Docket: 2008-1500(IT)I

BETWEEN:

DAVID J. DUNLOP,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on February 25, 2009, at London, Ontario.

Before: The Honourable Justice Patrick Boyle

Appearances:

Counsel for the Appellant:	James W. Dunlop
Counsel for the Respondent:	Tanis Halpape

JUDGMENT

The appeal from the reassessment made under the *Income Tax Act* with respect to the Appellant's 2006 taxation year is allowed, without costs, and the penalties assessed are vacated. The reassessment is referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with the reasons herein.

It is further ordered that the filing fee in the amount of $100 be reimbursed to the Appellant.

Signed at Ottawa, Canada, this 27th day of March 2009.

"Patrick Boyle"

Boyle J.

Citation: 2009 TCC 177
Date: 20090327
Docket: 2008-1500(IT)I

BETWEEN:

DAVID J. DUNLOP,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

(Delivered orally from the Bench on February 26, 2009, in London, Ontario and modified for clarity and accuracy.)

Boyle J.

[1] The only issue in this case involves a section 163 penalty for a repeated failure to report employment income.

I. Applicable law

[2] Subsection 163(1) provides that a person who has failed to report an amount required to be included in income and who had failed to report such an amount in any of the three preceding years, is liable to a penalty of 10% of the current year's unreported amount.

[3] Subsection 163(3) provides that the onus is on the Minister to substantiate the penalty. In this case, the unreported income for the year and for the preceding year is admitted to the extent described below.

[4] While the subsection 163(1) penalty is drafted as an automatic or strict liability penalty, the taxpayer will not be penalized if he can demonstrate he exercised a requisite degree of due diligence. See Justice Wood's decision in *Saunders v. Her Majesty The Queen*, 2006 DTC 2267.

[5] The subsection 163(1) penalty is 10% of the unreported amount. This is so even with respect to employment income where tax has been withheld. This can lead to harsh results where the penalty greatly exceeds the tax payable on the unreported income. For taxpayers in Ontario, like Mr. Dunlop, CRA also assesses Ontario's corresponding 10% provincial penalty. While the results may be harsh, the federal and provincial parliaments can and have enacted a penalty régime in a manner that does not distinguish between T4 employment income and other income. In the words of Justice Woods in *Saunders*:

> . . . Parliament has enacted subsection 163(1) to ensure the integrity of Canada's self-reporting system.

Justice Woods goes on:

> In my view, a Court should not lightly vacate the penalty provided for in the legislation.

II. Facts

[6] In 2005 and 2006, David Dunlop was a university student. He held part-time jobs. When he graduated in 2006, he started full-time employment. He attended university in a different city than his parents' home. His full-time employment was in yet another city. In addition to the taxpayer having a different temporary address while at school than his parents' permanent address, his parents moved homes in 2007 before the missing 2006 T4 was received.

[7] In 2005, David Dunlop did not report his part-time employment income from Bulk Barn. Apparently, he had not received his copy of the T4. CRA had received its copy and the taxpayer was assessed or reassessed on the additional T4 income and tax was paid in the ordinary course.

[8] In 2006, David Dunlop again did not receive his copy of the T4 slip from Bulk Barn. Before the end of April, he went into his Bulk Barn location to seek a copy. His employer is a franchised store. Its owner lived in another city. He had still not received his copy of the T4 by April 30.

[9] David's father and counsel in this appeal, James Dunlop, prepared David's 2006 tax return at the end of April 2007 for David's signature. In preparing the return, David estimated for his father the amount of his employment income from

Bulk Barn to be about $5,250. The written estimation of this amount from April 2007 was put into evidence.

[10] In completing the return as signed and filed, the Bulk Barn employment and missing T4 was disclosed as follows above "Line 101 – Employment income": "T4 missing from Bulk Barn – will amend when received."

[11] The return included David's other T4 and T3 amounts. There was tax owing which was paid.

[12] CRA's Notice of Assessment was dated May 2007. That initial assessment assessed David's tax liability as filed, that is not accounting for any Bulk Barn income. CRA reassessed the taxpayer on October 4, 2007 and included $6,463 of additional Bulk Barn income as shown on the T4 filed by Bulk Barn with CRA. Additional tax payable was assessed thereon in the amount of approximately $750. Of that, $554 of tax had already been withheld and remitted to CRA by Bulk Barn. In addition, the reassessment assessed the 10% federal penalty of $646 and a similar provincial penalty.

[13] Either the day before or the day after this reassessment was received in October 2007, David Dunlop's copy of the Bulk Barn 2006 T4 arrived in the mail. The T4 shows employment income of $6,464 and employee deductions totalling $938. This means David's take home was $5,526. David's estimate of $5,250 was within 5 % of that actual amount.

III. Analysis

[14] The question to be decided in this case is whether the taxpayer's disclosure of the missing T4 in his return showed he was duly diligent in attempting to ensure that the amount of his Bulk Barn income did not go unreported by him to CRA.

[15] Both parties in this case were well represented by able and thoroughly prepared counsel. I was referred to several cases where similar penalties were upheld in circumstances where there was no disclosure whatsoever in the return of the amounts reflected in missing information slips. That was the case in *Saunders*, as well as in *Paul v. Her Majesty The Queen*, 2008 DTC 3060. The taxpayers were unsuccessful in both of those cases.

[16] That was also the case in Justice Wood's decision earlier this month In *Raboud v. Her Majesty The Queen*, [2009] T.C.J. No. 71. In *Raboud*, Justice Woods vacated

the penalty in circumstances where the amounts on the missing information slips were not reported in the return, but were mailed in by the taxpayer the following month when they were received, seemingly without a cover letter or a T1 Adjustment Request form.

[17] Both counsel tell me they have been unable to find a decision considering whether or when some disclosure in the return of a missing information slip will constitute due diligence to avoid the amount of income going unreported. This is perhaps surprising, but the result is that neither side can be faulted for pursuing this case as a reasonably important principle to have considered by the Court.

[18] It is the Crown's position that the disclosure made in the return does not rise to the threshold of due diligence. The Crown points out that the language of subsection 163(1) imposes the penalty if the taxpayer fails to report an amount of income. This means disclosure of additional employment income for which a T4 should have been issued without including an estimate of the amount in the return is insufficient. According to the Crown, due diligence required the estimated amount to be included in the return.

[19] The Crown's further position is that the due diligence defence cannot be made out when the taxpayer did not give his employer his new address, especially since it was the same problem that appears to have caused the prior year's Bulk Barn T4 not to have been received.

[20] A helpful consideration to bear in mind in this analysis is the purpose of subsection 163(1), and whether the taxpayer's attempts to obtain his T4 and his disclosure in the return were likely to help satisfy or frustrate that purpose. As set out in *Saunders* above, the purpose of this penalty is to ensure the integrity of Canada's self-reporting system.

[21] Another helpful consideration in deciding what is sufficient diligence to be due diligence warranting the cancellation of the penalty, is what the tax authorities advise Canadian taxpayers to do in such circumstances. After all, late and lost information slips are not at all an uncommon occurrence. It is presumably for exactly these reasons that each year the topic warrants its own sections in CRA's Tax Guide.

[22] The 2006 Tax Guide was not put into evidence by either party in this appeal under the Court's informal procedures. It is readily available online at the CRA's official website. I did advise the parties in the course of the proceeding that I had consulted prior years' CRA tax guides and tabled my particular concerns with them.

[23] There are three parts of the 2006 Tax Guide that touched on this. Under the heading "Line 101 – Employment income" is written:

> Enter the total of amounts shown in box 14 of all your T4 slips. If you have not received your slip by early April, or if you have any questions about an amount on a slip, contact your employer. For more information see 'What if you are missing information?'

Under the later heading "What if you are missing information?", it is written:

> If you have to file a return for 2006, as explained on page 7, make sure you file it **on time** (see page 7) even if some slips or receipts are missing. If you know that you will not be able to get a slip by the due date, attach to your paper return a note stating the payer's name and address, the type of income involved, and what you are doing to get the slip. To calculate the income to report, and any related deductions and credits you can claim, use any stubs you may have, and attach them to your paper return. If you are filing electronically, keep all of your documents in case we ask to see them.

Thirdly, under the heading "How do you change a return?", it is written:

> If you need to make a change to any return you have sent us, **do not file another return for that year**. You should wait until you receive your *Notice of Assessment* before requesting any change to a return that has not been processed.

[24] Notably, for 2006, CRA was not advising taxpayers to put in a rough estimate of the employment income earned for which one had not yet received a T4 slip. It was instructing to only insert an amount if one had pay stubs that could be used to make the calculation and to include copies of those pay stubs. It does not say to make a best estimate in any other case.

[25] CRA recommended attaching a note to the paper return that identified the payer and the type of income and what is being done to get the missing slip.

[26] In this case, David Dunlop's notation in the return clearly identified additional employment income was paid to him by Bulk Barn. While he did not say what he was doing to get the missing slip, his notation in the return said he will amend the return when the missing T4 is received.

[27] By and large, David Dunlop clearly signed and filed a return that did what the CRA Tax Guide told him to do in the circumstances. While this alone does not mean

that as a matter of law he exercised sufficient due diligence to absolve him from liability for a subsection 163(1) penalty, he did exercise the diligence CRA said they expected him to in just the circumstances he found himself in.

[28] In these circumstances, I am satisfied that the taxpayer exercised sufficient diligence to ensure his Bulk Barn income did not go unreported. He disclosed the source and the nature of the income in his return. He undertook to amend his return when the T4 was received. He tried to contact his employer at the place of employment. It was reasonable in the circumstances for the Dunlops to assume it was only David's copy of the T4 that had gone astray and that CRA would have received its copy electronically or otherwise, and that CRA would thus know exactly the amounts involved.

[29] The approach taken by the taxpayer could not reasonably be considered to have been an attempt to frustrate or defeat the integrity of the self-reporting system. He was self-reporting to the extent he could and largely as advised by the CRA Tax Guide in the circumstances.

[30] A case such as this is materially different than those cases I was referred to where no disclosure whatsoever was made in the tax return. This also appears to be a stronger case for the taxpayer than in *Raboud*, where no disclosure was made in the return, but the taxpayer sent the information slips in when he received them and before the return was assessed.

[31] In these particular circumstances, I am allowing the taxpayer's appeal and vacating the penalty assessed. This does not mean that any mere disclosure of a source of income in a return will be sufficient to avoid a penalty for not reporting.

[32] Given this disposition of the appeal, while this Court does not have any jurisdiction over the Ontario penalty, it is administered by CRA on behalf of Ontario, and I am recommending that CRA consider reversing that penalty as well.

Signed at Ottawa, Canada, this 27th day of March 2009.

"Patrick Boyle"

Boyle J.

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COURT FILE NO.:	2008-1500(IT)I
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PLACE OF HEARING:	London, Ontario
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APPEARANCES:

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Counsel for the Respondent:	Tanis Halpape

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