

Federal Court



Cour fédérale

Date: 20180123

Docket: T-557-17

Citation: 2018 FC 59

Toronto, Ontario, January 23, 2018

PRESENT: The Honourable Mr. Justice Campbell

BETWEEN:

REFERRED REALTY INC.

Applicant

and

ATTORNEY GENERAL OF CANADA

Respondent

JUDGMENT AND REASONS

[1] On January 12, 2012, the Respondent Minister of National Revenue of Canada (Minister) garnished \$615,000 from the Applicant's bank account because of the Applicant's failure to file required tax returns and an ensuing arbitrary assessment of a tax liability of \$155,000. In response, pursuant to s. 221.2 of the *Income Tax Act (ITA)*, the Applicant made a request to the Minister to exercise discretion to grant re-appropriation of statute-barred credits against future tax liability in the amount of \$185,817.71, being the monies remaining from the garnishment

after the payment of all outstanding taxes and \$50,000 of penalties for late filing (see: Amended Notice of Application, paras. 10, 12, 13, and 14).

[2] By a decision dated January 10, 2017 (Decision) presently under review, a Delegate of the Minister (Delegate) rejected the Applicant's request. The central issue raised in the present Application is whether the Decision is reasonable. For the reasons that follow, I find that the Decision is unreasonable because it lacks justification (see: *Dunsmuir v New Brunswick*, 2008 SCC 9 at para. 47).

I. The Applicant's Failure to File

[3] In addition to the information provided in the Delegate's Decision as quoted below, the nature of the accounting problems experienced by the Applicant resulting in failure to file were reported to the Respondent Minister by the Applicant's accountants in a letter dated July 21, 2014:

Extraordinary circumstances

The taxpayer maintains a realty brokerage business in North Toronto. The business commenced operations in the beginning of 2004. The taxpayer hired an experienced administrator to run the accounting and administration function of the office. This individual maintained the records adequately through the fiscal years ended July 2004 and July 2005. Some small administrative suggestions were provided by the accountants but overall the accounts were complete and accurate.

A number of concerns were raised by the accountants in regards to the accounting records of the company while completing the 2006 year-end. The accountants spent a considerable amount of time in reviewing and analyzing the records and ultimately booked a number of adjustments to ensure the accounts were accurate. A number of concerns were raised at that time and they were taken

up with the office administrator and the shareholder president. The office administrator was terminated shortly thereafter.

After the administrator was terminated, it was determined that he had not been keeping up with his work requirements. The accounting records for the period subsequent to the July 31, 2006 year-end were incomplete and in many cases, documents were either misplaced or missing altogether. At that time, the taxpayer commenced a project to bring these records up to date. Unfortunately, the scope of the task was larger than expected and when the time came to file the T2 for the year-ended July 31, 2007, the accountants expressed concerns that there were too many unanswered questions to file an accurate tax return. Consequently, the taxpayer remitted an amount equal to the estimated income tax prior to the T2 tax filing deadline.

The taxpayer continued to attempt to bring the records up to date with the assistance of a new office administrator. However, this individual also turned out to be incapable to the task and misled both the president and the accountant as to the status of both the historical information and information relevant for years subsequent to July 31, 2007. This person was also terminated in the middle of 2009.

The taxpayer engaged an outside bookkeeper to go through the records from August 1, 2006 forward in an attempt to reconstruct all transactions and bring the filings up to date. Due to the volume of the task and a number of other factors, including some employee illnesses, this process took an extended period. In the meantime, the taxpayer estimated its taxes for each taxation year and remitted payment based on the estimates to meet its expected tax obligation. In early 2012, the accounts were finally brought into a state where filing could be completed for the year-ended July 31, 2007 and then subsequent periods through July 31, 2011. These filings were completed by July 2012.

Despite the difficulties the taxpayer was experiencing in bringing its accounting records into order, the taxpayer respected the fact that it had an obligation to pay tax and taxes were remitted for each period based on an estimate of the taxes payable based on their best attempt to determine the taxable income for each year. Reasonable efforts were made to rectify the bookkeeping problems and bring the accounts to a state where accurate returns could be filed.

[Emphasis added]

(Certified Tribunal Record (CTR), pp. 48-49)

II. The Minister's Policy

[4] In assessing the request pursuant to s. 221.2(1) of the *ITA*, the Minister may have regard to the *User Guide, Re-appropriation of T2 statute-barred Credits (Business Accounting Programs, December 2016)*, which states:

Guidelines

The following requirements must be met in order to request a re-appropriation of a statute-barred credit:

[...]

4. The corporate taxpayer must be compliant with all of its filing obligations before the CRA will consider re-appropriating a statute-barred credit.

[...]

Extraordinary circumstances

This section provides examples of various extraordinary circumstances and guidelines for evaluating them.

The types of circumstances beyond a taxpayer's control that may have prevented a taxpayer from filing their T2 return within three years from their tax year end may be summarized by, but not limited to, the following examples:

- natural or human-made disasters such as flood, heavy storms, or fire;
- civil disturbances or disruptions in services such as strikes or demonstrations;
- serious illness or accident; and
- serious emotional or mental stress caused by death, or loss or employment, accident in the immediate family, marital separation, or loss of employment.

[...]

CRA error or delay

The application of ministerial discretion may be warranted when the T2 statute-barred credit is a result of CRA action and through no fault of the taxpayer.

[...]

Other circumstances

The CRA may also apply ministerial discretion if a taxpayer's circumstances do not fall within the situations described above. Each case must be reviewed based on its own circumstances.

[Emphasis added]

(CTR, pp. 128, 168, 171-172)

III. The Decision

[5] The January 10, 2017 Decision under review provides basic uncontested facts and the outcome being challenged:

Re: Re-appropriation of T2 Statute-barred Credits

Dear Sir or Madam,

We apologize for the delay in responding to your request for a second- review of our decision to deny re-appropriation of the statute-barred credit of \$191,734.89 from the July 31, 2007, tax year-end.

Based on the information you provided in your correspondence dated March 11, 2016, we have upheld the original decision not to re-appropriate the statute-barred credits for the tax year-end noted above. Below, we have outlined the information we considered during our second review and the reasons for our decision.

You stated that the taxpayer did not wilfully ignore its obligations to file its returns of income in a timely manner. You also stated that in each of its 2007 to 2010 taxation years, the corporation paid all of the estimated taxes owing for that taxation year and that the

corporation had no intention to avoid its obligation to pay its tax liability as determined under the Income Tax Act. Furthermore, you stated that the taxpayer was unaware of the necessity of filing a return of income within three years in order to be able to receive a refund under subsection 164(1) of the Income Tax Act and that the corporation relied on the advice of its professional tax advisor that it should not file its returns of income until its books and records were in satisfactory condition. You also stated that you do not believe that the Minister's ability to re-appropriate is dependent upon whether a taxpayer has justifiable explanation for why its return of income was not filed.

Our records indicate that the Canada Revenue Agency issued several requests to the corporation to file missing returns. On October 21, 2008, the Canada Revenue Agency issued a Request to File letter for the 2007 tax year-end. On December 2, 2008, the Canada Revenue Agency issued a Second Request to File letter for the 2007 corporate tax year-end. The Canada Revenue Agency issued a letter dated March 2, 2011, stating that the corporate returns for the 2007, 2008, 2009 and 2010 corporate tax year-ends were outstanding and that if the returns were not filed by April 29, 2011, the Canada Revenue Agency may issue arbitrary assessments to those tax years. Although the corporation was made aware of its tax obligations, it did not comply with these requests. This indicates that the corporation knowingly had not taken measures to correct the non-compliance within a reasonable timeframe.

In your letter dated March 11, 2016, you noted that taxes were actually remitted when due. Corporation taxes are due either 2 or 3 months following their tax year-end depending on their type or information they report. Based on our records, the taxes were not remitted by the statutory due date for this corporation in any of the tax years outlined in your letter (i.e. 2007 to 2010). For example, for the tax year-end in question (July 31, 2007), the balance due date was October 31, 2007; however, the payment for this period was not remitted until January 31, 2008. We do not agree that this demonstrates due diligence of the taxpayer in upholding his obligations.

The subsection 150(1)(a) of the Income Tax Act requires that a corporation files income tax returns. Similarly, the subsection 230(1) of the Income Tax Act requires every person carrying on business and every person who is required to pay or collect taxes or other amounts to keep records and books of account in such form and containing such information as will enable the taxes payable to be determined.

The Canada Revenue Agency is committed to making information available to assist taxpayers understand their tax obligations. Corporation's filing and payment requirements as well as the limitation on receiving refunds if returns are not filed on time are explained in the T2 Corporation Income Tax Guide, within our website www.cra-arc.gc.ca. Similarly, the requirement to maintain adequate books and records is explained in the Information Circulars ICO5-1, Electronic Record Keeping, and IC78-10, Books and Records Retention/Destruction. The circulars explain that the taxpayer is not relieved of the responsibility of maintaining adequate books and records when they use services of a third party. This information can also be obtained through our toll-free enquiry line (800) 959-5525.

The subsection 221.2 of the Income Tax Act is discretionary. Discretion is typically exercised to relieve negative consequences due to circumstances which prevented the taxpayer from meeting his tax obligations. However, these circumstances must be demonstrated to have been outside of the taxpayer's control and the taxpayer should be able to demonstrate how he corrected any delay or omission within a reasonable time after he or she became aware of it.

From the information you provided, it appears the reason that prevented the taxpayer from meeting his obligations was due to an inability to keep adequate books and records for his corporation.

Keeping adequate books and records and filing tax returns are requirements under the Income Tax Act. The taxpayer reported that he was aware of the problem in 2006, and there is evidence of multiple written correspondences from the CRA advising the corporation of its late or missing returns. The taxpayer did not demonstrate that sufficient action was taken to remedy this situation within a reasonable timeframe as returns continued to remain outstanding until 2012.

Finally, during our review, we have also reviewed the corporation's current general filing compliance. Our records indicate that this corporation was required to file their GST returns on a monthly filing frequency since January 1, 2006; however, we have noted several occasions when returns were not filed on time and Failure to File Penalties were applied. Our current records also indicate that there is an overdue return on the corporation's [...] program account. The corporation must be filed up to date for all program accounts before considering re-appropriation of the T2 statute-barred credits.

Based on the information you provided and our review, we will not exercise Ministerial discretion to re-appropriate the statute-barred credits for the July 31, 2007 tax year-end because the corporation had knowledge that it was not complying with their corporation filing requirements, it was also aware of the source of the issue however did not take sufficient action to resolve it within a reasonable timeframe in order to comply with its filing obligations to the Income Tax Act.

If you believe this decision is not fair, you can apply to the Federal Court for a judicial review. [...]

[Emphasis added]

(CTR), pp. 79-80)

IV. Justification

[6] In my view, the Delegate was required to state a clear and supportable justification to deny the Applicant's re-appropriation request given the large sum of money under consideration.

[7] As outlined above, by the letter of July 21, 2014, the Delegate was advised of the serious problems encountered by the Applicant in re-structuring the corporation's financial affairs due to issues not of the Applicant's own making. There is no evidence that the Applicant was intentionally neglecting or avoiding its responsibility to maintain proper records. To the contrary, the evidence establishes that the Applicant's active efforts were directed to meeting its responsibility, and in the end result, upon professional advice, once the financial affairs were placed in order, all taxes and penalties were paid without objection or request for relief.

[8] With respect to consideration of whether the Applicant conformed to the "Extraordinary" and "Other" features of the Minister's Policy, the emphasized passages in the Decision makes it

clear that the Delegate's decision-making was centred on compliance with the statutory requirement that tax payers, including the Applicant, must keep adequate books and records. Without critical analysis of the Applicant's evidence of best efforts to meet the statutory requirement, the Delegate found that his or her subjective expectations were not met. As emphasised in the Decision, the Delegate made the statement that "the taxpayer did not demonstrate that sufficient action was taken to remedy this situation within a reasonable timeframe as returns continued to remain outstanding until 2012" without clarification of what "sufficient action" was expected, and what "reasonable timeframe" was expected.

[9] In my opinion, the statement is the only clear reason supplied in the Decision for refusing the Applicant's re-appropriation request. Read in context, I find that the statement constitutes the delivery of a punishment to the Applicant for perceived failure to meet the Delegate's unclear expectations. During the course of the hearing of the present Application, when this tentative finding was placed before Counsel for the Respondent for comment, no argument was presented in response that the finding is supportable in fact or law. In the result, I find that the Delegate's delivery renders the Decision unreasonable.

[10] As an adjunct feature of the delivery, the Delegate relied on the Applicant's GST record. Throughout the transaction between the Applicant and the Minister respecting the re-appropriation request, the GST record was not introduced as an issue. I find that, not only was it unfair for the Delegate to include it in the decision-making process without providing advance notice and an opportunity for the Applicant to respond, it is an extraneous consideration the introduction of which, in and of itself, renders the Decision under review as unreasonable.

V. Conclusion

[11] For the reasons provided, there is no justification in the Decision for rejecting the Applicant's request for re-appropriation of the statute-barred credit.

JUDGMENT

THIS COURT'S JUDGMENT is that the Decision under review is set aside, and the matter is referred back to the Minister for redetermination on the following direction:

The redetermination be conducted on a full and careful consideration of all the evidence with respect to the Applicant's efforts to comply with the *Income Tax Act*.

“Douglas R. Campbell”

Judge

FEDERAL COURT
SOLICITORS OF RECORD

DOCKET: T-557-17

STYLE OF CAUSE: REFERRED REALTY INC. v ATTORNEY GENERAL
OF CANADA

PLACE OF HEARING: TORONTO, ONTARIO

DATE OF HEARING: JANUARY 16, 2018

JUDGMENT AND REASONS: CAMPBELL J.

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