Docket: 2010-3733(IT)I

BETWEEN:

SHEILA SYMONDS,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on May 3, 2011 at Vancouver, British Columbia

Before: The Honourable Justice Wyman W. Webb

Appearances:

For the Appellant:	The Appellant herself
Counsel for the Respondent:	Holly Popenia

JUDGMENT

The Appellant's appeal in relation to the assessment of the penalty imposed pursuant to subsection 163(1) of the *Income Tax Act* in relation to the income tax return that she filed for 2008 is allowed and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that the penalty imposed pursuant to subsection 163(1) of the *Income Tax Act* in relation to the income tax return that she filed for 2008 is deleted.

The Respondent shall pay costs to the Appellant in the amount of $750.

Signed at Ottawa, Canada, this 20th day of May, 2011.

"Wyman W. Webb"

Webb, J.

Citation: 2011TCC274
Date: 20110520
Docket: 2010-3733(IT)I

BETWEEN:

SHEILA SYMONDS,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Webb, J.

[1] The issue in this appeal is whether the penalty that was imposed pursuant to subsection 163(1) of the *Income Tax Act* (the "*Act*") in relation to an amount that the Appellant failed to include in computing her income in her tax return that she filed for 2008 should be upheld or deleted. This subsection provides as follows:

> 163. (1) Every person who
>
> (a) fails to report an amount required to be included in computing the person's income in a return filed under section 150 for a taxation year, and
>
> (b) had failed to report an amount required to be so included in any return filed under section 150 for any of the three preceding taxation years
>
> is liable to a penalty equal to 10% of the amount described in paragraph (a), except where the person is liable to a penalty under subsection (2) in respect of that amount.

[2] Subsection 163(3) of the *Act* provides that:

> 163. (3) Where, in an appeal under this Act, a penalty assessed by the Minister under this section or section 163.2 is in issue, the burden of establishing the facts justifying the assessment of the penalty is on the Minister.

The penalty under subsection 163(1) of the *Act* is imposed on a person who fails to report, in that person's tax return that was filed for a particular year, an amount that is

required to be included in computing that person's income and also failed to report in a tax return that was filed for any one of the three preceding taxation years an amount that was required to be included in computing that person's income for such year.

[3] In *Saunders* v. *The Queen*, 2006 TCC 51, 2006 D.T.C. 2267, [2006] 2 C.T.C. 2255, Justice Woods stated that:

> 12 The penalty in subsection 163(1) is one of strict liability, although this Court has held that it can be vacated if the taxpayer can establish due diligence.

[4] Justice Boyle in *Dunlop* v. *The Queen*, 2009 TCC 177, 2009 D.T.C. 650, [2009] 6 C.T.C. 2223 reiterated that the penalty will not apply if the taxpayer "can demonstrate he exercised a requisite degree of due diligence".

[5] Justice Létourneau, on behalf of the Federal Court of Appeal, in *Les Résidences Majeau Inc.* v. *The Queen*, 2010 FCA 28, stated as follows:

> 7 As far as the penalty is concerned, we are satisfied that the judge did not make any mistake in upholding it. To avoid this penalty, the appellant had to establish that it was duly diligent.
>
> 8 According to *Corporation de l'école polytechnique* v. *Canada*, 2004 FCA 127, a defendant may rely on a defence of due diligence if either of the following can be established: that the defendant made a reasonable mistake of fact, or that the defendant took reasonable precautions to avoid the event leading to imposition of the penalty.
>
> 9 A reasonable mistake of fact requires a twofold test: subjective and objective. The subjective test is met if the defendant establishes that he or she was mistaken as to a factual situation which, if it had existed, would have made his or her act or omission innocent. In addition, for this aspect of the defence to be effective, the mistake must be reasonable, i.e. a mistake a reasonable person in the same circumstances would have made. This is the objective test.
>
> 10 As already stated, the second aspect of the defence requires that all reasonable precautions or measures be taken to avoid the event leading to imposition of the penalty.

[6] Although the penalty in issue is not identified in this decision of the Federal Court of Appeal, it appears from the decision[1] of Justice Tardif which was appealed to the Federal Court of Appeal that the penalty in issue is the penalty that was, prior

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[1] 2009 TCC 286, [2009] G.S.T.C. 90, [2009] 2009 G.S.T.C. 118.

to April 1, 2007, imposed under section 280 of the *Excise Tax Act*. The imposition of this penalty was also subject to the due diligence defence (see *Pillar Oilfield Projects Ltd.* v. *The Queen,* [1993] G.S.T.C. 49).

[7] The calculation of the amount of the penalty under subsection 163(1) of the *Act* is based only on the second amount that the taxpayer has failed to include in income. It is the position of the Respondent that the due diligence defence is only available to a taxpayer in relation to the failure to include this second amount in income. In this case, the two years for which the Appellant failed to include all of the amounts in her income were 2006 and 2008. The Respondent's position is that neither the amount of the first omission nor the circumstances related to the first omission are relevant. It is the Respondent's position that the Respondent is only required to establish that an amount (even $1) was not included in income in one year and a penalty can then be imposed if the taxpayer fails to include an amount in income in another year within the next three years, subject to a defence of due diligence, if one can be established by the taxpayer, in relation only to the second failure to include an amount in income.

[8] The penalty imposed in this case is in relation to unreported employment earnings of $28,611 for 2008. The Appellant had worked for Bowring prior to 2008 but had worked at another retail store (Fossil Canada Inc.) in 2008 before returning to Bowring. In filing her income tax return for 2008 (which was prepared by an accountant) she reported her employment earnings from Fossil Canada Inc. in the amount of $16,851 but she did not report her employment earnings from Bowring in the amount of $28,611. Income tax would have been deducted by Bowring and remitted to the Canada Revenue Agency in relation to the Appellant's employment earnings. The Appellant stated that as soon as she became aware that the amount had not been included, her accountant prepared a revised income tax return and the difference was an additional amount of less than $400 that was payable, which the Appellant promptly paid.

[9] Copies of the notices of reassessment for 2008 and for 2006 were introduced during the hearing. The notice of reassessment for 2008 (which was dated October 1, 2009) indicates that the difference between the total payable by the Appellant (including federal and provincial income tax), as a result of the reassessment (including the employment income from Bowring) and the total payable by the Appellant (including federal and provincial income tax) based on the return as filed, (in each case excluding the penalty that is in issue in this appeal) was as follows:

Total Payable (as reassessed):	($1,902)

Minus: Total Payable (as filed):	- ($3,274)
Difference (additional amount payable):	$1,372

[10] Therefore instead of the Appellant receiving a refund of $3,274 (which is the amount of the refund that the Appellant would have claimed in her tax return) the Appellant should have received a refund of $1,902. Both of these amounts would include amounts under the *Act* as well as under the *Income Tax Act* (British Columbia). The total amount of the penalty imposed under subsection 163(1) of the *Act* was $2,861.10 and since a penalty was also imposed under the *Income Tax Act* (British Columbia), the total penalty imposed in relation to this failure to report income was $5,722 which was 417% of the additional amount payable by the Appellant ($1,372) when the additional income tax that was deducted by Bowring is taken into account.

[11] The Appellant was subsequently reassessed on November 30, 2009 to increase the deductions from total income and hence to reduce the amount payable for 2008. The total amount payable by the Appellant for 2008 based on this notice of reassessment (excluding the penalty that is in issue in this appeal) was ($2,907). Therefore, based on this reassessment, the Appellant should have received a refund of $2,907 for 2008 instead of the refund of $3,274 that she had claimed. The reduction in the refund (which was a result of the increase in the amount payable by the Appellant) for 2008 was $367. When all of the income of the Appellant, all of the deductions available to the Appellant and the total amount of income tax deducted by all of her employers are taken into account, the difference between the amount payable as reported by the Appellant and the amount that was actually payable for that year was only $367. No adjustment was made to the penalty as a result of the reassessment dated November 30, 2009 and therefore the penalty in the amount of $5,722 remained. This penalty was 1,559% of the additional amount that was payable by the Appellant for 2008.

[12] In *Khalil* v. *The Queen*, [2002] T.C.J. No. 538, [2003] 1 C.T.C. 2263, Justice Mogan allowed an appeal from the assessment of a penalty under subsection 163(1) of the *Act* where the income amount that the person had failed to report was income from employment from which income tax had been deducted. Justice Mogan stated as follows:

> 13 I cannot conclude that a person has "failed to report an amount" within the meaning of subsection 163(1) when the person knows (i) that the amount was payable to her as income by a particular payor; (ii) that the payor withheld a certain portion of the amount as income tax to remit to Revenue Canada; (iii) that the payor

actually paid to the person only the balance remaining after deducting the tax withheld; and (iv) that the payor was required to report to Revenue Canada on a form prescribed by Revenue Canada the gross amount payable to the person and the portion withheld and remitted as tax….

[13] In *Alcala* v. *The Queen*, 2010 TCC 198, 2010 DTC 1147, [2010] 5 C.T.C. 2001, Justice Little, after quoting excerpts from the decision of Justice Mogan in *Khalil*, (including the excerpt quoted above) stated that:

> 26 To paraphrase Justice Mogan's decision from *Khalil*, I wish to state the following:
>
> > I cannot conclude that the Appellant has "failed to report an amount" within the meaning of subsection 163(1) when the Appellant, Ms. Alcala, knows:
> >
> > (a) that the payor (Total Credit Recovery) withheld a certain portion of the amount as income tax to remit to the Canada Revenue Agency (the "CRA");
> > (b) that the payor withheld a certain amount as an Employment Insurance Premium and withheld a certain amount as a Canada Pension Plan deduction and remitted these amounts to the CRA;
> > (c) that the payor actually paid to the person only the balance remaining after deducting the tax withheld plus the EI premium and the CPP deduction;
> > (d) that the payor was required to report to the CRA on a form prescribed by the CRA the gross amount payable to the person and the amounts withheld and remitted as tax; and
> > (e) that the Appellant testified that she had never received the T-4 slip issued by the payor for the 2006 taxation year.

[14] In *Peterson* v. *The Queen,* 2010 TCC 559, Justice Pizzitelli stated that:

> 14 Unlike the case of *Khalil v. Canada,* [2003] 1 C.T.C. 2263, relied upon by the appellant, where the penalty was greater than the tax liability as in the case here, the taxpayer there spoke little English and was a new immigrant unaware of the workings of our tax system and hence met the due diligence defence. The *Khalil* case has been considered many times by the Courts in argument including in *Re Saunders* above and treated in my view as restricted to its unique facts.
>
> 15 It does not in my view stand for the proposition that a taxpayer had not "failed to report an amount" where that person knows that:
>
> > 1) the amount was payable to her as income by a payor;

2) the payor withheld a certain portion of the amount as tax to remit to the tax authority;

3) the payor only paid the person the balance remaining after deducting the tax and

4) the payor was required to report to the tax authority the gross income and deductions in prescribed form,

as counsel for the appellant takes in following the dictum of Mogan, Tax Court of Canada Judge, in paragraph 13 of that case.

[15] In *Franck* v. *The Queen*, 2011 TCC 179, Justice Hogan stated as follows:

> 7 This reasoning was relied upon by the Tax Court of Canada in *Iszcenko v. The Queen* * and *Alcala v. The Queen* * in ruling in favour of the taxpayers. In *Iszcenko*, the taxpayer believed she did not have to report the income because it was a return of capital dividend and had been informed by her father-in-law to that effect.* In *Alcala*, the taxpayer relied on her accountant's statement that she was not required to do anything in respect of a late T4 since the CRA would automatically correct through matching.* In both cases the taxpayers were relatively inexperienced with the Canadian tax system. *Iszcenko* dealt with a more complex income scenario while *Alcala* was factually similar to *Khalil*.
>
> 8 The following are some examples of facts which have not been considered as supporting a defence of due diligence. Where a taxpayer was unable to get a T4 because her employer went out of business and her accountant failed to estimate her income using her record of employment, there was no due diligence since the taxpayer had failed to review her tax return before filing.* Similarly, where a taxpayer who had failed to give his T4 to his accountant believed that the CRA would correct the omission and where that taxpayer failed to verify the return before filing, there was no exercise of due diligence.* Finally, where the T4s were given by a taxpayer to her mother, who prepared her tax return, and where the taxpayer did not review the final product, there was no due diligence.*
>
> 9 What distinguishes these lines of cases from one another is the taxpayer's familiarity with the tax system. *Khalil* and *Alcala* involved inexperience while in *Iszcenko* there was a more complex income scenario. Woods J., in *Sounders*, highlighted the inexperience aspect of *Khalil* before declining to extend *Khalil* to Ms. Saunders' situation.* Similarly in *Paul*, Sheridan J. noted the fact that the taxpayer was a long-time member of the workforce as showing the unreasonableness of his belief. *Porter* did not involve a mistaken belief; rather, what was involved was simply a reliance on the tax return preparer to include the amounts from all T4s.
>
> (* denotes a footnote reference that was in the original text but which has not been included.)

[16] It seems to me that the Appellant cannot simply rely on the fact that income tax was deducted at source to avoid the penalty imposed under subsection 163(1) of the *Act*. It must be remembered that an individual's income is also relevant for the purposes of determining that individual's entitlement to a goods and services tax credit under section 122.5 of the *Act*, and, if applicable, a child tax benefit under section 122.6 of the *Act*. In order to avoid the imposition of the penalty, the Appellant must establish that the requirements of the due diligence defence, as set out by the Federal Court of Appeal in *Les Résidences Majeau Inc.*, referred to above, have been satisfied. In any event, in this case the Appellant was familiar with the tax system as she had been an employee for a number if years and had filed tax returns for several years.

[17] The Appellant did not review her tax return for 2008 before she filed it. The amount of income that was not reported ($28,611) was significant in relation to the amount of income that she did report ($16,851) and would represent 63% of her total employment earnings of $45,462 for 2008.

[18] However the amount that she failed to report for 2006 is significantly less. In that year she failed to report $872 of interest income. Her total income for 2006 (including this interest income) was $37,817. The unreported interest income was therefore only 2.3% of her total income for 2006. It is the position of the Respondent that the Appellant does not have the right to argue that the due diligence defence is available to her in relation to this failure to report $872 in 2006. Counsel for the Respondent did not include the recent decision of Justice Hogan in *Franck* v. *The Queen*, referred to above, in her book of authorities, although she did acknowledge that she was aware of this decision.

[19] In *Franck*, referred to above, Justice Hogan stated as follows:

> 2. …Because subsection 163(1) of the *Act* requires a failure to report in two of four consecutive years, a due diligence defence for either year will nullify the penalty.

[20] Because a case does not support a position being advocated is not a reason to omit the case from the authorities being presented to the Court. Although the *Franck* case was decided under the Informal Procedure, this cannot be the basis for the omission of this case in the Respondent's book of authorities as several of the cases that were included in the Respondent's book of authorities were decided under the Informal Procedure.

[21] The due diligence defence arises as a result of the classification of the offence as a strict liability offence. In *The Queen* v. *The Corporation of The City of Sault Ste. Marie*, [1978] 2 S.C.R. 1299, Justice Dickson (as he then was) writing on behalf of the Supreme Court of Canada stated that:

> I conclude, for the reasons which I have sought to express, that there are compelling grounds for the recognition of three categories of offences rather than the traditional two:
>
> 1. Offences in which mens rea, consisting of some positive state of mind such as intent, knowledge, or recklessness, must be proved by the prosecution either as an inference from the nature of the act committed, or by additional evidence.
>
> 2. Offences in which there is no necessity for the prosecution to prove the existence of *mens rea*; the doing of the prohibited act *prima facie* imports the offence, leaving it open to the accused to avoid liability by proving that he took all reasonable care. This involves consideration of what a reasonable man would have done in the circumstances. The defence will be available if the accused reasonably believed in a mistaken set of facts which, if true, would render the act or omission innocent, or if he took all reasonable steps to avoid the particular event. These offences may properly be called offences of strict liability. Mr. Justice Estey so referred to them in Hickey's case.
>
> 3. Offences of absolute liability where it is not open to the accused to exculpate himself by showing that he was free of fault.

[22] There are numerous cases that have held that a defence of due diligence, if established, may be relied upon by a taxpayer to avoid a penalty imposed under subsection 163(1) of the *Act*. The Respondent did not argue that the Appellant did not have the right to argue that such a defence was available but rather argued that the defence could only be argued in relation to the failure to include the amount in income in 2008 and not in relation to the failure to include the amount in income for 2006. However, it seems to me that since the penalty can only be imposed if a particular taxpayer fails to include an amount in income in two different years, the “prohibited act” consists of two failures - one is the failure to include an amount in income in one year and the second is the failure to include an amount in income in another year that is within three years following the first failure.

[23] Therefore if a taxpayer, as stated by Justice Hogan, can establish that he or she (or in the case of a corporation, it) exercised due diligence in relation to either the first failure to include an amount in income or the second failure to include an amount in income, then that taxpayer will be successful in relation to the assessment

of a penalty under subsection 163(1) of the *Act*. Even though the calculation of the amount of the penalty is only based on the second amount that the person failed to include in computing income, in order for the penalty to be imposed the person must have failed to include amounts in computing income in two different years and the two failures to include amounts in computing income would be part of the "prohibited act". In this case the Appellant will be successful if she can establish that she exercised due diligence in relation to either her failure to include $872 in her income for 2006 or her failure to include $28,611 in her income for 2008.

[24] As noted by the Federal Court of Appeal in *Les Résidences Majeau Inc.*, referred to above:

> 8 … a defendant may rely on a defence of due diligence if either of the following can be established: that the defendant made a reasonable mistake of fact, or that the defendant took reasonable precautions to avoid the event leading to imposition of the penalty.
>
> 9 A reasonable mistake of fact requires a twofold test: subjective and objective. The subjective test is met if the defendant establishes that he or she was mistaken as to a factual situation which, if it had existed, would have made his or her act or omission innocent. In addition, for this aspect of the defence to be effective, the mistake must be reasonable, i.e. a mistake a reasonable person in the same circumstances would have made. This is the objective test.

[25] In this case the Appellant was mistaken with respect to whether she had included all of her income in her tax return for 2006. I am satisfied that it is more likely than not that the Appellant had innocently missed the amount of $872 in completing her return for 2006. The amount is small compared to her total income and as soon as she received the notice of reassessment she promptly paid the amount owing. The amount omitted was only 2.3% of her total income for 2006 and therefore she had reported 97.7% of her total income for that year.

[26] The tax return for the Appellant for 2006 was not introduced. Only the reconstructed notice of assessment and the reconstructed notice of reassessment for 2006 were introduced. These notices only indicate the total income amounts – there is no indication of the amount of income reported from each source. Therefore there is nothing to indicate whether the Appellant had reported any interest income in 2006. It is not clear whether the Appellant has a copy of her 2006 income tax return. It was not established whether she has a copy or not. It is clear, however, that since the Appellant filed her tax return for 2006 that the Respondent would have the income tax return that was filed by the Appellant.

[27] In the *Law of Evidence in Canada*, third edition, by Justice Lederman, Justice Bryant and Justice Fuerst of the Superior Court of Justice for Ontario, it is stated at p. 377 that:

> **§6.449** In civil cases, an unfavourable inference can be drawn when, in the absence of an explanation, a party litigant does not testify, or fails to provide affidavit evidence on an application, or fails to call a witness who would have knowledge of the facts and would be assumed to be willing to assist that party. In the same vein, an adverse inference may be drawn against a party who does not call a material witness over whom he or she has exclusive control and does not explain it away. Such failure amounts to an implied admission that the evidence of the absent witness would be contrary to the party's case, or at least would not support it.*
>
> **§6.450** An adverse inference should be drawn only after a *prima facie* case has been established by the party bearing the burden of proof.*
>
> (* denotes a footnote reference that is in the original text but which has not been included.)

[28] It seems to me that this can also apply to a failure to produce a document that is within the exclusive control of a party. In this case that document is the income tax return of the Appellant. While the Appellant may have retained a copy, the original return would have been filed with the Canada Revenue Agency and therefore the Respondent would have exclusive control over the tax return that was filed by the Appellant for 2006. No satisfactory explanation was provided for the failure to introduce the Appellant's income tax return for 2006.

[29] In this case the Respondent has the burden of establishing the facts justifying the assessment of the penalty and the Appellant has the burden of establishing the facts that would support a due diligence defence. In my opinion the Appellant did establish a *prima facie* case for a due diligence defence as the amount that she failed to report for 2006 was only 2.3% of her total income for 2006 and I am satisfied that any failure to include that amount was innocent. It seems to me that, *prima facie,* a reasonable person could also have made the same mistake.

[30] It should also be noted that the Respondent was represented by counsel and the Appellant represented herself. It seems to me that an unfavourable inference can be drawn from the failure of the Respondent to introduce the income tax return that the Appellant had filed for 2006. The negative inference that I draw is that the return would have disclosed such other interest income that was reported so that a

reasonable person would have made the same mistake as the Appellant did in these circumstances.

[31] As a result the appeal is allowed and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that the penalty imposed pursuant to subsection 163(1) of the *Income Tax Act* in relation to the income tax return that the Appellant filed for 2008 is deleted.

[32] The Respondent shall pay costs to the Appellant in the amount of $750.

Signed at Ottawa, Canada, this 20th day of May, 2011.

"Wyman W. Webb"

Webb, J.

CITATION:	2011TCC274
COURT FILE NO.:	2010-3733(IT)I
STYLE OF CAUSE:	SHEILA SYMONDS AND HER MAJESTY THE QUEEN
PLACE OF HEARING:	Vancouver, British Columbia
DATE OF HEARING:	May 3, 2011
REASONS FOR JUDGMENT BY:	The Honourable Justice Wyman W. Webb
DATE OF JUDGMENT:	May 20, 2011

APPEARANCES:

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Counsel for the Respondent:	Holly Popenia

COUNSEL OF RECORD:

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