vancouver.

In Order To Assess a Group of Trusts on a Consolidated Basis Under Subsection 104(2), the Minister Must Consider Who the Ultimate Beneficiaries Are Across the Lifetime of Each Trust, Not on a Year-By-Year Basis

***Evoy Estate v. The Queen*, 2016 DTC 1207 (Tax Court of Canada)**

Mr. George Kenneth Evoy died in 2007. The terms of his will provided for the creation of three testamentary trusts, one for each of his three children: David, Karie, and Wendy. Each of the trusts had identical provisions that were customized to provide for the distribution of income and eventual termination of the trust for the benefit of the particular child's family. The trusts shared a common provision granting Mr. Evoy's spouse, Pauline, a life interest in the net annual income from each trust.

Subsection 104(2) of the *Income Tax Act* (the "Act") is an anti-avoidance rule that prevents a testator (or settlor) from taking advantage of the graduated marginal rate system by settling multiple, separate trusts and engaging in income splitting between them. The rule in effect permits the Minister to designate that multiple trusts be treated under the Act as a single trust where (a) substantially all of the property of each trust is received from the same person, and (b) the trusts are structured so that income accrues or will ultimately accrue to the same beneficiary or group or class of beneficiaries.

Pursuant to subsection 104(2) of the Act, the Minister of National Revenue assessed the trusts as one individual for each of their 2008, 2009, and 2010 taxation years. The trust established for the benefit of David Evoy and his family appealed the assessment.

The appellant trust argued that paragraph 104(2)(*b*) was meant to apply to the entire existence of the three trusts, and that though each trust conferred a common benefit to Pauline during her lifetime (including during the taxation years in issue), the income accruing after Pauline's death would accrue to distinct beneficiaries.

The Minister alleged that the requirement in paragraph 104(2)(*b*) was met since each of the trusts granted Pauline a life interest in its annual income. In reply to the appellant's argument about the distinct beneficiaries after Pauline's death, the Minister further argued that the application of paragraph 104(2)(*b*) could be made on an annual basis to

either designate or re-designate the beneficiary, group, or class of beneficiaries for whose benefit the income of the trust accrued or would ultimately accrue.

In the alternative, the Minister submitted that Mr. Evoy's children and their children constitute a class of beneficiaries sufficient to attract the application of paragraph 104(2)(*b*).

The Tax Court rejected both of the Minister's arguments. From a plain meaning standpoint, the Tax Court reasoned that the words "or will ultimately accrue" in paragraph 104(2)(*b*) suggested that the Minister was obliged to consider the lifetime of the trusts, not a single tax year at a time.

The Tax Court further questioned the Minister's position that a redetermination under subsection 104(2) could be made on an annual basis, when nothing in the provision allowed the Minister to re-designate a consolidated trust as multiple trusts in the event the conditions in paragraph 104(2)(*b*) were no longer met.

From a consequential standpoint, the Tax Court found that, if the Minister had the power to re-designate the applicability of the rule, it would lead to unpredictable results for the trustees of a consolidated trust who could not be expected to know whether to file a single return or multiple unconsolidated returns. Had Parliament intended to create an annual test, the Tax Court reasoned that there would be some express wording to that effect.

Looking to the income splitting mischief the provision was intended to combat, the Tax Court ruled that the purpose of the provision would accord more closely with the nature of tax planning through trusts if the designation was a one-time event lasting the length of the lifetime of the trusts.

The Tax Court rejected the Minister's alternative argument stating that none of the trusts had cross-over beneficiaries — each trust had a distinct class and none of the children and grandchildren of the settlor were entitled to receive benefits from all of the multiple trusts.

Though the issue was not addressed by the Tax Court, there may be an implicit assumption in the reasoning of the Tax Court that the phrase "ultimately accrue" ignores contingent beneficiaries. In the event that one of Mr. Evoy's children and all of that child's issue predeceased the termination of that child's trust, each of the trusts had contingent language to assign the capital of the trust to the trusts of the surviving children.

This decision ultimately provides an example of an approach to the statutory interpretation of an anti-avoidance provision that was heavily driven by a plain language approach and the particular facts before the Tax Court. As a result of changes to the Act that require trusts, with limited exception, to be taxed at the top federal marginal tax rate for their 2016 and subsequent taxation years, the rule now has limited applicability and seemingly applies only to historical tax returns and limited classes of testamentary trusts such as the qualified disability trust.

Neither party has filed an appeal of the Tax Court's decision.

— *Justin Shoemaker*

Corporate Issuer Liable for Tax on Look-Back Renunciations for Flow-Through Shares Issued to Non-Arm's Length Shareholders, Notwithstanding that Renunciations Were Invalid

***Tusk Exploration Ltd. v. The Queen*, 2016 DTC 1196 (Tax Court of Canada)**

The *Tusk* case provides useful commentary as to whether corporations making look-back renunciations in respect of flow-through shares are required to pay tax arising from the look-back renunciations even where the look-back renunciations are invalid.

The provisions of the *Income Tax Act* (the "Act") relating to flow-through shares allow investors in resource corporations to claim deductions from income for the purposes of the Act for certain expenses incurred by the corporation — including Canadian Exploration Expenses ("CEE") — instead of the corporation itself claiming such expenses. Flow-through shares thus provide a means for resource companies to finance their exploration activities.

Pursuant to subsection 66(12.61) of the Act, the effect of a renunciation of CEE is that the shareholder to whom the renunciation is made is deemed to have incurred the expenses in the amount of the renunciation on the effective date of the renunciation. Where a renunciation is made, the corporation making the renunciation is generally deemed not to have incurred the CEE. Only corporations that are "principal business corporations" may issue flow-through shares, and only where certain additional conditions are satisfied.

Normally, a corporation may renounce only the amount of CEE that has been incurred by it on or before the effective date of the renunciation. However, subsection 66(12.66) allows a corporation to renounce CEE that has not yet been

incurred by the corporation by deeming the corporation to have incurred the CEE on the last day of the year preceding the year in which the CEE was actually incurred. This look-back provision therefore provides an additional benefit for corporations and their flow-through share investors.

For a principal business corporation to be entitled to make look-back renunciations, it must meet the conditions set out in paragraph 66(12.66), including that the corporation deal at arm's length throughout the calendar year of the renunciation with the purchaser of flow-through shares to whom look-back renunciations of CEE not yet incurred were made.

One of the consequences to a corporation of making a look-back renunciation in respect of flow-through shares is that the corporation becomes liable for a tax under Part XII.6 of the Act. Simplified, in light of the accelerated deduction of CEE to the shareholder, this tax applies to the issuer for each month until the CEE is actually incurred. The Part XII.6 tax is deductible by the corporation in computing its income for Part I tax purposes.

In the *Tusk* case, the corporation was a principal business corporation engaged in the business of mineral exploration and development in Canada. In its 2002 to 2006 taxation years, the taxpayer had issued flow-through shares to both arm's length and non-arm's length shareholders, making look-back renunciations for CEE that had not yet been incurred by it. In this regard, the taxpayer had not been aware of the arm's length requirement in respect of its look-back renunciations.

The Minister denied the CEE deductions in the year of the look-back renunciations to the non-arm's length shareholders to whom renunciations had been made. As the taxpayer had not paid Part XII.6 tax, the Minister also assessed the taxpayer for such tax in respect of all of the look-back renunciations, including the renunciations that were invalid as they were made in favour of the non-arm's length shareholders. Although Part XII.6 tax would not have been payable in respect of the non-arm's length shareholders had look-back renunciations not been made in favour of them, the Minister assessed the tax as the provision required only that the corporation have "purported to renounce" CEE not yet incurred.

In her analysis, Miller J. noted that the central question was the meaning of the phrase "purported to renounce" in section 211.91 of Part XII.6. Miller J. noted that "[i]n interpreting the phrase "purported to renounce" in section 211.91, [. . .] the section must be interpreted with regard to its text, context and purpose, harmoniously with the scheme and object of the Act as a whole."

In rejecting the taxpayer's contention that the phrase "purported to renounce" should be interpreted to mean "has the effect of", the Court held that:

> [S]uch an interpretation of "purport" makes no sense when this definition is used within the entire sentence. It is clear that "an amount purported to be renounced in respect of expenses incurred or to be incurred" must refer to an amount "claimed" to be renounced or "intended" to be renounced whether the claim is true or not. This interpretation is supported by the French version of section 211.91. There, the phrase "censément renoncé" is used and it generally means "supposedly renounced" or "apparently renounced".

Miller J. held that the taxpayer's interpretation of section 211.91 would render the word "purported" redundant and thus would be contrary to the legislative intention.

The Court supported its interpretation of section 211.91 by pointing to the broader context of the scheme for flow-through shares as set out in the Act. Miller J. noted that the scheme regarding look-back renunciations is based upon a legal fiction which allows corporations, in effect, to back-date expenses to the year immediately prior to the year in which the expenses were incurred. The Court reasoned that the phrase "purported to renounce" referred not merely to expenses that are effectively renounced but to expenses "that the corporation claimed to renounce, whether the claim turns out to be true or not."

The Court noted that, according to the Technical Notes regarding section 211.91, the purpose of the Part XII.6 tax in respect of look-back renunciations was to compensate "the fisc for the acceleration of the deduction resulting from the application of subsection 66(12.66)".

As a result, notwithstanding that she recognized that her interpretation may be punitive where the renunciation is ineffective, Miller J. determined that the taxpayer in this case was liable for Part X11.6 tax on all look-back renunciations made in the taxation years in question, not simply those in respect of arm's length shareholders.

Although the *Tusk* decision has been appealed to the Federal Court of Appeal, the decision sends a cautionary note to corporate taxpayers (and their shareholders) with respect to the need for care in using flow-through shares to finance exploration and development projects.

— *Krupa Kotecha, Articling Student*

The Potential Perils of Rejecting a Settlement Offer Made in a Tax Appeal

***Golini v. The Queen*, 2016 DTC 1199 (Tax Court of Canada)**

The Tax Court (C. Miller J.) was asked to make a determination of costs award with respect to a dismissed tax appeal.

By way of background, Mr. Golini had participated in a series of very complicated transactions involving private corporations and the purchase of life insurance and annuities. These transactions were claimed by Golini to give rise to a substantial annual interest deduction by him on borrowed funds, and the acquisition by him of preferred shares with a substantial adjusted cost base ("ACB") and paid-up capital ("PUC").

The Minister took the position that the transactions constituted "smoke and mirrors" and assessed Golini on the basis of sham, adding to Golini's income for 2008 a dividend of $7,500,000 and disallowing claimed interest expense of $80,000.

Golini appealed the assessment to the Tax Court, where the Minister made a settlement offer which would have vacated the $7,500,000 added to Golini's income as a dividend, reduced from $6,000,000 to $1.00 the ACB and PUC of the preferred shares that Golini had acquired, and maintained disallowance of the $80,000 interest expense. Golini rejected the settlement offer and proceeded to trial.

While the Court rejected the Minister's claim that the transactions were a sham, the Court found that Golini had received a shareholder benefit of $5,400,000 (rather than the $7,500,000 dividend), but also found that Golini was entitled to an annual interest deduction of $80,000. As this result would have increased Golini's tax liability in 2008 beyond the amount assessed by the Minister (due to the dividend tax credit mechanism that had been available on the $7,500,000 dividend assessed), Golini's tax appeal was dismissed.

Given that Golini's appeal had been dismissed and that the Minister's settlement offer had been rejected, the Minister was seeking a lump-sum recovery of not less than $700,000 in costs pursuant to subsection 147(3.2) of the *Tax Court of Canada Rules* (the "Rules"). The amount comprised "substantial indemnity costs" equal to 80% of solicitor and client costs from the date of the settlement offer, party and party costs up to that date, and disbursements. Solicitor and client costs are generally the real legal costs incurred by a litigant whereas party and party costs are a much lower amount based upon a tariff set out in the Rules.

Pursuant to subsection 147(3.2) of the Rules:

> Unless otherwise ordered by the Court, if a respondent makes an offer of settlement and the appellant obtains a judgment as favourable as or less favourable than the terms of the offer of settlement or fails to obtain judgment, the respondent is entitled to party and party costs to the date of service of the offer and substantial indemnity costs after that date, as determined by the Court, plus reasonable disbursements and applicable taxes.

Relying on this provision, the Minister argued that the terms of the settlement offer were more favourable than the outcome of the dismissed appeal, and the Minister should be awarded substantial indemnity costs, equal to 80% of solicitor and client costs pursuant to subsection 147(3.5) of the Rules.

In contrast, Golini's position was that the Minister was not entitled to substantial indemnity costs because the judgment was more favourable to him than was the settlement offer. Golini argued that while the judgment would have included a $5.4 million shareholder benefit in his 2008 income, the judgment would be more favourable to him than the settlement offer given that it would have given him an $80,000 interest deduction for each subsequent taxation year and would preserve the $6,000,000 in PUC and ACB on the shares in question.

Given the magnitude of the substantial indemnity costs, the main issue before Miller J. was whether the Tax Court's appeal decision was as favourable as or more favourable than the offer of settlement, although Miller J. noted that even under the Rules in issue, he retained discretion in setting a costs award.

In determining that the decision of the Tax Court to dismiss Golini's tax appeal was not more favourable than the settlement award, Miller J. stated that "it belies logic that the Appellant would reject an offer so that he can proceed to trial to have his case dismissed." In Miller J.'s view, the immediate tax cost of the $7,500,000 dividend included in Golini's income is not offset by the value to him of the $6,000,000 ACB and PUC of the shares in issue and of the $80,000 in annual interest deduction in future years (which in any event were not, Miller J. noted, in front of the Tax Court on the tax appeal, such that it was not clear how the CRA would assess those years).

After concluding that the judgment was less favourable than the settlement offer and that the Minister was therefore entitled to substantial indemnity costs, Miller J. considered whether substantial indemnity costs should be awarded at the normal 80% rate where a decision in an appeal is less favourable than a settlement offer that was rejected. Some

of the factors under subsection 147(3) of the Rules that the court may consider include the result of the proceeding, the conduct of the parties, the amount in issue, the importance of the issue, the volume of work, and the complexity of the issue.

In reaching his decision, Miller J. relied on the result of the proceeding and the conduct of the parties. While the result of the decision was an appeal dismissal, it was not based on the Minister's primary argument of sham, but rather based on a determination that a shareholder benefit had resulted from the transactions in issue. As the Minister had not succeeded in the primary argument as to sham, Miller J. gave some weight to this factor in reducing the substantial indemnity costs. Miller J. also found that the Minister acted improperly in not clearly outlining to Golini prior to an appeal the "full nature of the sham argument." Miller J. therefore reduced the substantial indemnity costs award from 80% to 60%.

As a result, the taxpayer was required to pay more than $500,000 in costs to the Minister, approximately $440,000 of which were for substantial indemnity costs. *Golini* serves as a reminder to the parties to a tax appeal of the importance of carefully determining whether to accept or reject a settlement offer.

The decision also illustrates that the Tax Court will consider improper, vexatious, or unnecessary conduct by the other party in its assessment of costs. While Miller J. found that the conduct of the parties was not uncommon as part of the procedural wrangling and litigation tactics, more egregious behaviour may rise to a level of incivility which may impact an award of costs.

— *Yaroslavna Nosikova, Articling Student*

Federal Court Decision Creates Uncertainty Regarding Existence of Common Interest Privilege in Transactional Context

***MNR v. Iggillis Holdings Inc.*, 2016 DTC 5141 (Federal Court of Canada)**

The *Iggillis* case is an important decision concerning common interest privilege. It will have significant implications to commercial parties to a transaction that wish to share legal advice received from their respective counsel.

To understand the significance of the case, it is necessary to understand that solicitor-client privilege protects from disclosure communications between a lawyer and a client, where such communication is made for the purposes of giving or seeking legal advice and is intended by the client to be confidential. The doctrine of common interest privilege, while not a separate type of privilege itself, may serve as an exception to the waiver of privilege that takes place when privileged communication is shared with a third party (given that the disclosure of such communication to a third party is inconsistent with the notion that the information is intended to be confidential). Prior to the decision in *Iggillis,* several Canadian trial and appellant courts had recognized that unaffiliated parties acting with the common interest of closing a transaction may, under the doctrine of common interest privilege, be permitted to share privileged materials *without* waiving the privileged nature of the communication.

In the case at bar, the Minister sought to obtain access to a legal memorandum that addressed the tax consequences arising from a series of commercial transactions. The memorandum was prepared by counsel for Abacus Capital, an affiliate of the purchaser, with considerable assistance from counsel for the other party involved in the transaction. The memorandum was subsequently shared with the taxpayer (the vendor in this instance). Given that structuring in a tax-efficient manner was necessary for the transactions to proceed, the memorandum itself was crucial to the execution of the deal. The Minister contended that the transactions entered into by the taxpayer and the purchaser were intended to avoid payment of the tax triggered by the sale of the corporate partners' assets, and that the contents of the memorandum would serve to support such an intention.

Annis J. noted that the memorandum contained legal advice provided to the parties by their respective counsel in the strictest confidence. As a result, at first instance the memorandum was a form of communication protected from disclosure under solicitor-client privilege. The next and more difficult issue pertained to whether the privilege over the communication was waived or, in the alternative, was protected by the doctrine of common interest privilege.

In considering the latter issue, the Federal Court distinguished advisory common interest privilege ("CIP"), where parties' have *separate* counsel that together share a common interest in advancing a transaction, from joint client privilege ("JCP"), where multiple parties receive legal advice from a *single* law firm. On the basis of this and other distinctions, Annis J. held that common interest privilege was not an acceptable extension of joint client privilege:

> All communications in a JCP situation are within the solicitor-client relationship and the privilege is coherent with the SCP [solicitor-client privilege] doctrine. Conversely, the communications in an allied lawyer CIP situation are not limited to those between a lawyer and his or her client seeing as the lawyer does not have a

> solicitor-client relationship with the other parties who have their own separate counsel. Therefore, to apply the doctrine of SCP to communications in the allied lawyer setting is to protect communications that are not solely between an attorney and the attorney's client and therefore not essential to the relationship. Such an application of the doctrine of SCP is contrary to its own *raison d'être*, that is encouraging full and frank disclosure of information by the client to the lawyer and by its essential nature being to the benefit of the administration of justice. (Emphasis in original.)

The Court also noted that the differences between joint client privilege and common interest privilege supported a departure from the precedent in *Pitney Bowes of Canada Ltd*. (2003 DTC 5179 (FCC Trial Division)), which Annis J. identified as having been decided under joint client privilege circumstances.

Another important distinction drawn by the Court related to litigation common interest privilege (which arises in the context of pending or anticipated litigation) and advisory common interest privilege (which arises in the context of a commercial transaction). On the basis of the differences between the two types of common interest privilege, the Court concurred with certain US jurisprudence (and in particular the result in *Ambac Assurance Corp v. Countrywide Home Loans Inc*. (27 NY (3d) 616 (CA 2016)), which held that advisory common interest privilege, unlike litigation privilege, was inconsistent with solicitor-client privilege.

In addition to the American cases and commentary drawn on to support the Court's analysis, Annis J. emphasized several negative policy consequences in favour of the Court's conclusion that common interest privilege should not be extended in the transactional context. Primarily, the Court expressed concern that the expansion of privilege in this context would allow parties to improperly shield communications relevant to the proper administration of justice. On the other hand, Annis J. noted that the benefits of extending solicitor-client privilege to include common interest privilege did not provide a sufficient rationale for sanctioning such an extension:

> [T]he Court concludes that there is little or no reliable evidence that advisory CIP is supported by the economic and social values of the commercial transactions it is said to foster. Most commercial transactions would be concluded without the requirement of CIP based on traditional profit motives that have always motivated their formation. Those that do require the privilege are transactions that present a high risk of anticipated litigation, where the application of CIP undermines the administration of justice in the area of commercial transactions, tending towards less compliance with the law. Many of the cases described in the jurisprudence where a CIP is advanced involve commercial transactions of no, or even detrimental value to society. In any event, the only evidence on the effect of CIP, apart from the opinions of judges, demonstrates that the absence of a CIP has had no impact on the conclusion of commercial transactions or any failure to comply with the law.

As a result, the Court concluded that the memorandum at issue was not protected by advisory common interest privilege and, consequently, could not be shielded from disclosure. Given *Iggillis*, there is significant uncertainty regarding the circumstances, if any, under which advisory common interest privilege can serve to protect communications arising in the transactional context.

Besides the profound implications for counsel acting in commercial deals in which legal advice might be shared between parties represented by different lawyers, the *Iggillis* case is interesting in several other respects. First, the decision appears to characterize common interest privilege as a separate type of privilege (essentially as an expansion or new and distinct subset of solicitor-client privilege) as opposed to an exception to the waiver of privilege that *already exists* with respect to confidential communication. Secondly, although the Court in *Iggillis* does rely on American jurisprudence and commentary to support its rejection of advisory common interest privilege, the decision does not address the underlying doctrinal differences between solicitor-client privilege in the two jurisdictions, and thus does not fully consider the existence of a rationale for advisory common interest privilege in the Canadian transactional context. Lastly, the decision seems to accept, almost without question, the Minister's contention that commercial entities will inappropriately employ the doctrine of common interest privilege for the purposes of sheltering evidence of tax avoidance, which would thus create obstacles to the proper administration of justice.

As *Iggillis* has been appealed to the Federal Court of Appeal, it has yet to be seen whether this contentious decision will be upheld. Until then, the uncertainly over the existence of privilege in the transactional context suggests that both parties and their counsel should avoid presumptions of confidentiality in respect of the communications between them.

— *Krupa Kotecha, Articling Student*

Nothing Special About Computation of Arrears Interests Under a GAAR Reassessment

***Quinco Financial Inc. v. The Queen*, 2016 DTC 1175 (Tax Court of Canada)**

In this decision, the Tax Court of Canada considered whether, in the case of a reassessment that produces additional tax owing based on the application of the general anti-avoidance rule ("GAAR"), arrears interest begins to accrue from the appellant taxpayer's balance-due date for the relevant taxation year, as would be the case with any other reassessment, or from the date of the GAAR assessment, on the basis that the additional tax liability associated with the application of the GAAR only arises when the Minister issues the reassessment to recast the tax consequences from the relevant transactions from the consequences as they stood at the time the taxpayer filed the tax return for the year.

The issue was brought before the Tax Court under a rule 58 motion for a determination of a question of mixed fact and law. The notice of reassessment giving rise to the question was issued on April 7, 2009, reflecting a reassessment of the taxpayer's liability for its taxation year ending August 27, 2004. Based on the Minister's decision to apply GAAR to deny certain capital losses, the Minister assessed arrears interest payable by the taxpayer beginning on October 28, 2004, the taxpayer's balance-due date for the year and some four and a half years prior to the date of the reassessment. The taxpayer objected to the reassessment by way of a notice of objection dated June 19, 2009.

The taxpayer raised three arguments for why interest on a GAAR assessment should only begin to accrue on the date the assessment was issued, rather than on a taxpayer's balance-due date.

The taxpayer first argued that the tax liability and reassessment methodology under the GAAR should be treated as distinct from other taxing provisions under the *Income Tax Act* (the "Act"), based on the fact that the GAAR overrides the standard of strict compliance and technical conformity in favour of an object, spirit, and purpose approach to assessing tax. The taxpayer reasoned that the GAAR does not recharacterize a transaction but instead, on assessment, imposes tax consequences by nullifying the benefits associated with a transaction.

While the Tax Court acknowledged that the GAAR differs from other taxing provisions, it found that the GAAR is nonetheless part of the Act and, in order to read the Act as a coherent whole, courts should, to the best extent possible, try to give contemporaneous effect to both the GAAR and other provisions of the Act. In this regard, the Tax Court found that the GAAR does not create an assessment divorced from other provisions of the Act, but instead depends on the very textual, contextual, and purposive nature of the provisions with which it interacts.

Despite the onus requirements and limitations related to its application, the Tax Court held that the GAAR does not function by creating an independent, stand-alone assessment or by recharacterizing a transaction; it instead considered the GAAR to be incorporated by reference into an assessment as part of the taxpayer's liability under the Act generally.

The taxpayer's second argument concerned the difficulty of self-assessing its own liability under the GAAR. In relation to a non-GAAR provision, a taxpayer might self-assess to avoid arrears interest by filing a tax return reporting a higher amount of tax owed corresponding to the application of the provision at issue. By doing so, the taxpayer could immediately file a notice of objection to the original assessment issued by the Minister (accepting the tax return "as-filed") to put into issue the uncertain tax position. This would allow the taxpayer to avoid the exposure to potential arrears interest covering several years, as was the case for the appellant taxpayer. However, in the case at bar, the taxpayer argued that the GAAR makes such a practice impossible based on the fact that only the Minister can determine if there has been abuse or misuse of a provision and only the Minister can determine the reasonable circumstances leading to the denial of a tax benefit.

The Tax Court rejected this argument, finding that the different components, onuses, and burdens under the GAAR do not overly mystify the standard required to be adhered to by a taxpayer to the point of vagueness. Reflecting the practical reality of tax planning, the Tax Court noted that all aggressive or complicated tax planning involves some level of uncertainty, but typically arises from well-planned, documentary-intensive steps involving advice from tax planners who, in their approach to the GAAR, like any other provision of the Act, will weigh the consequences of the GAAR on a reassessment. The Tax Court saw no reason why the application of the GAAR, as opposed to any other provision, prevented the taxpayer from self-assessing.

The taxpayer's third argument raised certain matters of statutory interpretation in an attempt to prove that if Parliament had intended for arrears interest on a GAAR assessment to accrue from the taxpayer's balance-due date, it would have enacted express language to that effect. As evidence, the taxpayer argued that the Minister's discretion over the GAAR makes it analogous to certain penalty provisions under the Act and, as a result, the start of the accrual period for arrears interest under the GAAR should be similar to that of paragraph 161(11)(*c*) of the Act, which sets the commencement date for arrears interest on certain penalties to the date of the assessment under which the penalty is assessed.

The Tax Court also rejected this argument. By applying a plain language interpretation of subsection 161(1) of the Act, the Tax Court found no reason to carve GAAR-based assessments out of the normal requirement that interest accrue after a taxpayer's balance-due date where a taxpayer's tax payable exceeds amounts paid on account of tax for the year. Contextually and purposively, the Tax Court held that deferring interest until after an assessment has been issued would allow a new deferral advantage for a taxpayer who had carried out an abusive avoidance transaction. In the Tax Court's view, this would be an absurd consequence for a provision intended to nullify the tax benefits of abusive transactions. The Tax Court further suggested that the words "other amount payable" in the definition of "tax benefit" under subsection 245(1) of the Act would be wide enough to encompass the interest in question.

The outcome in this case confirms prior jurisprudence on GAAR reassessments, which should not be considered to be different from other reassessments for the purposes of accrued interest. Both parties in the case made reference to the decision of Justice Hogan in *J.K. Read Engineering Ltd.* (2014 DTC 1216 (TCC)), which reached much the same conclusion.

On September 29, 2016, the appellant filed a notice of appeal of the decision.

— *Justin Shoemaker*

Court Prefers CRA's "Weak" Evidence Over Testimony of Fraudster Taxpayer

***Mpamugo v The Queen*, 2016 DTC 1176 (Tax Court of Canada)**

The *Mpamugo* case provides some insights into the factors a court will consider when making a determination as to whether or not the Minister mailed a Notice of Assessment in instances where a taxpayer asserts that it was not sent.

The taxpayer in this case was an individual who was tried and convicted for his role in running a college in Ontario that assisted non-students with fraudulently obtaining government-sponsored student loans. The taxpayer was also convicted of obstruction of justice stemming from the creation of false documents after the fraud investigation began.

The Minister reassessed the taxpayer's 1998 to 2002 taxation years, producing tax on approximately $6.8 million dollars of additional income. The taxpayer subsequently filed Notices of Appeal with the Tax Court of Canada contesting the reassessments.

Under the *Income Tax Act* (the "Act"), in order to file an appeal with the Tax Court, the taxpayer must have previously filed a timely Notice of Objection with the Minister. In this case, the Minister brought a motion to dismiss the taxpayer's appeal on the basis that the taxpayer had not filed timely Notices of Objection to any of the subject reassessments. Curiously, the taxpayer also brought a motion to quash his own appeals on the basis that the Notices of Reassessment were never sent to him; his rationale was that, since there was nothing to which he could object, it was impossible for him to have met the preconditions for filing a Notice of Appeal and, as a result, his appeal should be quashed.

In setting out the Tax Court of Canada's reasons for its decision, Graham J. began by considering the taxpayer's allegation that the Notices of Reassessment were never sent to him. As outlined in the jurisprudence, Graham J. noted that a taxpayer may assert either that he or she did not receive a Notice of Assessment (and thus believes that it was not mailed), or that a Notice of Assessment was mailed to the wrong address and thus, in effect, not mailed. The burden then falls on the Minister to introduce sufficient evidence to prove, on a balance of probabilities, that the Notice of Assessment was indeed mailed to the taxpayer or mailed to the address that the CRA properly had on file. The Tax Court affirmed that the credibility of the taxpayer is to be taken into account during the latter stage. Consequently, the initial burden fell to the Minister to adduce sufficient evidence to show that the Notice of Assessment was mailed to the taxpayer.

Graham J. noted that the test to prove mailing of a Notice of Assessment (on a balance of probabilities) is not burdensome. Subsection 244(1) of the Act allows a CRA officer to provide as evidence, absent proof to the contrary, an affidavit stating that the officer has charge of the appropriate records and has knowledge of the practices of the CRA, that he or she has examined those records, and that those records show that a Notice of Assessment was mailed. Although the Tax Court held that the affidavit which was relied on by the Minister as evidence did not comply with subsection 244(10) on the grounds that portions of the affidavit were based on hearsay, the affidavit was nonetheless considered by Graham J. alongside other evidence provided by both parties. The admission of this evidence was based on Rule 72 of the *Tax Court of Canada Rules (General Procedure*), which permits affidavit evidence based on information and belief to be admitted if the source of the information and the fact of the belief are stated.

The CRA officer who provided the affidavit had consulted with other officers that, by the nature of their positions, were

familiar with the normal procedure followed by the CRA in the mailing of Notices of Assessment. Based on the officer's recitation of the CRA's checks and balances to ensure that such Notices of Assessment were printed (as had been relayed to him by other officers), Graham J. found the affidavit to be weak evidence that the CRA anticipated printing the Notices of Reassessment and mailing them to the taxpayer. Furthermore, the Court concluded that the correct address would have appeared on the Notices, based on the fact that the CRA officer providing the affidavit testimony had personally reviewed the CRA's mailing address history report (and testified to this effect).

Moreover, the Tax Court did not accept the taxpayer's assertions that he did not receive the Notices of Reassessment because the CRA failed to follow his oral instructions to change his mailing address to the various detention centres at which he was held. In addition to the logical inconsistencies inherent in the taxpayer's claims, Graham J. found the taxpayer to be lacking in credibility, also finding both his oral and affidavit testimony to be full of inconsistencies, exaggerations, and omissions. Consequently, Graham J. held that, although he could not conclude that the Notices were indeed received, there was no evidence from which he could infer the Notices were not mailed.

Graham J. noted that, in other instances where the Court had concluded that the Minister failed to prove mailing, the Minister either had no evidence of mailing or the Minister's weak evidence was outweighed by the taxpayer's credible testimony that he or she did not receive the Notice in question. This was not the situation in the case at bar. On the basis of the conclusion that the Notices were (more likely than not) mailed, the Minister's motion to quash the appeal was allowed.

The *Mpamugo* case is instructive as to the various points in the deliberation process at which the Court will take into account the credibility of a testifying individual when making a determination as to whether a Notice of Assessment was mailed, and the burden of proof that is accordingly placed on the Minister. The Tax Court of Canada's decision has been appealed to the Federal Court of Appeal.

— *Krupa Kotecha,Student-at-Law*

Litigant Unable To Obtain Order To Have Minister Pay Funds That Might Have Been Improperly Garnished Into Court

***Linda F. Dunn et al. v. Attorney General of Canada*, 2016 DTC 5118 (Ontario Superior Court of Justice)**

This proceeding was an application before the Ontario Superior Court of Justice for an order to have the Minister pay into court funds that the CRA garnished from TD Waterhouse Canada on account of outstanding tax debts of the account holder, Mr. Egan.

The applicants' claim to the garnished funds was derived from litigation against Mr. Egan in which they alleged that Mr. Egan had misappropriated funds from an estate of which they were beneficiaries. In the course of their legal proceeding against Mr. Egan, the applicants obtained a court order requiring TD Waterhouse to liquidate approximately $350,000 of securities from Mr. Egan's TD Waterhouse trading accounts and pay the proceeds into court pending resolution of the litigation between the applicants and Mr. Egan. The CRA's garnishment order to TD Waterhouse Canada was issued and fulfilled before the date on which the applicants obtained their court order recovering assets in Mr. Egan's TD Waterhouse accounts. As the CRA's garnishment order depleted the balance in Mr. Egan's TD Waterhouse account, the applicants' order against TD Waterhouse was ineffective in achieving its purpose of preserving assets to satisfy a potential judgment against Mr. Egan. The application against the Minister in this proceeding was a curious attempt by the applicants to require the Minister to recognize the applicants' order concerning Mr. Egan's account with TD Waterhouse even though the CRA's garnishment order was issued more than a year before the applicants' order.

The Minister's garnishment order was a Requirement to Pay, presumably issued pursuant to subsection 224(1) of the *Income Tax Act* (Canada). Although TD Waterhouse Canada had received and complied with other court orders requiring it to pay funds form Mr. Egan's trading account into court in connection with other persons who had litigation claims against Mr. Egan, those orders were issued before the date of the Requirement to Pay.

As for the applicants' litigation, Mr. Egan was the executor of an estate whose beneficiaries included the applicants. The beneficiaries were successful in having Mr. Egan removed as executor and sought recovery of amounts that were held in Mr. Egan's TD Waterhouse account on the basis that those assets were or could be traced to misappropriated estate property.

Having regard for the nature of the applicants' claim against Mr. Egan, it is easy to see why they felt that the CRA's Requirement to Pay should not thwart their right to recover the assets in Mr. Egan's TD Waterhouse trading accounts should their right to recover against Mr. Egan be ultimately proven in court. However, as discussed below, the Court dismissed the application.

The Court acknowledged that, had the applicants sought an order for funds in Mr. Egan's TD Waterhouse accounts to be paid into Court before the balances were garnished by the CRA, the Court could have issued the order. But now that the garnished funds were in the hands of the Crown, the Court had difficulty seeing how the granting of the order against the Minister aligned with the purpose of Rule 45.02 of *Rules of Civil Procedure* (Ontario), which is to preserve a specific fund pending a determination of ownership. Setting aside a threshold issue arising from the fact that neither the CRA nor the Federal Crown were parties to the litigation between the applicants and Mr. Egan, the Court noted that the garnished funds were no longer an identifiable fund, as they had simply been added by the Receiver General to the Consolidated Revenue Fund. But more importantly, had the Minister been ordered to pay funds into Court, those funds would be no more secure in the hands of the Court than they would be in the hands of the Receiver General.

At the hearing of the application, the Minister also raised a jurisdictional issue with the relief sought by the applicants based on the argument that section 18 of the *Federal Courts Act* grants the Federal Court the exclusive jurisdiction to order the type of relief sought by the applicants, which the Minister characterized as injunctive in nature. As the Court had decided to deny the application for the reason discussed above, the Court chose not to make a finding on the jurisdictional issue. However, the Court directed the Minister's attention to subsection 17(2) of the *Federal Courts Act*, which gives provincial superior courts concurrent jurisdiction with the Federal Court in cases where property of any person is in possession of the Crown.

At the end of the day, the applicants are not entirely without a remedy against the Minister, as they could add the Minister and the CRA as parties to their litigation against Mr. Egan. They simply will not have the funds on deposit with the Court if they are successful and will need to take additional steps at that time to recover funds from the Crown.

— *Yaroslavna Nosikova, Articling Student*

RECENT CASES

Appeal court orders new trial for taxpayer acquitted of failing to file tax returns

The taxpayer was charged with fourteen counts under section 238(1) of the *Income Tax Act*, relating to his failure to file tax returns for several corporations. The trial judge held that the offences in question were strict liability offences for which the only available defence was one of due diligence. He concluded that, given his circumstances, the accused had exercised due diligence in attempting to comply with notices requiring him to file tax returns for the corporations in question, and an acquittal verdict was given. The Crown appealed from that acquittal, arguing that the trial judge had erred in finding that the accused exercised due diligence. It also sought to introduce new affidavit evidence showing that the returns which the accused had testified were filed actually remained outstanding.

The appeal was allowed, and a new trial ordered. The appellate Court first considered the question of whether the new evidence relating to tax filings should be introduced. The test for such admission required that the evidence in question be admissible, that it be sufficiently cogent to warrant its admission because it might have resulted in a different verdict and, finally, that there must be a reasonable explanation for why the evidence was not tendered at trial. The Court noted that there was an element of confusion at the trial over the question of whether the returns in question had been filed. As well, the trial judge had found the defendant's evidence on that question to be credible, and gave weight to his representation that the returns had been filed. In the appellate Court's view, if the representation made was demonstrably false, it might well have affected the findings made at trial, and it concluded that a new trial was required in order to test that evidence. The Court then considered the issue of due diligence and held that the trial judge had erred in his consideration of such issue. Specifically, the judge failed to take into account the fact that the defendant had previously been challenged by the Canada Revenue Agency for his failure to file corporate tax returns, and that he had been warned by the Agency about such failure for several months prior to the issuance of a formal demand to file. In the appellate Court's view, the defendant's previous knowledge was relevant to any assessment of whether he acted with due diligence, and such previous knowledge should have been taken into account by the trial judge. The Court concluded that the acquittals should be set aside, the new evidence should be admitted, and that a new trial should be held, limited to the question of due diligence.

The Queen v. Allard

2016 DTC 5136

Taxpayer not entitled to order cancelling tax certificate registered against his property

The Minister assessed the taxpayer under section 160 of the *Income Tax Act* (the "Act") for tax owing by his father when the latter transferred property to him for less than its fair market value. The Crown registered a certificate of tax owing against the property and this resulted in a memorial issued under section 223 of the Act. During 2012, the taxpayer's representative obtained from the Land Registry Office a copy of the Crown's lien against the property in the amount of $69,329.75, but his accountant obtained a Client Summary from the CRA website on May 10, 2012 stating that the taxpayer's account balance was zero. The taxpayer sold the property on December 17, 2012, but a $150,000 holdback was set aside pending resolution of the discrepancy between the Crown's lien registered against title to the property and the CRA's Client Summary. Arguing that the Crown was estopped from enforcing the memorial because of the CRA's misrepresentation of fact in its Client Summary, the taxpayer applied to the Federal Court for an order cancelling the memorial which had been issued under section 223.

The taxpayer's application was dismissed. As the parties agreed, estoppel requires: (a) an unambiguous and unequivocal representation to induce a course of conduct; (b) an act or omission resulting from that representation; and (c) detriment to the person to whom the representation is made (see *Canadian Superior Oil Ltd. v. Paddon-Hughes Development Co.*, [1970] SCJ No 48). Estoppel could not be utilized in this case, however, to erase the taxpayer's outstanding tax debt, since estoppel cannot be used to remove an obligation to obey a statute or, as in the present proceedings, to pay a valid and binding tax assessment (see *Maritime Electric Co. v. General Dairies Ltd.*, [1937] 1 DLR 609). In addition, the taxpayer failed to establish estoppel by representation in accordance with the three criteria in the *Canadian Superior Oil* case.

Vallelunga v. The Queen

2016 DTC 5132

Court refused to release funds from bankrupt's RDSP to her creditors

The bankrupt, A, a 53-year-old person with one or more severe and prolonged impairments in physical or mental function, qualified for the disability tax credit under section 118.3 of the *Income Tax Act* (the "ITA"). She held a Registered Disability Saving Plan ("RDSP") containing $6,800 which had come from her parents in 2012. She had contributed nothing to the RDSP, but the balance of the $32,250 held in the Plan had come from Government of Canada grants under the *Canada Disability Savings Act*, amplified by some market growth. The respondent bank was the trustee of A's RDSP. A's Trustee in bankruptcy applied to the Supreme Court of British Columbia for an order declaring whether or not the funds in A's RDSP (of which she was the sole beneficiary) were exempt from seizure under subsection 67(1) of the *Bankruptcy and Insolvency Act* (the "BIA"). The parties agreed that there was no specific provision of the BIA or the ITA governing this exemption issue, but that the Court had the discretion to determine it.

Under the trust instrument governing A's RDSP, no funds could be paid out to her creditors or to her to satisfy those creditors, and the Trustee was bound by this restriction as well. Under the trust instrument, however, the Court had discretion to release funds to satisfy A's creditors. However, in exercising this discretion, the Court should be guided by what was just and equitable in the particular circumstances. The underlying purpose of an RDSP is to ensure that severely disabled persons are able to save for their retirement, and there is an even greater societal interest in preserving the integrity of such a plan than in the case of an RRSP. Releasing funds from A's RDSP for the benefit of her creditors in this case, moreover, would cause three dollars for each one dollar paid out to be refunded to the Government of Canada. This result would severely prejudice A while according minimal benefit to her creditors. And refusing to release funds from A's RDSP to her creditors in this case would not erode public confidence in the bankruptcy scheme. As a result of the foregoing findings it would not be fair and equitable to release such funds.

Re Alary

2016 DTC 5123

Appeal from denial of ITC dismissed where required form not timely filed

On June 30, 2010, the taxpayer filed a completed T661 form to claim scientific research and experimental development ("SR&ED") expenditures. The Minister accepted the claim for SR&ED expenditures but denied the taxpayer's claim for investment tax credits ("ITCs") in respect of those SR&ED expenditures, as the taxpayer had not filed the prescribed form for claiming such ITCs on or before the June 30 deadline. The taxpayer appealed from the denial of the ITC claim, but that appeal was dismissed by the Tax Court of Canada. The taxpayer then appealed from that dismissal to the Federal Court of Appeal.

The appeal was dismissed. Section 127(9) of the *Income Tax Act* provides that no amount shall be payable in respect of an ITC if the taxpayer fails to file a prescribed form containing prescribed information in respect of the amount. The Tax Court of Canada had held that no ITCs were payable due to the taxpayer's failure to file such prescribed information in prescribed form by the statutory deadline. The Federal Court of Appeal held that the only issue on the appeal was whether the Tax Court judge had erred in concluding that the filing of such prescribed form was the only way in which an ITC could be claimed, and it concluded that the Tax Court had made no reviewable error in so finding. The appellant had argued that, notwithstanding its failure to file the prescribed form by the deadline, the Minister nonetheless had received, in other forms filed by the appellant, all of the information needed to calculate the available ITC. The respondent took the position, and the appellate Court agreed, that the appellant's argument was an attempt to convert information provided on other forms into a stand-alone application for ITCs. The Court held that it was a taxpayer's responsibility to inform the Minister whether it was claiming an ITC in relation to SR&ED expenditures and the way to do so was to file the prescribed form containing the prescribed information by the prescribed deadline. The appellant had not communicated its intention of claiming ITCs in the manner required by the statutory deadline, and its failure to do so was fatal to its appeal of the Minister's reassessment.

Easy Way Cattle Oilers Ltd. v. The Queen

2016 DTC 5130

Assessment including assessed interest not constituting nil assessment

A reassessment was issued by the Minister, which included an amount from a registered education savings plan ("RESP") in the taxpayer's income, together with offsetting education-related deductions, which also included an amount for assessed interest. The taxpayer appealed from that assessment and the Minister brought a motion seeking to have the appeal quashed, on the basis that the taxpayer was contesting a *nil* assessment.

The motion was dismissed. The Court held that the reassessment issued by the Canada Revenue Agency ("CRA") included an amount of interest and that such interest, as opposed to post-assessment accrued interest, formed part of the assessment. Appellate jurisprudence provides that a taxpayer may challenge the tax, interest, or penalties assessed in a year. Where an appeal is brought, it can proceed with respect to any aspect of the assessment and is not limited to the interest assessed. While the amount of interest assessed was very small, it was not *nil*, and the CRA had chosen to add such interest amount to the reassessment. As the reassessment was therefore not a *nil* assessment, the appeal could proceed.

Shreedhar v. The Queen

2016 DTC 1203

Taxpayer prohibited from acting as agent without Court permission

The Court brought a motion to prohibit the taxpayer from appearing as an agent without first obtaining permission. While there is no specific legislation or rules providing for such action, the Court, as a statutory court, has the power to do this as part of its inherent power to control its own process. The Court's concern was raised by the conduct of the taxpayer in his appearances as agent for six taxpayers.

To ensure the proper administration of justice, an order was issued prohibiting the taxpayer from acting as agent without first receiving written court permission. His application for permission may not exceed ten pages in length, he can still appear on his own behalf, and a copy of the order is to be given to all former clients. An order prohibiting an agent from acting will only be made to protect the proper administration of justice and not simply if the Court feels that a taxpayer would be better represented by someone else. Factors to consider in such an order include whether the agent's behaviour causes or facilitates (a) an abuse of the court process, (b) scandalous or frivolous arguments, (c) appeals with no reasonable grounds for appeal, (d) contempt of court, or (e) bringing the administration of justice into disrepute. Other factors include exhibiting an unacceptable ignorance of the law, threatening or abusive behaviour, taking undue advantage of clients, and not acting in an ethical or honourable manner. The taxpayer as agent raised pseudo-legal commercial arguments which were consistently rejected. He denied the jurisdiction of the Court and argued his clients were not subject to taxation. It was troubling that he continued to introduce these arguments to his clients even after they had been rejected. Clients who dismissed him subsequently received reduced assessments and more favourable results. He intimidated his clients, took payment up front, and refused to have his clients testify or introduce other evidence, which might have ensured greater success for them. Agents are only allowed to appear in Informal Procedures whose monetary cap is $25,000. The taxpayer had several clients whose monetary amounts exceeded $25,000. By hiring the taxpayer as agent, they capped their potential savings. In two instances where the taxpayer appeared as agent he started off by disputing the jurisdiction of the Court. When informed by the Court that

the clients could continue the matters without the agent, they nevertheless left the Court with the taxpayer leading to adverse results. Upon returning to the Court later, they testified that they felt embarrassed and realized their mistake in hiring the taxpayer. They felt coerced by him and made substantial payments to him up front. While they should have realized that the taxpayer's promise that they owed no tax was too good to be true, that does not excuse the taxpayer's behaviour. If the taxpayer would be allowed to continue acting as an agent, court time and client time would be wasted as he would continue to take advantage of clients' naivete and desperation.

In the Matter of Chris Shannon

2016 DTC 1204

TAX NOTES

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For Wolters Kluwer Canada Limited

Tara Isard, Senior Manager, Content
Tax & Accounting Canada
(416) 224-2224 ext. 6408
email: Tara.Isard@wolterskluwer.com

Natasha Menon, Senior Research Product Manager
Tax & Accounting Canada
(416) 224-2224 ext. 6360
email: Natasha.Menon@wolterskluwer.com

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Wolters Kluwer Canada Limited
300-90 Sheppard Avenue East
Toronto ON M2N 6X1
1 800 268 4522 tel
1 800 461 4131 fax
www.wolterskluwer.ca

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