Docket: 2020-582(IT)I

BETWEEN:

JEFFREY C. CHAN,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on March 31, 2022, at Toronto, Ontario

Before: The Honourable Justice B. Russell

Appearances:

Counsel for the Appellant:	Jesse Waslowski
Counsel for the Respondent:	Christopher Ware

JUDGMENT

The appeal is allowed and the three appealed April 2, 2019 reassessments are referred back to the Minister for reconsideration and reassessment on the basis that the Appellant is not liable for penalties pursuant to paragraphs 162(7)(a) and 162(10)(a) of the federal *Income Tax Act* for any of his 2013, 2014 and 2015 taxation years. In this informal procedure appeal the Appellant is awarded fixed costs of $3,000.

Signed at Halifax, Nova Scotia, this 29th day of July 2022.

"B. Russell"

Russell J.

Citation: 2022 TCC 87
Date: July 29, 2022
Docket: 2020-582(IT)I

BETWEEN:

JEFFREY C. CHAN,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Russell J.

Overview and Issue:

[1] The appellant Jeffrey C. Chan has appealed three reassessments raised April 2, 2019 by the Minister of National Revenue (Minister) regarding respectively the appellant's 2013, 2014 and 2015 taxation years. The Minister confirmed these reassessments November 29, 2019; hence this appeal.

[2] Specifically the appellant challenges the two penalties imposed by each of the appealed reassessments - a penalty per paragraph 162(7)(a) of the federal *Income Tax Act* (Act) for failure to file per subsection 233.3(3) of the Act a form T1135 (Foreign Income Verification Statement); and as well a penalty per paragraph 162(10)(a) of the Act on the basis that the said failure to file was made knowingly or under circumstances amounting to gross negligence.

[3] The appellant submits he was wrongly reassessed as he was not the beneficial owner of the relevant foreign asset, being the assets held in a Bank of China account opened in his name May 2011, funded by his father, Joseph Chan (Joseph). Joseph passed away February 7, 2018.

[4] The respondent's position is that during the taxation years in issue the appellant was the owner of the subject Bank of China account and therefore he had the legal obligation of filing form T1135s respecting the account.

[5] Apparently the Minister reassessed the Estate of the late Joseph Chan as well for these same penalties in respect of the subject bank account - presumably on the basis that if the appellant were not responsible for filing form T1135s during the relevant period, then Joseph had had that legal responsibility.

Legislation:

[6] Paragraph 233.3(3)(b) of the Act provides:

> Returns respecting foreign property [T1135] – (3) A reporting entity for a taxation year or fiscal period shall file with the Minister for the year or period a return in prescribed form on or before the day that is – (b) where the entity is not a partnership, the entity's filing-due date for the year.

[7] Paragraph 162(7)(a) of the Act provides in relevant part:

> Failure to comply – Every person…who fails – (a) to file an information return as in when required by this act or the regulations… is liable in respect of each such failure…to a penalty…

[8] Paragraph 162(10)(a) of the Act provides in relevant part:

> Failure to furnish foreign-based information – Every person or partnership who, (a) knowingly or under circumstances amounting to gross negligence, fails to file an information return as and when required by any of sections to 233.1 to 233.4…is liable to a penalty…

Evidence:

[9] Two witnesses testified - the appellant and also Canada Revenue Agency (CRA) auditor C. Oliver.

[10] In summary the appellant's evidence was that he holds a graduate degree in accounting. During the 2013-2015 period he was employed as a financial analyst and now is employed as a treasury manager. He speaks English and basic Chinese. In 2011 when he was 24, his father Joseph, who as well was an accountant, required his son to accompany him in travelling to a destination in China, at Joseph's expense, whereat Joseph caused the opening of Bank of China (BofC) account #…0322 (Ex. R-1).

[11] The appellant testified that his father Joseph's intention was to open this BofC account jointly with his son. But the BofC would not do that, advising the account

could be in one person's name only. Nor would the BofC permit a power of attorney over the account. Joseph decided the BofC account should be opened in the name of his son, the appellant. That is what was done. The BofC account was entirely funded by Joseph.

[12] By 2014, the BofC would permit a power of attorney to be given to Joseph. In that year the appellant signed a power of attorney over the account in favour of his father, Joseph. This apparently allowed Joseph online access.

[13] Joseph had told his son the appellant that through the BofC account he wanted to have Chinese currency and a presence in China, to aid in seeking redress of an injustice regarding his own father (the appellant's grandfather). The grandfather had been militarily executed following the end of the Chinese civil war in the late 1940s. The appellant testified that Joseph was reluctant to discuss personal matters such as this, even with family including the appellant himself and Joseph Chan's wife. The appellant testified that applying to redress injustice in this regard was a "very, very unstructured" process; far from being simply the submission of an application form.

[14] Ultimately it was unclear how the existence of the BofC account aided Joseph's efforts in this regard. The appellant made general reference to the BofC account establishing a China presence that Joseph, not living in China, did not otherwise have.

[15] The appellant never carried out any transactions involving the BofC account except under his father Joseph's direction. As well, it was Joseph who kept the bank card and associated PIN with which the account could be accessed. The appellant testified also that his father used the power of attorney in travelling to China and using an ATM within that country to carry out account transactions. The appellant said that as far as he was concerned it was his father Joseph's account.

[16] Also, on occasion Joseph would request his son to assist him in carrying out desired transactions electronically involving the BofC account, as Joseph was not "tech-savvy". The BofC account statements were kept by Joseph, not the appellant. The account also was used by Joseph as an investment account. The appellant kept none of his own investments in that BofC account; plus he typically invested in 100% equities and on a more high-risk basis, as opposed to the less risky investing his father engaged in using the subject BofC account.

[17] The appellant's view is that with his father's 2018 passing, intestate, the subject BofC bank account belongs to his mother. By about that time the account held, in Chinese currency, more than $Cdn 2 million.

[18] In cross-examination the appellant acknowledged the CRA conclusion that his father Joseph Chan had had unreported income from between 2007 and 2016, apparently through Joseph Chan's operation of his accounting practice, preparing false tax returns through use of false T1s and T4s. The appellant said he had had no knowledge of this. He had helped his father prepare 100 - 200 tax returns a year but he explained that his assistance was only to the extent of providing electronic data entry assistance in the evenings, again because his father was not "tech savvy". The appellant had his own day job to focus on.

[19] The appellant agreed that on paper he was the sole owner of the Bank of China account. The power of attorney for Joseph Chan that the appellant signed in 2014, giving his father on-line access to the account. But the appellant as well assisted Joseph Chan with on-line transactions again due to the latter not being "tech—savvy".

[20] For the years 2016 though 2019 the appellant did file form T1135s, although apparently specifying he was a nominee for his father and, with his father's passing in 2018, his father's estate. This apparently was prompted by commencement in 2016 of the CRA audit of Joseph.

[21] That audit was conducted by the second witness – also called by the appellant - CRA income tax offshore compliance auditor C. Oliver. The Joseph Chan audit in due course was extended to include an audit of the appellant.

[22] In summary Mr. Oliver's evidence was that Joseph in the conduct of his accounting practice in Canada had accumulated funds deposited into the subject BofC account through receipt of unreported investment income, unreported rental income, and unreported income through preparation of valid and invalid T1 returns.

[23] Mr. Oliver said Joseph Chan was filing returns for individuals who were non-residents of Canada. He was generating significant refunds. Mr. Oliver testified that there was a working income tax benefit such that if one had T4 income of $7,000 - $10,000 a tax refund would be generated. As well, there were other improper income sources. This allowed for accumulation of about $ 2 million (Cdn) of unreported income that CRA assessed during the relevant period.

[24] The appellant testified that he was unaware of these improper actions of his father in the conduct of the latter's accounting practice, until the CRA audit had uncovered same and his father had admitted these improper actions.

[25] In the course of the Joseph Chan audit Mr. Oliver received a letter from Joseph's lawyer dated August 23, 2017. (Joseph and the appellant were separately represented.) The letter responded to CRA's audit requirement letter per section 231.1 of the Act seeking certain information regarding Joseph.

[26] One of CRA's questions was whether during the 2005 to 2015 period did Joseph have bank, investment or trading accounts registered in the name of other persons, that he controlled or had access to.

[27] The lawyer's response on behalf of client Joseph (who passed away approximately six months later) provided information regarding the subject BofC account. That account was one of three accounts identified in the lawyer's letter. The letter states that Joseph Chan "has control of and access to, Bank of China accounts - #…0322 and #…5614".

[28] The response further read:

> [w]hile these accounts were opened in the name of his son, Jeffrey Chan, [Joseph Chan] is the sole beneficial owner of the accounts. The funds deposited into the accounts all emanate from [Joseph Chan]. All actions taken by Jeffrey Chan in relation to the accounts were at the direction of [Joseph Chan]. [Joseph Chan] opened the accounts in the name of his son in order that any amounts in the accounts on [Joseph Chan's] death would then pass to his son. The source of funds included [Joseph Chan's] unreported income, the derivation of which is set out in more detail in…this letter.

[29] Mr. Oliver testified that he determined that the account and the funds in it belonged to the appellant, "because the account was opened up in his name".

[30] Mr. Oliver also testified that CRA had learned of the existence of the subject BofC account from the appellant, who through his counsel advised that he was the nominee holder of a BofC account holding approximately $2 million, and provided bank statements for it. Mr. Oliver said that the appellant had said that the account was opened at the direction of his father and that it was not his. Mr. Oliver testified also that the appellant had said that the account could not be in his father's name due to the execution of his grandfather by the Chinese government.

Submissions:

[31] In argument appellant's counsel submitted that two key facts had been established – that the appellant was not the beneficial owner of the subject bank account and that the appellant reasonably believed he was not the owner of that account. Establishment of either asserted fact would be sufficient to allow the appeal. Alternatively, gross negligence in believing his father owned the account has not been established.

[32] Also, appellant's counsel submitted that the appealed reassessments for the 2013 and 2014 taxation years were statute-barred. He acknowledged that that issue had not been pleaded in his client's Notice of Appeal. He submitted, however, that the respondent's pleading in its Reply of the relevant initial assessment dates, in the course of setting out the assessment history of the three taxation years, enabled the appellant to raise the statute-barred issue. (Neither party pleaded subsection 152(4) of the Act, which permits the respondent to reassess outside the normal reassessment period.) It seems that that issue was first identified the evening prior to the hearing, when the appellant's book of authorities was provided to respondent's counsel.

[33] The appellant asserts that the appellant did not beneficially own the account in light of his father's express intent that the appellant be his nominee. Also, if there is insufficient evidence to establish the late father's intent, also there is no evidence to rebut the presumption of resulting trust. The appellant laid out what this required - a transfer of title and establishment of the three certainties of a trust; being object, subject and intent; all of which, he argues, were established here.

[34] The appellant relies also on the statement of Rothstein, J. in *Pecore v. Pecore*, [2007] 1 SCR 795 at paragraph 27 that, "[t]he presumption of resulting trust is a rebuttable presumption of law and general rule that applies to gratuitous transfers." Also noted at paragraph 44 of that decision is that the presumptions of resulting trust and advancement can be rebutted on the civil standard of a balance of probabilities.

[35] The appellant argued also that the appeal could be allowed in the basis that the appellant had reasonable grounds to believe that he was not the owner of the account. This would apply not only to rebutting the gross negligence penalty but also the administrative penalty of subsection 162(7). The appellant says that the administrative penalty is subject to a due diligence defence. The defence of due diligence was addressed in *Corporation de L'École Polytechnique v Her Majesty*, 2004 FCA 127, at paragraph 28:

> The due diligence defence allows a person to avoid the imposition of a penalty if he or she presents evidence that he or she was not negligent. It involves considering whether the person believed on reasonable grounds in a non-existent state of facts which, if it had existed, would have made his or her act or omission innocent.

[36] Finally, regarding gross negligence penalties, the appellant cites *Van Der Steen v. Her Majesty*, 2019 TCC 23, wherein my colleague Justice Sommerfeldt cited *Farm Business Consultants Inc*., [1994] 2 CTC 2450 at 2457:

> A court must be extremely cautious in sanctioning the imposition of penalties under subsection 163(2) of [the ITA]… [T]he routine imposition of penalties by the Minister is to be discouraged… [A] court must… scrutinize the evidence with great care and look for a higher degree of probability than would be expected where allegations of a less serious nature are sought to be established. Moreover, where a penalty is imposed under subsection 163(2)…, if a taxpayer's conduct is consistent with two viable and reasonable hypotheses, one justifying the penalty and one not, the benefit of the doubt must be given to the taxpayer and the penalty must be deleted.

[37] Turning to the respondent Crown, its initial submission is that the proposed statute-barred issue was not pleaded and so should not be considered, noting as well that the appellant is represented by experienced counsel.

[38] Further, the respondent cites *Cassan v. The Queen*, 2017 TCC 174, in asserting that the presumption of resulting trust does not apply in Tax Court proceedings where the Minister has pleaded assumptions of fact assumed to be true (although rebuttable on the basis of a balance of probabilities). Thus, in this case the presumption of resulting trust does not apply to shift the burden of proof to the respondent.

[39] As well, the respondent submits that the appellant was the beneficial owner of the subject BofC account and insufficient evidence has been presented to prove that his father was the owner. In cross-examination the appellant agreed that on paper he was the sole owner of the subject account. Also, the appellant has not provided a plausible explanation for why Joseph Chan was beneficial owner of the subject account.

Analysis:

[40] In my view the appellant did not have beneficial title to the subject BofC account during the subject 2013 – 2015 period, notwithstanding that the account was

in his name. I reference in particular Joseph Chan's clear statement in 2017 through his lawyer that he had retained beneficial ownership of the funds in the account for his lifetime, which included the three taxation years in issue.

[41] That 2017 statement that Joseph considered that he was the beneficial owner of the account is borne out by his conduct and that of the appellant during the relevant period. The funds in the count were wholly sourced by Joseph, both at the time in 2011 in opening the account and thereafter. The funds were illegally gained by Joseph in the conduct of his accounting practice but that does not change that he not the appellant sourced the funding of the account.

[42] As well, it was only Joseph, not at all the appellant, who actively used the account during the relevant three year period. Joseph engaged in transactions utilizing the funds and adding to the funds, throughout that period. The appellant on the other hand did not deal at all with the account or funds therein, other than to electronically assist his less "tech-savvy" father from time to time, at the latter's request. The appellant considered the funds in the account as belonging to his father.

[43] The fact that some or most of the funds paid into the account were ill-gotten gains of Joseph does not go to the nature of Joseph's interest in the account during the relevant three year period.

[44] As well Joseph's intent, as stated in 2017 via his lawyer, was that the account go to the appellant upon Joseph's passing. This was based on Joseph's direction in 2011 that the account be opened in the appellant's name. This is entirely consistent with the conclusion that in the meantime, including the three taxation years in issue, prior to his death in early 2018, he not the appellant held beneficial ownership of the BofC account.

[45] Thus as Joseph sourced the funding of the account at all times and he alone exercised control and usage of the account, it appears reasonably clear that he alone utilized and thus enjoyed the benefit of the account. Thus I conclude that Joseph was the beneficial owner of the account, while his son the appellant merely held legal title, as his father's nominee. Accordingly, Joseph rather than the appellant had the obligation, as beneficial owner of the BofC account assets, to file the required form T1135s for the three years in issue.

[46] In reaching this conclusion I do not ascribe any relevance to the matter of seeking retribution for the grandfather's military execution in China. The evidence in that regard was too tentative and imprecise to draw any conclusions therefrom.

Seeking retribution was Joseph's project, and the appellant knew little about it until review of his father's papers subsequent to his father's passing in 2018.

[47] It is clear I do not accept the respondent's position that the appellant being the named holder of the account was accordingly the beneficial owner of same. Apart from everything else said, the appellant's testimony was that in 2011 his father essentially had to encourage if not urge his son the appellant to accept having the BofC account opened in his name. There was no evidence suggesting otherwise. He was his father's nominee.

[48] Thus it follows that the appellant would not be liable for either of the penalties he has appealed for each of the 2013, 2014 and 2015 taxation years.

[49] Should I be wrong in concluding that Joseph rather than the appellant held the beneficial interest in the BofC account assets during the three pertinent taxation years, then I consider that for the same reasons as given above the appellant had reasonable cause to believe that his father, and not he himself, held the beneficial interest in the account assets.

[50] Having reasonable cause to so believe should suffice to absolve the appellant of liability for the three gross negligence penalties per paragraph 162(10)(a). Holding such reasonable belief would be incompatible with conduct or intention indicative of gross negligence. Likewise there should not be liability for the three paragraph 162(7)(a) failure to file penalties, as the defence of due diligence has been established – that is, the appellant reasonably believed in a mistaken set of facts that if true would have made his act or omission to act innocent.

Conclusion:

[51] The appellant's appeal is allowed and the appealed reassessments are referred back to the Minister for reconsideration and reassessment on the basis that the appellant is not liable for penalties pursuant to paragraphs 162(7)(a) and 162(10)(a) of the Act for his 2013, 2014 and 2015 taxation years. In this informal procedure appeal the appellant is awarded fixed costs of $3,000.

Signed at Halifax, Nova Scotia, this 29th day of July 2022.

"B. Russell"

Russell J.

CITATION:	2022 TCC 87
COURT FILE NO.:	2020-582(IT)I
STYLE OF CAUSE:	JEFFREY C. CHAN AND HER MAJESTY THE QUEEN
PLACE OF HEARING:	Toronto, Ontario
DATE OF HEARING:	March 31, 2022
REASONS FOR JUDGMENT BY:	The Honourable Justice B. Russell
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APPEARANCES:

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