Tax Notes

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RECENT INCOME TAX INTERPRETATIONS

Tuition Carry-Forward Pool After Departure from Canada

The CRA was asked if an individual whom had left Canada (and whom had presumably ceased to be a Canadian resident for tax purposes) could still use the carryforward pool of his tuition, education, and textbook tax credits (earned while he was still a Canadian resident) upon his return to Canada (and, presumably, after becoming a Canadian resident again) at a later date.

The CRA confirmed that the individual could use the pool of tax credits at the later date since the pool does not expire when an individual becomes a non-resident. The pool is calculated under subsection 118.61(1) of the *Income Tax Act*, and deducted under subsection 118.61(2) as the lesser of two amounts:

- Unused tuition, education, and textbook tax credits carried forward form previous year.
- Student's Part I tax for the year, if only certain non-refundable credits were claimed.

Note that, since 2017, the education and textbook amounts cannot be used to claim the tax credit, but can be carried forward indefinitely and used in a future taxation year to claim such credit.

— External Technical Interpretation, Business and Employment Division, March 11, 2019, Document No. 2018-0784491E5

Eligible Medical Expenses — Pharmacogenomics Test

The situation the CRA was asked to consider involved the cost of consultation services provided by a pharmacist, which included the cost of a pharmacogenomics test. Although this is not clearly indicated in the document, the services appear to have been rendered in British Columbia, since the CRA noted that pharmacists in that province are recognized as medical practitioners for the purpose of paragraph 118.2(2)(*a*) of the *Income Tax Act* (the "Act"), and amounts paid to them for their services were eligible for the medical expense tax credit ("METC"). The CRA was asked if the amounts paid for the services rendered by the pharmacist and the pharmacogenomics test would be eligible for the METC. Relying on the wording of paragraphs 118.2(2)(*a*) and 118.2(2)(*o*) of the Act, and paragraphs 1.26 and 1.27 of Income Tax Folio S1-F1-C1, the CRA confirmed that the

amounts would qualify for the METC, provided all the requirements in those two provisions were met. However, the CRA noted that the question of whether expenses qualified for the METC was one of fact.

— *External Technical Interpretation, Business and Employment Division, January 9, 2019, Document No. 2018-0760741E5*

Taxability of Benefits Received Under Student Loan Program

The CRA was asked if the following student benefits would be taxable in the following scenarios:

(1) The benefit is received in the form of an interest-free student loan.

(2) The benefit is received in the form of the application, to the principal balance of a student loan, of an amount equivalent to the interest paid by the debtor of the loan.

The CRA confirmed that, in both situations, the benefit would not be taxable. In the first situation, the benefit received from the interest-free loan is not taxable as a scholarship, bursary, or similar form of assistance taxable under paragraph 56(1)(*n*) of the *Income Tax Act* (the "Act"), and is not taxable under subsection 80.4(1) since it is not related to a previous, current, or future office of employment. Furthermore, the benefit is not income under any other source under the Act, and thus is not taxable. In the second situation, the amount applied to reduce the principal balance of the student loan is not a scholarship, bursary, or any other source of income under of the Act and is therefore not taxable.

— *Internal Technical Interpretation, Business and Employment Division, November 19, 2018, Document No. 2018-0777321I7*

Deductibility of Expenses Incurred by Elected Officials

The Canada Revenue Agency ("CRA") was asked if legislative assembly and elected municipal officers were allowed to deduct certain expenses under section 8 of the *Income Tax Act* (the "Act"). Before 2019, non-accountable allowances paid to elected officials to cover expenses connected with carrying out their work-related duties were not taxable if they did not exceed 50% of their salary. However, these types of allowances are now fully taxable. The CRA confirmed that the elected officials are now permitted to deduct certain expenses under paragraphs 8(1)(*h*) or 8(1)(*h*.1), subparagraphs 8(1)(*i*)(ii) or 8(1)(*i*)(iii), or subsection 8(13)of the Act, provided they meet the following conditions:

- They incur the expenses in the course of performing their office duties.
- The expenses are specifically identified in section 8 of the Act.
- The officials are required by written or verbal contract to incur those expenses.
- They must keep Form T2200 on file, duly signed by their employer.

A municipality may certify the conditions of the office by completing and signing Form T2200 for the elected municipal officer. The CRA also confirmed that, even if Form T2200 refers only to an "employee", this term may be read as an "officer" in situations where a person earns income from an office since the term "employee", as defined in subsection 248(1) of the Act, also includes an "officer".

— *External Technical Interpretation, Business and Employment Division, March 19, 2019, Document No. 2018-0758641E5*

Taxation of Power of Attorney Fees

The Canada Revenue Agency ("CRA") was asked how an individual not in the business of providing power of attorney services would be taxed if he received compensation in the form of power of attorney fees to provide these types of services. The CRA confirmed that the compensation received by the individual to provide those services would be taxed as income from an office under paragraph 6(1)(*c*) of the *Income Tax Act* (the "Act"), and the payor of those fees would be required under paragraph 153(1)(*a*) of the Act and section 101 of the *Income Tax Regulations* to withhold income tax at source and report the fees on a T4 form. However, if the individual is in the business of providing this type of service, he would have to include the fees in his income under subsection 9(1) of the Act, and the payor would only be required under paragraph 153(1)(*g*) to report them on a T4A and would not have to deduct any income tax at source.

— *External Technical Interpretation, Business and Employment Division, March 11, 2019, Document No. 2018-0749251E5*

Medical Expense Tax Credit – Fertility Expenses

The CRA was asked if the cost of sperm and/or eggs of a donor was an eligible medical expense for the purpose of claiming the medical expense tax credit ("METC") under subsection 118.2(1) of the *Income Tax Act* (the "Act"). More specifically, the CRA was asked, considering the enactment of subsection 118.2(2.2) of the Act, whether the previously-mentioned cost could be treated as a "substance" for the purpose of paragraph 118.2(2)(*n*).

The CRA confirmed that, although this is a question of fact, it is unlikely that the cost mentioned above would be considered an eligible medical expense because the costs incurred by an individual for fertility treatments are only eligible if paid for a patient who is the individual, his or her spouse or common-law partner, or his or her dependant. The medical expenses provided to the donor would include the medical services, the amounts paid for drug, and the laboratory or other diagnostic procedures or services, and could only be used to claim an METC for the patient-donor. Therefore, unless the egg or sperm donor is the individual, spouse or common-law partner, or dependant, the medical expenses paid on behalf of the donor would not qualify as eligible medical expenses for the purpose of claiming the METC. Regarding the second question, the CRA confirmed that the fees paid for obtaining sperm or eggs from a donor or donor organization are in respect of locating the donor and reimbursing him or her for his or her various expenses. Therefore, those fees are not considered "amounts paid for a substance" within the meaning of paragraph 118.2(2)(*n*) of the Act.

— *Internal Technical Interpretation, Business and Employment Division, December 21, 2018, Document No. 2018-0751891I7*

Medical Expense Tax Credit – Embryo Freezing Costs

The situation the Canada Revenue Agency (the "CRA") was asked to consider involved a male individual in a same-sex spousal or common-law relationship who wanted to claim a medical expense tax credit ("METC") for the expenses incurred in using the services of an egg donation organization and their fertility clinic to create embryos for surrogate implantation. More specifically, the expenses were paid to freeze those embryos, and the fertility treatments were done on the egg donor.

The CRA confirmed that the cost of freezing embryos for a patient when medically indicated (e.g., for the condition of infertility) qualified as an eligible medical expense, provided the requirements in paragraph 118.2(2)(*o*) of the *Income Tax Act* (the "Act") were met. Further, since 2017, subsection 118.2(2) of the Act also permits expenses paid for reproductive technologies to be claimed as eligible medical expenses, even if they are not medically indicated because of a medical condition of infertility. The cost of freezing embryos, as part of the in vitro fertilization ("IVF") procedure prescribed by a medical practitioner, was paid for by the individual, and was therefore an eligible medical expense for

the purpose of claiming the METC.

The CRA noted that the above measure could apply to a year before 2017 (but not before 2008) if the taxpayer made a specific request to the CRA by completing a Form T1-ADJ for that year.

— Internal Technical Interpretation, Business and Employment Division, November 5, 2018, Document No. 2018-0763791I7

Reward Donation Program

The situation the Canada Revenue Agency (the "CRA") was asked to consider involved merchants offering rewards to their clients for visiting their stores, and then giving their clients the option to either keep those rewards or have them paid to a registered charity supported by the merchants. Where the clients chose the second option, the merchants made the payments to the registered charity. The rewards program could also be operated by a marketing company or the registered charity itself. First, the CRA was asked if the clients were considered the donors of the amounts directed to the registered charity for the purpose of claiming the charitable tax credit under subsection 118.1(3) of the *Income Tax Act* (the "Act"). Second, the CRA was asked if the merchants could claim a tax deduction from their income for the rewards given under the program.

Regarding the first question, the CRA confirmed that, to be considered the donors of the rewards, the clients had to be considered the legal owners of the rewards immediately before their transfer to the charity. Whether this was the case or not could only be determined by the legal effect of the transactions involved in operating the program. The CRA added that the tax consequences of any particular donation program on its participants depended on the legal relationships between them under the relevant agreements. Regarding the second question, the CRA noted that the rewards program would always be funded by the merchants, and that their business expenses to fund the program would be subject to the application of subsection 9(1), paragraphs 18(1)(*a*) and (*b*), and section 67 of the Act.

— External Technical Interpretation, Financial Industries and Trusts Division, February 28, 2019, Document No. 2018-0761161E5

Ontario Seniors' Public Transit Tax Credit

The CRA was asked if fares paid by seniors to a transit organization for a transportation service qualified for the Ontario Seniors' Public Transit Tax Credit ("OSPTTC"). The actual names of the transportation service and organization providing the service were blacked out from the technical interpretation. However, the organization appears to be a charitable one providing rides to adults, children, and senior citizens living in a specific area, regardless of whether they had disabilities. The transportation service was offered by volunteer drivers using their own vehicles, but the costs of operating their vehicles were reimbursed to them. The Canada Revenue Agency ("CRA") noted that the service was not operated by a municipality and that an unnamed entity provided funding on an annual basis.

The CRA confirmed that the fares would not qualify for the purpose of claiming the OSPTTC since the entity providing the transportation service was not a "qualified Ontario transit organization" providing "Ontario public transit services". For a definition of those two terms, see subsection 103.0.1(1) of the Ontario *Taxation Act*. In this situation, it does not appear that the service was operated by the Government of Ontario nor one of its municipalities. Furthermore, the entity providing the service in question was not considered a "specialized transportation service provider" since it was provided by volunteers and was not designed to transport persons with disabilities.

— External Technical Interpretation, Business and Employment Division, January 24, 2019, Document No. 2017-0733511E5

Allowances Paid under Prescribed International Development Assistance Programs

The CRA was asked to consider the following situation:

- An employer undertook an international development assistance program (“IDAP”) funded by Global Affairs Canada (“GAC”). The latter company replaced the Canadian International Development Agency (“CIDA”) when CIDA was disbanded in 2013.
- A Canadian resident employee (the “employee”) left Canada to perform foreign services under the IDAP.
- In addition to his regular salary, the employee received the following representation and other special allowances to compensate him for inconveniences resulting from different living conditions or additional expenses in the foreign country:

  (1) post living allowance;

  (2) post differential allowance; and

  (3) overseas service premium.

The CRA was asked if those allowances could be excluded from the employee’s income by virtue of subparagraph 6(1)(*b*)(iii) of the *Income Tax Act* (the “Act”). Relying on subparagraph 6(1)(*b*)(iii) and paragraph 250(1)(*d*) of the Act and section 3400 of the *Income Tax Regulations* (the “Regulations”), the CRA concluded that the three allowances described above would constitute “representation or other special allowances” to be excluded from the employee’s income. The CRA added that the programs funded by the GAC (a successor to the CIDA), for the purpose of section 3400 of the Regulations, would constitute prescribed international development assistance programs of the Government of Canada, and would therefore be eligible for the application of paragraph 250(1)(*d*) of the Act.

The CRA assumed that the employee was resident in Canada at any time during the three-month period preceding the day of his departure to work in the foreign country.

— *External Technical Interpretation, Business and Employment Division, January 31, 2019, Document No. 2017-0695931E5*

CURRENT ITEMS OF INTEREST

Tax Relief for Canadians Affected by Flooding

Recognizing the difficulties facing taxpayers affected by recent flooding, the CRA is encouraging individuals, businesses, and first-responders to request taxpayer relief online, by phone, or by filing form RC4288. Each request is considered on a case-by-case basis.

Progress of Legislation

C-97, *Budget Implementation Act, 2019, No. 1*, received Second Reading in the House of Commons and is currently with the Standing Committee on Finance.

C-82, *Multilateral Instrument in Respect of Tax Conventions Act*, is currently undergoing Second Reading in the Senate.

S-6, *Canada–Madagascar Tax Convention Implementation Act, 2018*, which has already received Third Reading in the Senate, has received Second Reading in the House of Commons and has been reviewed by the Standing Committee on Finance.

Saskatchewan Court of Appeal Upholds Federal Carbon Tax

The Saskatchewan Court of Appeal released its decision today upholding the federal government's right to impose a carbon tax. In a split decision, Chief Justice Richards, writing for the majority, stated at para 164:

> Having worked through both the pith and substance of the Act and the scope of Parliament's jurisdiction in relation to greenhouse gas pricing, it is now possible to determine the validity of the Act. As explained earlier, this involves an inquiry as to whether the pith and substance of the Act comes within a head of federal authority. The answer to that inquiry is self-evident in light of the foregoing analysis. The pith and substance of the Act is about establishing minimum national standards of price stringency for greenhouse gas emissions. Parliament has jurisdiction over this subject matter by virtue of the national concern branch of Peace, Order, and good Government. It follows that the Act is constitutionally valid.

And in conclusion held "The Greenhouse Gas Pollution Pricing Act is not unconstitutional either in whole or in part".

Saskatchewan's Attorney General is on record as saying prior to the release of the decision that, if the court did not hold in Saskatchewan's favour, it would be seeking leave to appeal to the Supreme Court of Canada.

Canada To Implement New Anti-Dumping Measures for Steel

The Canadian Government has announced that it intends to enact final safeguard measures for imports of heavy plate and stainless steel wire.

In October 2018, in response to the introduction by the US of tariffs on steel and aluminum products, the Canadian Government imposed provisional steel safeguard measures for a period of 200 days. The Government asked the Canada International Trade Tribunal ("CITT") to undertake an inquiry into whether final safeguards are warranted. A WTO member may take a "safeguard" action (i.e., restrict imports of a product temporarily) to protect a specific domestic industry from an increase in imports of any product which is causing, or which is threatening to cause, serious injury to the industry.

The CITT has now concluded that final safeguards are warranted. In response to the ruling, the Government will hold an intensive 30-day consultation with industry and workers, to determine what further protections are required.

The Government said that new measures will include a targeted review of dumping cases to boost protections through higher duties and greater flexibility for the Canada Border Services Agency to address price and cost distortions in foreign markets when determining whether dumping has occurred. The Government will also consult on the framework for the remission of the surtaxes currently imposed on imports from the US.

Canada Revenue Agency Consults on Improving Services

The Canada Revenue Agency ("CRA") is seeking public feedback on how it can improve the services it provides to taxpayers.

The aim of the CRA's consultations is to help the CRA to better understand taxpayers' perception of and experience with the agency. The CRA is seeking comments on questions relating to its performance, the difficulties people face when interacting with it, and how its services can be improved. It is also interested in receiving views on the impact of previous service innovations.

The CRA will conduct seven in-person consultations at locations throughout Canada during May and June. An online consultation will run from April 23 to June 18. Summaries of each in-person consultation will be published as sessions conclude, and a final report is expected in the fall.

Revenue Minister Diane Lebouthillier said:

> Our Government is committed to ensuring that the CRA puts people at the center of everything it does. Over the past three years, we have introduced changes that are leading to real results for Canadians. With these public consultations, we are taking another step in listening to Canadians and responding to their concerns, expectations, and desire to improve how the CRA delivers services.

Ontario Budget Highlights

On April 11, 2019, Ontario Finance Minister The Honourable Victor Fedeli tabled the 2019 Ontario Budget. Notable tax measures in the Budget include:

- a new refundable Childcare Access and Relief from Expenses ("CARE") tax credit, which will provide tax relief on a percentage of child care expenses that are eligible for the child care deduction, up to a dollar limit;
- a new non-refundable Low-income Individuals and Families Tax ("LIFT") credit which is equal to the lesser of $850 and 5.05% of employment income (subject to a phase-out as income exceeds $30,000);
- paralleling the federal CCA measures from the 2018 Fall Economic Statement; and
- eliminating the probate fees on small estates ($50,000 or less) and extending the deadline to file the estate administration tax information returns.

A full overview of all tax measures announced in the Budget can be found in the WK Budget Dispatch.

FOCUS ON CURRENT CASES

This is a regular monthly 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.

Taxpayers May Validly Serve a Notice of Objection on the Minister After Receiving an Audit Proposal Letter Despite Not Yet Having Received a Notice of Reassessment

***Ihama-Anthony v. The Queen*, 2019 DTC 1009 (Tax Court of Canada)**

This decision of the Tax Court of Canada concerns an application brought by the taxpayer under section 166.2 of the *Income Tax Act* (the "Act") for an extension of time to serve a notice of objection on the Minister of National Revenue. In the course of its decision, the Court considers both the substantive requirements of a notice of objection and whether or not a taxpayer is entitled to serve an objection prior to having received a notice of reassessment.

In this matter, on December 8, 2014, the CRA had sent a letter to the taxpayer requesting that he provide the CRA with particulars of certain business expenses deducted in 2011 and 2012. The taxpayer sent the requested documentation to the CRA only to have the documentation returned to him a few weeks later.

On March 23, 2015, the taxpayer received a letter from an auditor with the Ottawa tax services office, following which he called the auditor. In the call, the auditor indicated that the taxpayer's documentation package submitted previously had not properly categorized the documents. The auditor requested that the taxpayer re-categorize the documents and prepare an itemized spreadsheet, following which the taxpayer faxed the materials requested to the auditor.

On May 11, 2015, a new auditor sent a letter to the taxpayer stating that the CRA had decided to reassess the taxpayer's 2011 and 2012 taxation years, disallowing $26,922 of business expenses deducted in 2011 and $21,877 of business expenses deducted in 2012.

The letter indicated that the reassessments would result in a charge for interest at the prescribed rate. The letter further indicated that the CRA would send notices of reassessment setting out the amounts of the taxes owing, with the interest accrued to the date of the reassessments.

The taxpayer received the letter in mid-May and, on the same day, called the new auditor who sent the letter. In the course of the call, the taxpayer learned that the new auditor had not received any of the documentation submitted by the taxpayer to the other auditor. The new auditor requested that the taxpayer re-fax the documents. On the day of the call, the taxpayer therefore sent a fax containing the documentation. The taxpayer did not alter the materials in any way except to write the case number and the new auditor's name on the old cover sheet from the earlier fax.

Subsequently, on May 19, 2015, the CRA issued the 2011 and 2012 reassessments.

It was only on March 16, 2018, after being contacted by a CRA collections officer who advised that the taxpayer had not filed notices of objection, that the taxpayer filed notices of objection to the reassessments of his 2011 and 2012 taxation years. The taxpayer subsequently received a letter dated April 19, 2019 from the CRA advising that the notices of objection were out-of-time, having been mailed outside the 90 day period following the date of the notices of reassessment. The letter indicated that while the CRA had treated the late-filed notices of objection as an application for an extension of time to object under section 166.1 of the Act, because the notices of objection had been received more than one year and 90 days after the date of the notices of reassessment, an extension of time could not be granted.

On May 17, 2018 the taxpayer filed an application for an extension of time to the Court.

In respect of this application, the provisions of paragraph 166.2(5)(*a*) of the Act provide that, for the Court to grant an extension of time to file an objection, the taxpayer must have applied to the CRA, under subsection 166.1(1) of the Act, for an extension of time within one year after the expiration of the time otherwise required by the Act for filing a notice of objection.

In this case, the notices of reassessment were issued on May 19, 2015, meaning that in order to be eligible for relief from the Court under section 166.2, the taxpayer was required to have made an application to the CRA for an extension of time by August 17, 2016 (i.e., 90 days plus one year after the reassessment).

The Court nonetheless took the creative step of considering whether the fax sent by the taxpayer in mid-May of 2015, which responded to the auditor's May 11, 2015 proposal to deny the taxpayer's business deductions, was a valid objection within the meaning of section 165 of the Act.

The Court cited the Federal Court of Appeal's decision in *870 Holdings Ltd.* (2004 DTC 6001), which states that while the statutory requirements for a notice of objection are minimal, a valid notice of objection must: (1) be addressed to the Chief of Appeals of the relevant district; and (2) be in writing and set out the reasons for the objection and the relevant facts.

As to the second requirement, the Court relied upon its prior jurisprudence in concluding that an objection must include an actual objection to an assessment or at least some indication that the particular taxpayer is objecting to an assessment. The Court noted, however, that a notice of objection need not be made using the CRA's suggested Form T400A.

The Court considered the letter that the taxpayer had faxed to the auditors. The Court noted the taxpayer's polite, cooperative tone in the faxed letter and his purported desire to report the expenses in the manner requested by the CRA. The Court stated that there was nothing in the fax that suggested that it was sent in contemplation of the reassessments or even that the taxpayer disagreed with the CRA's position in respect of the denied expenses.

The Court noted that while the sending of the fax suggests that the taxpayer was concerned about a pending reassessment, when the taxpayer testified in respect of his telephone conversation with the auditor, the taxpayer gave the impression that he was focused primarily on the non-receipt or misplacement by the CRA of the documents that he had previously faxed to the CRA, and not on disputing the pending reassessments.

The Court noted that while subsection 165(6) gives the Minister a limited discretion to relieve issues of form in respect of the service of a notice of objection, this discretion is limited to the manner of service under subsection 165(2) and does not extend to the requirements in subsection 165(1).

In respect of the requirement under subsection 165(2) that a notice of objection be addressed to the Chief of Appeals, the Court noted that there is mixed jurisprudence as to whether a notice of objection needs to be addressed to the Chief of Appeals where service was otherwise proper. However, the Court found in this matter that the taxpayer had not met the requirement to serve an objection on the Chief of Appeals.

While the above determinations of the Court were sufficient to dispose of the taxpayer's application, the Court also considered whether the taxpayer could object to a notice of reassessment prior to the issuance of the notice of reassessment. In this regard, the Court noted that subsection 165(1) refers to a taxpayer who objects to an "assessment" (which, under the Act, includes a reassessment) rather than to a taxpayer who objects to a "notice of assessment", suggesting that it might be possible for a taxpayer to object to a reassessment before the notice of reassessment was issued.

The Court considered a trio of cases on the subject: *Jablonski* (2012 DTC 1066 (TCC)), *Dionne* (2012 DTC 1189 (TCC)), and *Persaud* (2014 DTC 1031 (TCC)). The Court distinguished the *Jablonski* and *Dionne* cases: *Jablonski* because the taxpayer in that case did not attempt to plead that a notice of objection filed prior to a notice of reassessment was valid, and *Dionne* because the events that prompted the taxpayer's representative to send a letter that was later claimed to be a notice of objection did not suggest that a notice of reassessment was pending. Instead, the Court agreed with the reasoning in *Persaud* that a notice of objection prepared in response to a proposal letter, which informs a taxpayer that a reassessment is about to be issued, may, if validly served on the relevant Chief of Appeals, constitute a valid notice of objection.

Notwithstanding this decision, practitioners should note that, even assuming that the Court is correct that an objection may be served prior to the issuance of a notice of reassessment, any such right to object prior to issuance of a notice of reassessment is expressly limited by the Court to situations in which the CRA has advised the taxpayer in writing (e.g., in a proposal letter) that a notice of reassessment is about to be issued. In respect of this determination by the Court, it is also noteworthy that in the recent case of *Boguski* (2019 DTC 1002 (TCC)), the Court states without any discussion or analysis that objections filed prior to an assessment are invalid.

In the taxpayer's case, given that there is no indication that the CRA ever considered the expense documentation submitted by the taxpayer given what seems to have been an internal routing error by the CRA, consideration might be given to whether any taxpayer relief might be available through a remission order under the *Financial Administration Act* or, from interest, pursuant to the provisions of subsection 220(3.1) of the *Income Tax Act*.

— *Justin Shoemaker*

Taxpayers Cannot Be Treated Like Cattle Herded on Their Way to a Slaughterhouse: Minister Unsuccessful in Application Under Section 174 To Have Court Determine a Question Common to Multiple Taxpayers

***MNR v. Boguski et al*, 2019 DTC 1002 (Tax Court of Canada)**

This apparently is the first application heard by the Tax Court under amendments to section 174 of the *Income Tax Act* as that section applies to a large group of unrelated taxpayers.

A large number of taxpayers had claimed Canadian development expenses ("CDEs") related to mining rights that the taxpayers had purchased in Canada (the "Properties"). Prior to the section 174 application being brought, there were 23 appeals that Justice D'Arcy had directed would proceed under the Tax Court of Canada's lead case rules. Two of these appeals had been filed under the Court's general procedure rules while the remaining 21 appeals had been filed under the Court's informal procedure rules. Justice D'Arcy had directed that the two general procedure appeals be heard as the "Lead Cases".

After an additional 200 taxpayers were identified by the CRA as having filed notices of objection to the denial of CDEs claimed in respect of the Properties, the Court suggested in case management conferences that the CRA should ask these taxpayers to agree to be bound by the final judgment in the Lead Cases. 69 taxpayers agreed to be bound by the Lead Cases and 67 taxpayers did not (this latter group of 67 being referred to as the "Assessed Taxpayers"). The Minister decided that instead of issuing notices of reassessment for each of these 67 taxpayers, consistent with what the Court had suggested, she would file a section 174 application for a determination of whether the rights acquired by the taxpayers in the Properties were tax shelters.

Section 174 is a provision that was expanded in 2013 as part of a suite of changes aiming to streamline processes in the Court. The section now applies not only to questions arising out of *the same* transaction or occurrence (or series), but also to *substantially similar* transactions or occurrences (or series), which was said to be the case in this matter.

Section 174 states that the Minister may apply to the Court for a determination of a question of law, fact, or mixed law and fact in substantially similar transactions. Subsection 174(3) states that if the Court is satisfied that a question set out in an application under this section is common to assessments or proposed assessments in respect of two or more taxpayers who have been served with a copy of the application, the Court can make an order naming taxpayers in respect of whom the question will be determined, make an order joining parties, or determine the question in any manner it considers appropriate. Importantly, as made clear by D'Arcy J, the Court must exercise its discretion in deciding whether to determine a question pursuant to section 174, and the Court must ensure that all parties are treated fairly, that the Court's resources are used efficiently, and that there is not undue administration or compliance hardship placed on the parties. The determination under this section must also allow for issues raised by the parties to be resolved in the most expeditious, least expensive way.

The Court directed that it would hear the CRA's section 174 application in two parts. As stated by D'Arcy J:

> First, the Court will decide whether it should issue an order under subsection 174(3). Specifically, the Court will decide whether it will determine the Question. If the Court decides that the Question should be determined, then the second hearing, a hearing to answer the Question, will occur.

In respect of the first part of the process adopted by the Court, the Court determined that it would not issue the order to determine the question under section 174. The Court reached this determination notwithstanding that the Minister had formed the opinion that the question was common to the Assessed Taxpayers and to the appellants in the Lead Cases, such that the Minister was entitled to bring the application under section 174.

Although entitled to bring the application, the Minister was required to satisfy the Court that the question was common to the assessments in issue and that she had served a copy of the application on the Assessed Taxpayers and the Lead Cases' appellants. Even if that were done, the Court noted that it was for the Court itself, not the Minister, to

decide whether the Court should determine the question.

In respect of the requirement that the Minister satisfy the Court that the question was common to the assessments in issue, the Court stated that it was not provided with adequate evidence for many of the Assessed Taxpayers. Documentary evidence was heavily redacted, such that the Court gave it no weight, or incomplete: documents said "to be attached" were not. Further, some of the produced notices of objection did not refer to the Properties or the CDEs. The Court noted that some of the notices of objection were invalid on the basis that they were filed before the Minister's final assessment for a particular taxation year. (In this regard, the Court does not address certain jurisprudence, including the recent decision in *Ihama-Anthony* (2019 DTC 1009 (TCC)) (which is under appeal), that in some limited circumstances objections may be served prior to assessments being issued.)

For 19 of the Assessed Taxpayers, the Court was provided with valid notices of objection that showed the taxpayer objected to the denial of CDEs and referenced the Properties in at least some of the taxation years at issue. The Court therefore found that the Minister had satisfied it that the question at issue was common to these notices of objection. Accordingly, the Court went on to determine whether it would exercise its discretion and order a hearing to determine the question.

The Court determined that it would not exercise its discretion to order a hearing to determine the question pursuant to section 174. The Court was of the view that the approach that the Minister proposed was cumbersome. The Minister's suggested course of action was that the Assessed Taxpayers be joined as parties to the Lead Cases, subject to each of the Assessed Taxpayers filing "pleadings" setting out their cases to enable the Minister to know what facts and reasons each Assessed Taxpayer was relying on before deciding whether to join each taxpayer in the action. Instead, the Court stated that if it were to exercise its discretion to order a hearing to determine the question, it would join all of the Assessed Taxpayers as parties to the Lead Cases. The Court held that the right of all of the Assessed Taxpayers to fully participate in the answering of the question arose once the Minister named them in the Application.

The Court held that directing a hearing involving 42 parties would not be fair to the parties; in this regard, a fair hearing involving 42 parties who in this case were in five different provinces might be impossible. Numerous times in its reasons for judgment, the Court highlighted that many of the Assessed Taxpayers were self-represented and that the proposed course of action would be highly confusing for them. A pre-hearing conference call involving 42 parties would be highly ineffective. As the question in issue was one of mixed fact and law, it would be necessary for evidence to be led but, the Court noted, discoveries would be very difficult and unfair to the 42 parties. Any particular witness might have to be cross-examined by 41 different parties; further, parties would have to provide 44 or more copies of each document entered as evidence.

Justice D'Arcy had previously determined that the most expeditious and least expensive way to resolve the issues related to the claimed CDEs was by hearing the two Lead Cases, which would involve counsel for the Respondent and one counsel for the appellants in the two Lead Cases. The Minister had ignored this determination when she brought the application that would result in 39 self-represented parties. The Court suggested that if the Minister thought that answering this question could resolve the issues related to the Properties, she should have brought an application under Rule 58 of the *Tax Court of Canada Rules (General Procedure)*, which allows for the hearing of a question in the context of an appeal before the Court. The Court noted that given the factual matters in issue, it is unlikely that a Court would have granted an order under Rule 58, such that if the Court ordered a hearing under section 174, this would in effect circumvent prior Court rulings regarding Rule 58.

The proposed approach of the Minister pursuant to section 174, in the Court's view, would result in the opposite of the efficiencies that the provision was intended to achieve: with 42 taxpayers, it would lead to an inefficient use of the Court's resources, and a significantly more expensive and time-consuming approach to a just outcome for the taxpayers. The CRA had not followed the Court's prescribed approach of issuing reassessments or notices of confirmation, as suggested in case management conferences, which the Court had highlighted as the "efficient and fair" way to deal with appeals of large groups of applicants.

The question remains as to when section 174 would be an appropriate avenue to pursue to group together a large number of applicants. However, as the decision has been appealed to the Federal Court, there may be further clarification forthcoming shortly.

— *Sarah Ferguson, Articling Student*

Tax Court Provides Some Clarity as to the Meaning of "Advantage" Under the TFSA Rules

***Louie v. The Queen*, 2018 DTC 1166 (Tax Court of Canada)**

This decision is apparently the first to address the taxation of a tax-free savings account. The decision specifically addresses the issue of when a taxpayer is extended an "advantage" within the meaning of that term under subsection 207.01(1) of the *Income Tax Act* (the "Act"), such that the taxpayer is liable to pay tax under Part XI.01. The decision deals with a series of swaps that occurred before the definition of advantage was amended to explicitly include "swap transactions". Notwithstanding the amendment, the decision is illustrative in understanding the interpretive approach to the TFSA rules.

The general purpose of the TFSA tax exemption in section 146.2 is to encourage households, particularly those with low and modest incomes, to invest. That section sets out the rules for the creation of a TFSA, and allows the compounding of investment returns and the tax-free distribution of accrued gains. Part XI.01 sets out anti-avoidance rules that prevent taxpayers from taking advantage of the TFSA provisions in a way not intended by Parliament. One such rule is the taxation of an "advantage" under subsection 207.05(1). That anti-avoidance provision taxes 100% of the increase in FMV that is attributable to transactions that would not occur in an open market between arm's length parties.

In this case, the taxpayer, as Lamarre ACJ states, was "a sophisticated investor with extensive knowledge of the stock market." She opened a TFSA in 2009, when the rules were introduced, and from May 15 to October 17, 2009, made 71 share exchanges ("swaps") in which she transferred TSX-listed shares between her TFSA and either her RRSP or her Canadian direct trading account.

A swap requires assets of equal value to be exchanged. TD Waterhouse, with whom the taxpayer had her accounts, permitted its customers to choose any price between the high and low on the day the stock was traded. For the shares swapped out of her TFSA, the taxpayer always selected the highest price at which the shares had traded during the day up to the time of the swap. Conversely, for the shares swapped into her TFSA, she always selected the lowest price at which the shares had traded. The swaps always happened shortly before the close of trading on the TSX. Also, the taxpayer generally conducted swaps on days on which the prices of the swapped shares were highly volatile. A number of times, she swapped the same shares in and out within a 24 hour time frame.

This reveals a strategy. For example, the taxpayer may have swapped the same shares from one account into the other and vice versa. Lamarre ACJ explained it in the following way:

> In swapping shares of Company A into her TFSA, she would have picked the lowest price. When swapping shares of Company A out of her TFSA, she would have picked the highest price. The end result would have been a greater number of shares swapped in (because of the low price) compared to the number of shares swapped out (because of the high price). While quantities of shares are moving between accounts, the overall value of the two accounts is not affected.

And even if the taxpayer did not swap exactly the same shares, she still managed to achieve the same result. There was a risk that the shares swapped in might decrease in value and the shares swapped out might increase, which would have been contrary to what the taxpayer presumably intended. She neutralized this risk by swapping the same shares repeatedly.

The Court determined that, in the result, the taxpayer had managed to artificially transfer shares out of her RRSP and Canadian direct trading account into her TFSA and thus to significantly increase the proportion of her capital stock held in her TFSA. By the end of 2009, the taxpayer's TFSA increased from $5,000 (her initial contribution limit) to $206,615.09, representing a 4,032% increase in its value.

Effective October 17, 2009, the definition of advantage was amended to include "swap transactions", and at that time the taxpayer stopped the swaps. She left her shares in the TFSA where they were subject to true market forces in the 2010–2012 years. In 2010 and 2012, the value of the TFSA increased. The Minister of National Revenue assessed the taxpayer under the advantage tax provisions with respect to the increase in the value of the taxpayer's TFSA account in 2009, 2010, and 2012. The Minister's rationale in assessing advantage tax in 2010 and 2012, after the swap trading had ceased, was that but for the increases in the value of the TFSA attributable to the swap trading, the taxpayer would not have had the shares in her TFSA that increased in value during 2010 and 2012. In 2011, the taxpayer suffered a loss, so the MNR did not assess her for that year.

With "swap transactions" not yet included in the definition, the Court had to determine whether during the relevant period the swaps nevertheless constituted an "advantage" under the definition in subsection 207.01(1). At the relevant time, paragraph (*b*) of that definition read:

> (*b*) a benefit that is an increase in the total fair market value of the property held in connection with the TFSA if it is reasonable to consider, having regard to all the circumstances, that the increase is attributable, directly or indirectly, to
>
> (i) a transaction or event or a series of transactions or events that
>
> (A) would not have occurred in an open market in which parties deal with each other at arm's length and act prudently, knowledgeably and willingly, and
>
> (B) had as one of its main purposes to enable a person or a partnership to benefit from the exemption from tax under Part I of any amount in respect of the TFSA [. . .]

The Explanatory Notes to the 2009 Budget state that paragraph (*b*) "is intended to guard against transactions designed to artificially shift taxable income away from the holder and into the shelter of a TFSA or to circumvent the TFSA contribution limits." The Court's task in this case was to determine, for each of the years 2009, 2010, and 2012, whether the swaps would have occurred in an open market and whether their purpose was to enable the taxpayer to benefit from the TFSA exemption.

The Court determined that the taxpayer's goal was to transfer TSX-listed shares from her RRSP and her Canadian direct trading account into her TFSA. In doing so, the taxpayer incurred transaction costs of $3,195. The Court inferred that the taxpayer entered the swaps for the purpose of benefitting from the Part I tax exemption on the sale of the shares subsequently held in the TFSA. The Court reasoned that the taxpayer "must have intended to benefit from a tax-free distribution from her TFSA as opposed to a taxable withdrawal from her RRSP or a taxable gain within her [Canadian direct trading account]."

The Court further concluded that the series would not have occurred in an open market. The taxpayer's ability to select a transfer price from within a range would not be possible in an open market, where the price of the shares would be fixed at the time of the swap and would necessarily be the same whether the taxpayer was transferring the shares into or out of her TFSA. Here, the taxpayer was able to cause her TFSA to profit from the difference between the daily lows and highs of her shareholdings. On this point, the court distinguished *Untermyer* ([1929] SCR 84 (SCC)), in which the Supreme Court held that picking a price between the high and low of the day was an appropriate valuation method. In *Untermyer*, the owner of the shares possessed a significant stake in the company, and because there was no actual market price that took into account a significant sale of shares, the Supreme Court recognized that a range of prices may be an appropriate proxy for the FMV of those shares at that time. In the current appeal, the market price of the shares at the time of the swaps was known. The prices selected reflected the highs and lows of the

day, not the FMV of the shares at the moment of the swaps.

The Court noted that had the taxpayer made only one swap or a small number of swaps over a long period, the ability to select the price may have been a less heavily weighted factor. It was the repetitiveness of the swaps that was key. Absent this repetition, the overall value of each account would have depended solely on the evolution of the value of the shares as influenced by market variables. The risk of price changes would in that case have made the strategy of the taxpayer inefficient. As explained earlier, the taxpayer managed to neutralize this risk factor.

The Court concluded that pursuant to the definition of "advantage" in subsection 207.01(1), the taxpayer had received an advantage in relation to her TFSA in 2009. But, ultimately, the Court determined that "indirectly" did not mean that the taxpayers' benefit in 2010 and 2012 could be attributed to the 2009 swaps.

While paragraph (*b*) is itself an anti-avoidance provision, it pertains to a legislative scheme the very purpose of which is to encourage a tax-free increase in savings. The Court stated that because of the "inherent tension between the purpose of the provision and the scheme as a whole" some restraint in the application of the phrase "directly or indirectly" was necessary; it must be balanced by the subsequent phrase requiring one to ask whether it is "reasonable to consider, having regard to all of the circumstances". In *Canada Trustco* (2005 DTC 5523), the Supreme Court of Canada noted that the presence of the word "reasonably" in subsection 245(4) — with regard to whether it may (reasonably) be considered that a transaction would result directly or indirectly in an abuse of the Act — "tempered" the interpretation of the provision, "suggesting some ministerial and judicial leeway in determining abuse."

Accordingly, the Court determined that the broad scope of "directly and indirectly" did not *reasonably* extend to the 2010 and 2012 taxation years, during which the taxpayer was no longer engaging in swaps. Not only that, the taxpayer chose not to cash-out the gains arising from her swap activity by selling her shares and realizing a tax-free capital gain. Instead, she decided to risk leaving the shares in the TFSA where they were subject to market forces and, accordingly, real market risk. It was reasonable in the circumstances to attribute the 2010 and 2012 increases to the post-2009 financial recovery rather than to the 2009 swap transactions.

The taxpayer was found to be liable, pursuant to subsections 207.05(1) and (2), for tax in respect of the advantage arising from the swap transactions undertaken in 2009, equal to the increase in the FMV of the TFSA which was $200,795.

As the decision has been appealed, further clarification as to the scope of the advantage tax may be forthcoming shortly.

— *Hilary Smith, Articling Student*

Can a Notice of Reassessment Be Vacated Because It Was Initiated as a Consequence of Tax Filings by a Taxpayer Who Lacked Mental Capacity?

***Estate of the Late Anna Ntakos*, 2018 DTC 1167 (Tax Court of Canada)**

This was an application to the Tax Court of Canada for extensions of time by an estate to file notices of objection to assessments or reassessments of the deceased, Anna Ntakos, for five taxation years. The Tax Court did not grant the extensions (and, based on the timing of relevant events described in the reasons for decision, it seems that the Tax Court would not have had the statutory authority under subsection 166.2(5) of the *Income Tax Act* (Canada) (the "Act") to grant the extension in any event). However, for three of the taxation years, the Tax Court vacated the underlying notices of reassessment on the basis that Ntakos did not have the requisite mental capacity during the period of time immediately preceding her death to make the tax filings that the Minister used to issue the reassessments to which the estate was seeking to object.

This case might be an instance of a hard case making bad law, as it seems that the Tax Court may have felt sympathy towards the circumstances in which the estate found itself and desired to rectify a bad situation using a novel

approach. Unfortunately, in vacating the reassessments, it appears that the Tax Court neither took into account subsection 152(7) of the Act — which allows the Minister to make an assessment or reassessment without requiring any filing to be made by a taxpayer — nor elaborated on where the Tax Court found the statutory authority to vacate a reassessment if it is not done in the course of disposing of an appeal pursuant to subsection 171(1) of the Act.

Before her death, Ntakos and her two brothers-in-law were shareholders of a holding company that owned the shares of a corporation that operated their family's construction supplies business. She became a shareholder of the holding company as a consequence of the death of her husband (and brother to the other two shareholders). The evidence indicated that she was generally a passive participant in the affairs of the corporations and the family business following the death of her husband.

During the early 2000s, bitter disputes arose between the two surviving brothers concerning the income and other financial benefits that the shareholders would receive out of the family business relative to one another. It appears that Ntakos was largely content to stand on the sidelines of the dispute, as it was also during this period that the deceased was diagnosed with breast cancer and began to physically and mentally deteriorate.

One of the outcomes from the dispute between the brothers was that they agreed (likely without Ntakos' involvement or consent) to retroactively reallocate management fees and employment income that the shareholders received from the operating company over several years. The changes to the allocations of the shareholder receipts from the operating company required corresponding changes to be made to their tax filings, and the outside accountant that the brothers used to prepare the financial statements for the companies prepared and filed amended T1 tax returns or requests for adjustment with the Canada Revenue Agency on behalf of the three shareholders in 2003. In the case of Ntakos, the accountant filed requests for adjustment for her 1998, 2001, and 2002 taxation years to increase her income for those years. The Minister used the requests to issue reassessments for those years, to which the taxpayer's estate was now seeking an extension to object.

As the adjustments to Ntakos' taxable income was intended to be a reallocation of payments among the three shareholders, one presumes that there were offsetting reductions to taxable income in the T1 adjustment requests that the accountant prepared for one or both of the two surviving brothers. Although not expressly discussed in the Tax Court's reasons for decision, it is likely that, for Ntakos, the reallocation reflected in the amended tax filings was only a paper transaction and was not accompanied by any actual further payments to her by either the company or one of the other shareholders.

When the Tax Court turned to considering the estate's request for extension, the Court divided its analysis into two time periods and the tax filings that were made (or purportedly made) on her behalf in each period, leading the Minister to issue the assessment/reassessment to which the estate was seeking to object. Based on the evidence, the Tax Court determined that Ntakos did not have the requisite mental capacity to provide instructions to a third party in respect of her affairs during the period between her cancer diagnosis in the fall of 2002 and her death in October 2004.

The Tax Court began with the taxpayer's tax filings that caused the Minister to issue the relevant assessment or reassessment for Ntakos' 1999 and 2000 taxation years. The Court concluded that the relevant tax filings were made at a time when Ntakos had the mental capacity to do such things and, therefore, the taxpayer's right to object to the assessment/reassessment for those years was extinguished. Although the reasons for decision did not walk through the statutory conditions in subsection 166.2(5) that must be satisfied before the Tax Court can grant an extension to object, it seems clear that the estate would have been unable to satisfy the condition in paragraph 166.2(5)(*a*), which requires the application for extension to be commenced in the Tax Court within one year of when the rights to object to the relevant assessment or reassessment would have otherwise lapsed.

The Tax Court then went on to consider the T1 adjustment requests that were filed by the outside accountant after Ntakos was diagnosed with cancer in the fall of 2002. With regards to the circumstances surrounding those filings, the Tax Court stated that: "This odd amalgamation of terminal illness, mental capacity, vulnerability and misrepresentation of authority compel this Court to act." The Court went on to find that, since Ntakos did not have the requisite mental capacity to authorize anyone to make a tax filing on her behalf after her diagnosis, the T1 requests for adjustment that the accountant filed in 2003 in respect of Ntakos' 1998, 2001, and 2002 taxation years cannot be regarded as valid

requests made by the taxpayer and, therefore, the reassessments that the Minister issued in response to those requests were declared invalid and were vacated by the Court.

On the Court's decision to vacate the 1998, 2001, and 2002 reassessments, it is far from clear that the Court had the statutory authority to do so in the circumstances. There is some tax jurisprudence footnoted in the reasons for decision on which the Tax Court appears to have relied as authority for the proposition that a reassessment can be invalidated if issued by the Minister in response to a tax filing made without taxpayer authority or mental capacity. However, the case law that the Court cited involved situations where the Minister issued a reassessment beyond the normal reassessment period on the basis of a reassessment waiver that was given by the taxpayer. In those types of circumstances, it is clear that a waiver that was given to the Minister without taxpayer authority or by a taxpayer that did not have the mental capacity to do so would invalidate any reassessment because the Minister's authority to reassess beyond the normal reassessment period (under subparagraph 152(4)(*a*)(ii)) is predicated on the validity of the waiver given by the taxpayer.

Here, even though the triggering event for the Minister to reassess Ntakos' 1998, 2001, and 2002 taxation years was the outside accountant's filing of the T1 adjustment requests in 2003, the Minister's statutory authority for issuing those reassessments is likely paragraph 152(4)(*b*) of the Act, which authority the Minister is entitled to exercise without any action on the part of the taxpayer or the taxpayer's authorized representative. Subsection 152(7) of the Act serves to underscore the point, stating:

> 152(7) The Minister is not bound by a return or information supplied by or on behalf of a taxpayer and, in making an assessment, may, notwithstanding a return or information so supplied or if no return has been filed, assess the tax payable under this Part.

Thus, even though T1 adjustment requests are taxpayer-filed documents that the Canada Revenue Agency routinely uses to initiate taxpayer reassessments as an administrative matter, such documents appear to have no recognized legal status within the scheme of the Act insofar as compelling or restricting the Minister with respect to the issuing of an assessment or reassessment. (It should be noted, however, that there are provisions in the Act in which the Minister can be compelled to reassess a taxation year on the filing of an amended tax return: see subsection 152(6) of the Act.) Therefore, it seems questionable that an improperly filed T1 adjustment request should render invalid the reassessment that the Minister issued in response.

While the Tax Court should be commended for trying to find a way to provide relief to the estate in the circumstances, it seems that there would have been two more suitable routes that the estate might have pursued to obtain appropriate tax relief in the circumstances, neither of which would have involved litigation in the Tax Court. The first option would have been for the estate to ask that the Minister reassess to reduce the tax payable for a taxation year after the expiry of the normal reassessment period with the taxpayer's consent pursuant to subsection 152(4.2) of the Act; unfortunately, that avenue is now likely foreclosed for the estate because subsection 152(4.2) requires the request to have been made no later than 10 calendar years after the tax year to which the adjustment relates. The second option is for the estate to seek a remission order from the Governor-in-Council pursuant to the *Financial Administration Act*.

— *Sarah Ferguson, Articling Student*

RECENT CASES

Minister not entitled to an order compelling corporate taxpayer to comply with a request to answer oral questions

In the course of an audit as to whether the corporate taxpayer had complied with the transfer pricing rules in section 247 of the *Income Tax Act*, the CRA requested the taxpayer's employees to attend interviews and to answer orally various questions (the "Request"). The taxpayer refused to permit this, but did offer to answer the Minister's questions in writing. The Minister then brought a summary application seeking a compliance order under subsection 231.7(1) of the *Income Tax Act* directing the taxpayer to comply with the Request. In dismissing the Minister's application (2017 DTC 5102 (FC)), the Federal Court concluded, in essence, that: (a) 231.1(1)(*a*), upon which the Minister had been relying to justify the Request, could not be interpreted as the Minister was suggesting; and (b) to compel oral interviews as the Minister was proposing would in effect allow the Minister a pre-emptive discovery of the

taxpayer, thus circumventing the procedures under the *Tax Court of Canada Rules (General Procedure)*, and possibly prejudicing the taxpayer's position in any subsequent litigation with the Minister. The Crown appealed to the Federal Court of Appeal.

The Crown's appeal was dismissed. Neither the text, nor the context, nor the legislative history of paragraph 231.1(1)(*a*) supported the Minister's interpretation of that paragraph in this case.

MNR v. Cameco

2019 DTC 5042

Appeal allowed where payments to taxpayer qualifying for deduction under subparagraph 110(1)(*f*)(ii)

The taxpayer, a federal employee, was injured while engaged in his employment duties. Pursuant to the terms of the applicable Collective Agreement, he made a compensation claim to the provincial workers' compensation board, which approved his claim, finding that the on-duty injury had left him unable to work. He was then granted injury-on-duty leave by his employer. During the time he was on leave he received his full salary and a T4 was issued for each of those years in that amount. The taxpayer appealed from the assessment of such income, arguing that 85% of the income constituted workers' compensation payments that were reportable as income but subject to an offsetting deduction in the computation of taxable income.

The appeal was allowed. The Tax Court of Canada reviewed the relevant provisions of both the *Income Tax Act* ("Act") and the *Government Employees Compensation Act* ("GECA"). It held, based on that review, and the terms of the applicable Collective Agreement, that compensation equal to 85% of the appellant's income was paid to him by the federal government, as a self-insurer, rather than by the provincial Workers' Compensation Board. The Court held that such arrangement was sanctioned by the GECA, and that 85% of the total pay received by the appellant while on leave constituted compensation "received under an employees' or workers' compensation law", with eligibility and quantum determined by the workers' compensation process of the province. The Court concluded, therefore, that 85% of the amounts received by the appellant while on injury-on-duty leave constituted income under paragraph 56(1)(*v*) of the Act and consequently was deductible under subparagraph 110(1)(*f*)(ii) of the Act. His appeal was therefore allowed, with costs.

McCarthy v. The Queen

2019 DTC 1054

Appeal allowed where impugned transactions not constituting abusive avoidance transactions

The corporate taxpayer undertook a recapitalization and restart transaction in which its assets and liabilities were moved to a new corporation. The remaining corporate shell was then used to raise funds through an initial public offering, and certain tax attributes previously earned by the corporation, including tax losses and investment tax credits, were used to shelter income earned by the new business. The Minister assessed the series of transactions as resulting in a change of control and as contravening the general anti-avoidance rule ("GAAR"), and the taxpayer appealed from that assessment to the Tax Court of Canada.

The appeal was allowed. The Court held that the first issue for determination was whether, in the course of the transactions, there had been a change in control, such that the appellant would be precluded from deducting the tax attributes. If no change in control had taken place, the Court was required to determine whether the series of transactions contravened the GAAR. To do so, it was necessary to determine whether a tax benefit had been obtained, whether the transactions undertaken constituted avoidance transactions and, if so, whether such avoidance transactions were abusive. The Court first considered the change of control issue and concluded, following a review of the transactions undertaken, that no change of control had occurred, as the transactions were carefully structured so as to avoid an acquisition of control under the relevant provisions of the *Income Tax Act*. The Court then considered the respondent's position that the transactions undertaken were abusive avoidance transactions that contravened GAAR.

The Court held first that it was clear that the transactions in issue resulted in a reduction of tax, and therefore a tax benefit, to the appellant. As well, the appellant had not argued in its Notice of Appeal that the transactions in question were undertaken for non-tax reasons, and the Court held that it was therefore precluded from taking the position that the alleged avoidance transactions were entered into primarily for a non-tax purpose. The sole remaining issue for determination was whether such avoidance transactions were abusive, and the Court concluded that they were not. In the Court's view, based on its textual and contextual analysis of the object, spirit, and purpose of the tax attribute streaming restrictions and the corporate control rules set out in the *Income Tax Act*, the transactions did not constitute an abuse of such provisions. The taxpayer's appeal was therefore allowed.

Deans Knight v. The Queen

2019 DTC 1059

Appeal from denial of disability tax credit allowed in part

The taxpayer applied for the disability tax credit (DTC) for the 2010 through 2017 taxation years. The Minister made a determination that she was not entitled to such credit on the basis that "her mental impairments did not affect her ability to perform the necessary basic activities for everyday life all or substantially all of the time". She appealed from that determination to the Tax Court of Canada.

The appeal was allowed in part. The Tax Court noted that the Minister had agreed that the appellant had a severe and prolonged impairment in mental functions and that such had been certified by a medical doctor. In order to qualify for the DTC she was also required to establish that such impairment markedly restricted her ability to perform one or more basic activities of daily living and that, even with therapy and appropriate medication it had that effect all or substantially all of the time. The Court noted that the determination of whether a taxpayer qualifies for the DTC was largely a factual question, and it therefore reviewed both the appellant's medical history as outlined in the medical reports filed as evidence and her educational and employment history. The Court noted as well that the principles set out in the jurisprudence indicate that where there is doubt as to whether an individual qualifies for the DTC, that doubt should be resolved in favour of the individual. Based on its review of the appellant's history and current circumstances and the relevant jurisprudence, the Court was satisfied that, on a balance of probabilities, she qualified for the DTC beginning in 2015 and in each year thereafter. Her appeal was therefore allowed with effect from the 2015 taxation year. There was no order as to costs.

Green v. The Queen

2019 DTC 1057

Motion to strike appeal for judicial review of decision affecting taxpayer where no assessment was issued dismissed

This case involves the Westminster Savings Credit Union, which received, as part of a GST/HST audit, a letter stating it was not considered as a credit union. The letter also stated the Appellant would not be assessed for prior periods. Since no assessment was issued, the Appellant could not file a Notice of Objection or appeal to the Tax Court. Consequently, the Appellant appealed to the Federal Court for a judicial review of this decision. The Attorney General is of the view that the Appellant is disguising a tax matter into an administrative law issue. It therefore filed a motion to strike, which is the sole object of this decision.

The motion was dismissed. The Attorney General bases its motion to strike on its opinion that the appeal for judicial review has no chance of success and that the Federal Court has no jurisdiction to review the matter over which the Tax Court of Canada has exclusive jurisdiction. Finally, the Attorney General argues that there is no cognizable administrative law claim, the argument being that the letter does not constitute a decision, order or act of proceeding The Appellant feels it is immediately affected by the decision because it renders supplies made to other credit unions taxable because subsection 150(6) of the *Excise Tax Act* is not applicable. There is no other remedy than a judicial review by the Federal Court. Given that it must be ''plain and obvious'' that the application for judicial review cannot succeed, to justify the motion to strike, the Appellant argues that the motion to strike must be denied. After reviewing the jurisprudence on the stringent ''plain and obvious'' standard, the Court stated that it suffices that there be a chance

that the applicant might succeed for the matter to be allowed to proceed. As expressed by *JP Morgan* (2014 DTC 5001 (FCA)): "There must be a "show stopper" or a "knockout punch"— an obvious, fatal flaw striking at the root of this Court's power to entertain the application". The Court ruled that it is not plain and obvious that the application cannot succeed, is "bereft of any possibility of success". The Court states that if there was an assessment, clearly there would be that knockout punch. But in the absence of a tax assessment, the Court is not persuaded that the test is satisfied. The Court is convinced that a full record is needed to address the various issues involved, which may well be contentious. They are not ripe for a motion to strike. In the view of the Court, this matter, including the preliminary issues, is deserving of its day in court. As a result, the motion to strike is dismissed.

Westminster v. Canada (AG)

2019 DTC 5047

Whether bankrupts honest but unfortunate bankrupts entitled to discharge

Mr. Ebenal and Mrs. Ebenal operated a residential renovation services business and a hair dressing business through a numbered corporation. The Ebenals' financial difficulties began in 2013 when Mr. Ebenal discovered that his pension had been embezzled and his savings had been lost. When the Ebenals made assignments into bankruptcy for the first time on January 24, 2018, Mr. Ebenal's tax debt amounted to $218,168 in tax plus $200,568 in penalties and interest, and Mrs. Ebenal's tax debt amounted to $216,532 plus $195,668 in penalties and interest. The Minister opposed the Ebenals' application to the Court of Queen's Bench for Saskatchewan for a discharge on the grounds that both bankruptcies were tax driven and that there was surplus income available for the creditors.

The Ebenals' application was granted. There is a presumption that a bankrupt who fails to pay income tax owing is a dishonest debtor (see, for example, *Re Lattery* 2018 SKQB 281). In the present proceedings, however, the Ebenals rebutted this presumption in the absence of any evidence of their dishonesty, and in fact they did not know that they had earned the amount leading to the CRA assessments in issue. The Ebenals were, therefore, honest but unfortunate bankrupts who were entitled to a discharge. As a result, Mrs. Ebenal was discharged after serving a one-day suspension, and Mr. Ebenal was discharged on the condition that he pay a $217 fee owing to the Trustee.

Ebenal (Re)

2019 DTC 5044

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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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