

Federal Court of Appeal



Cour d'appel fédérale

Date: 20150522

Docket: A-257-14

Citation: 2015 FCA 134

**CORAM: GAUTHIER J.A.
WEBB J.A.
RENNIE J.A.**

BETWEEN:

KINGLON INVESTMENTS INC.

Appellant

and

HER MAJESTY THE QUEEN

Respondent

Heard at Toronto, Ontario, on April 27, 2015.

Judgment delivered at Ottawa, Ontario, on May 22, 2015.

REASONS FOR JUDGMENT BY:

WEBB J.A.

CONCURRED IN BY:

**GAUTHIER J.A.
RENNIE J.A.**

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REASONS FOR JUDGMENT

WEBB J.A.

[1] Graham J. of the Tax Court of Canada allowed the motion of Kinglon Investments Inc. (Kinglon) and struck certain parts of the Reply filed by the Crown (2014 TCC 131). The Tax Court Judge also granted the Crown leave to file an amended Reply. Kinglon has appealed from this order insofar as it granted the Crown leave to file an amended Reply and the Crown has cross-appealed from this order insofar as it struck the parts in question from the Reply and awarded costs.

Background

[2] Kinglon was reassessed for several taxation years to deny all of the amounts that it had claimed as capital cost allowance in relation to a licence that it had purchased to market a certain heart drug. While the Minister of National Revenue relied on a number of grounds for the reassessments, the ground that is in issue in this appeal is the claim by the Minister that the licence is an unregistered tax shelter.

[3] There are a number of conditions that must be satisfied in order for the licence to be a tax shelter for the purposes of the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) (*Act*). In particular, certain statements or representations must be made with respect to the amount that would be deductible if the licence is acquired. In this case, the Tax Court Judge struck the parts of the Reply related to the claim that the licence was an unregistered tax shelter because, although the Crown identified the particular individuals who were assumed to have made the required statements or representations, the Crown did not specify on whose behalf those individuals were acting when such statements or representations were being made.

[4] For the reasons that follow, I would allow the cross-appeal and dismiss the appeal.

Standard of Review

[5] The decision of the Tax Court Judge to strike part of the Reply is a discretionary interlocutory decision. In *Imperial Manufacturing Group Inc. v. Decor Grates Inc.*, 2015 FCA 100 (paragraphs 18 to 29), Stratas J.A. concluded that the standard of review as set out in *Housen v. Nikolaisen*, [2002] 2 S.C.R. 235, 2002 SCC 33, applies to appeals from such decisions.

Therefore, the standard of review is correctness for questions of law. Findings of fact (including inferences of fact) will stand unless it is established that the Tax Court Judge made a palpable and overriding error. For questions of mixed fact and law, the standard of correctness will apply to any extricable question of law and otherwise the standard of palpable and overriding error will apply. An error is palpable if it is readily apparent and it is overriding if it would change the result.

Test for Striking Pleadings

[6] In *R. v. Imperial Tobacco Canada Ltd.*, 2011 SCC 42, [2011] 3 S.C.R. 45, the Supreme Court of Canada confirmed that a “claim will only be struck if it is plain and obvious, assuming the facts pleaded to be true, that the pleading discloses no reasonable cause of action”, which could also be stated as “the claim has no reasonable prospect of success” (paragraph 17).

Analysis

[7] Since the Crown has cross-appealed on the basis that the Tax Court Judge should not have struck any part of the Reply, I will first address this issue. If the Crown is successful in the cross-appeal, then there will not be any need to address Kinglon’s appeal.

[8] The question in this cross-appeal is whether, assuming the facts as alleged in the Reply are true, the Tax Court Judge erred in assessing whether the Crown has a reasonable prospect of success in relation to its claim that the licence is a tax shelter.

[9] A tax shelter is defined in section 237.1 of the *Act* and is either a gifting arrangement or a property (in respect of which certain conditions are satisfied). In this case, there is no suggestion that there was any gifting arrangement. Therefore, the only relevant parts of the definition of tax shelter in this case are those parts that relate to a property. The relevant parts of this definition of tax shelter are as follows:

“tax shelter” means

...

(b) [...] a property (including any right to income) [...] in respect of which it can reasonably be considered, having regard to statements or representations made or proposed to be made in connection with the [...] the property, that, if a person were to [...] acquire an interest in the property, at the end of a particular taxation year that ends within four years after the day on which the [...] interest is acquired,

(i) the total of all amounts each of which is

(A) an amount, or a loss in the case of a partnership interest, represented to be deductible in computing the person's income for the particular year ... , or

...

would equal or exceed

(ii) the amount, if any, by which

(A) the cost to the person of [...] the interest in the property at the end of the particular year, determined without reference to section 143.2, would exceed

(B) the total of all amounts each of which is the amount of any prescribed benefit that is expected to be received or enjoyed, directly or indirectly, in

« abri fiscal »

[...]

b) [...] bien (y compris le droit à un revenu), [...] pour lequel il est raisonnable de considérer, compte tenu de déclarations ou d'annonces faites ou envisagées relativement [...] au bien, que, si une personne devait conclure [...] acquérir une part dans le bien, le montant visé au sous-alinéa serait, à la fin d'une année d'imposition qui se termine dans les quatre ans suivant le jour [...] la part, acquise égal ou supérieur au montant visé au sous-alinéa (ii)

(i) le total des montants représentant chacun

(A) un montant ou, dans le cas d'une participation dans une société de personnes, une perte qui est annoncé comme étant déductible dans le calcul du revenu de la personne pour l'année [...] ou,

[...]

(ii) l'excédent éventuel du montant visé à la division (A) sur le total visé à la division (B)

(A) le coût, pour la personne, [...] de la part dans le bien à la fin de l'année, déterminé compte non tenu de l'article 143.2,

(B) la valeur totale des avantages [...] avec laquelle elle a un lien de dépendance pourrait recevoir, directement ou indirectement, au titre

<p>respect of the [...] interest in the property, by the person or another person with whom the person does not deal at arm's length.</p>	<p>du bien acquis aux termes de l'arrangement ou au titre de la part dans le bien.</p>
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[10] In order to consider whether the Crown's claim has a reasonable prospect of success, it is necessary to understand the argument that the Crown is making in relation to the definition of tax shelter. In order to be a tax shelter, certain statements or representations must be made. The definition of a tax shelter does not, however, specify either the person who must make the statements or representations, or the person to whom such statements or representations must be made.

[11] In *Baxter v. The Queen*, 2007 FCA 172, [2007] F.C.J. No. 605, the issue that this Court had to decide in relation to the communication of the statements or representations was whether the statements or representations had to be made to the particular taxpayer (paragraph 40 of the reasons). Although Ryer J.A. in paragraph 44 noted that "neither of the parties to this appeal, nor the TCC in its decision, focused much attention on the identity of the party who must have made the statements or representations", he offered the following comments in relation to this issue:

9. The definition requires that statements or representations must be made, at some time, in connection with the property that is offered for sale. If no statements or representations have ever been made in connection with a property, then that property cannot constitute a tax shelter. Because the property that is contemplated by the definition of tax shelter is a property that is assumed to have been acquired by the prospective purchaser and the statements or representations are required to have been made in connection with that property, it follows that the statements or representations must have been made prior to any actual sale of the property that is offered for sale. Further, while the definition does not specify to whom or by whom the statements or representations must be made, in my view they must be made to the prospective purchasers of the property by or on behalf of the person who proposes to sell the property.

...

44. While neither of the parties to this appeal, nor the TCC in its decision, focused much attention on the identity of the party who must have made the statements or representations, in my view, it would be reasonable to conclude that it must be each person who constitutes a promoter, as defined in subsection 237.1(1) (a "promoter").

(emphasis added)

[12] Although the Tax Court Judge, in paragraph 15 of his reasons, stated that “[t]here is, at a minimum, the appearance of a conflict between paragraphs 9 and 44 of *Baxter*”, it seems to me, without deciding the issue, that it is possible that the statements in these paragraphs could be reconciled on the basis that Ryer J.A. was concluding that the required statements or representations had to be made by a promoter who was acting on behalf of the person who is proposing to sell the property.

[13] In Part C of the Reply (Statutory Provisions, Grounds Relied on and Relief Sought) filed in this case, the Crown, in paragraph 17, simply states that the licence was a tax shelter but does not explain the reasoning to support this conclusion. In the memorandum filed in this appeal and during oral argument, the Crown clarified its position, which is that it would be sufficient for the requirements of the definition of tax shelter if the required statements or representations were made by Jay Granatstein, an accountant, and David Rottfleisch, a lawyer, as promoters without the need to specify on whose behalf such statements or representations were made. The Crown is relying on the comments in paragraph 44 of *Baxter* that it would be sufficient if the person making the statements or representations is a promoter. Implicit in this position is that the comments in paragraph 9 of *Baxter* are *obiter*, otherwise the comments in paragraph 9 would be binding on the Tax Court. However, if the comments in paragraph 9 are *obiter*, then the comments in paragraph 44 would also be *obiter*.

[14] The argument of the Crown is based on paragraphs (a) and (c) of the definition of promoter and that it is not necessary that either Mr. Granatstein or Mr. Rotfleisch were acting on behalf of any other person.

[15] The definition of promoter is set out in section 237.1 of the Act:

<p>“promoter” in respect of a tax shelter means a person who in the course of a business</p> <p>(a) sells or issues, or promotes the sale, issuance or acquisition of, the tax shelter,</p> <p>(b) acts as an agent or adviser in respect of the sale or issuance, or the promotion of the sale, issuance or acquisition, of the tax shelter, or</p> <p>(c) accepts, whether as a principal or agent, consideration in respect of the tax shelter, and more than one person may be a tax shelter promoter in respect of the same tax shelter;</p>	<p>promoteur » Personne qui, quant à un abri fiscal et dans le cours des activités d’une entreprise :</p> <p>a) émet ou vend l’abri fiscal ou fait la promotion de son émission, de sa vente ou de son acquisition;</p> <p>b) agit, à titre de mandataire ou de conseiller, en ce qui concerne l’émission ou la vente de l’abri fiscal ou la promotion de son émission, de sa vente ou de son acquisition;</p> <p>c) accepte, à titre de principal ou de mandataire, une contrepartie relativement à l’abri fiscal. Au même abri fiscal peuvent correspondre plus d’un promoteur d’abris fiscaux.</p>
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[16] While initially the Crown was arguing that the two individuals could also be promoters under paragraph (b), the Crown is now only arguing that either paragraph (a) or (c) would be applicable (paragraph 45 of the Crown’s Memorandum) and that the provisions of paragraphs (a) and (c) do not indicate that the person must be acting for someone else.

[17] In his reasons for judgment, the Tax Court Judge noted that:

16 The parties agree that, in Kinglon's case, the statements or representations in question were made by an accountant and / or a lawyer. It appears that one or both of those individuals was acting on behalf of Kinglon at the time. It is possible that one or both of these individuals may have been acting for Cardiopharma either exclusively or in addition to acting for Kinglon.

17 Based on the foregoing, I am not prepared at this point in the proceedings to foreclose the possibility that a judge of this Court, upon hearing all of the evidence, could reasonably conclude that:

(a) a tax shelter can exist regardless of who makes the statements or representations so long as they are made to the taxpayer;

(b) a tax shelter can exist in a circumstance where an individual who acts for both the taxpayer and the vendor makes statements or representations to the taxpayer; or

(c) a tax shelter can exist in a circumstance where an individual, acting solely on behalf of the taxpayer, designs a transaction which will have the desired effect, then arranges for a vendor to participate in the transaction and finally makes statements or representations to the taxpayer.

[18] The Tax Court Judge in paragraph 17(a) noted that a possible interpretation of the *Act* is that “a tax shelter can exist regardless of who makes the statements or representations so long as they are made to the taxpayer”. This statement appears to reflect the position of the Crown that the individuals who make the required statements or representations would not have to be the vendor or someone acting on behalf of the vendor in order for the licence to be a tax shelter. In light of this statement and based on the Crown’s position, it would not follow that the Crown would have to identify the person on whose behalf Mr. Granatstein and Mr. Rotfleisch were making the statements or representations. Although Kinglon argued that paragraph 17(a) is to be interpreted based on the comments of the Tax Court Judge in paragraph 16, in my view, paragraph 17(a) is clear and should not be modified by the Tax Court Judge’s comments in paragraph 16.

[19] Since the Tax Court Judge acknowledged that one possible interpretation of the relevant provisions of the *Act* is that a tax shelter could be found to “exist regardless of who makes the

statements or representations so long as they are made to the taxpayer”, it was a palpable and overriding error on his part to then find that the Reply was deficient because the Crown did not specify on whose behalf the two individuals were making the statements or representations.

[20] The issue before this court in *Baxter* was not related to whether the person making these statements or representations had to be acting on behalf of any other person. Therefore, the comments in paragraphs 9 and 44 of *Baxter* would be *obiter*. While another Court may adopt these comments, the issue in relation to striking pleadings is not whether a person will be successful but whether it is plain and obvious that such person will not be successful. Since these comments are *obiter* and since there is no specific requirement in the definitions of tax shelter or promoter that the person making the required statements or representations must be the person who is attempting to sell the property or must be making such statements or representations on behalf of such person, it is not plain and obvious that the Crown will not be successful.

[21] Since no facts would have to be pled in support of this argument of the Crown, the parts of the Reply related to the allegation that the licence was a tax shelter should not have been struck.

[22] Kinglon has, since it brought its motion before the Tax Court, continuously maintained its position that the legal argument of the Crown is not clear. As noted above, the Crown’s position is not apparent in Part C of the Reply as the Crown simply states that the licence was a tax shelter but does not explain the reasoning to support this conclusion. Before us, the Crown undertook to amend the Reply to clarify its legal argument in relation to why, in the Crown’s

view, the licence is a tax shelter. I would grant leave for the Crown to file an amended Reply to explain such reasoning.

[23] The Tax Court Judge, in paragraph 21 of his reasons, also identified certain other alleged deficiencies in the details provided in the pleadings of the Crown. It seems to me that to the extent that Kinglon may require any further particulars with respect to the any of the pleadings Kinglon could file and serve a demand for particulars as provided in Rule 52 of the *Tax Court of Canada Rules (General Procedure)*, SOR/90-688.

[24] As a result I would allow the cross-appeal and I would dismiss Kinglon's motion to strike the parts of the Reply related to the issue of whether the licence is a tax shelter. As noted above, since I would allow the cross-appeal and not strike the parts of the Reply in issue, there is no need to address Kinglon's appeal.

Proposed Disposition

[25] Therefore, I would:

- (a) dismiss Kinglon's appeal;
- (b) allow the Crown's cross-appeal;
- (c) set aside the Order issued by the Tax Court and dismiss Kinglon's motion to strike the parts of the Reply related to the issue of whether the licence is a tax shelter;
- (d) grant the Crown leave to file and serve, within 30 days of the date of the order of this Court, an amended Reply to clarify the reasoning of why, in the Crown's view, the licence was a tax shelter;

- (e) not award either party costs in the Tax Court; and
- (f) award the Crown costs only in relation to the cross-appeal to this Court.

“Wyman W. Webb”

J.A.

“I agree

Johanne Gauthier J.A.”

“I agree

Donald J. rennie J.A.”

FEDERAL COURT OF APPEAL

NAMES OF COUNSEL AND SOLICITORS OF RECORD

DOCKET: A-257-14

STYLE OF CAUSE: KINGLON INVESTMENTS INC.
v. HER MAJESTY THE QUEEN

PLACE OF HEARING: TORONTO, ONTARIO

DATE OF HEARING: APRIL 27, 2015

REASONS FOR JUDGMENT BY: WEBB J.A.

CONCURRED IN BY: GAUTHIER J.A.
RENNIE J.A.

DATED: MAY 22, 2015

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