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INCOME TAX APPEALS

This issue of the Legal Business Report provides current information to the clients of Alpert Law Firm on the rules governing income tax appeals and administrative changes regarding notices of objection and reassessment periods.

Alpert Law Firm is experienced in providing legal services to its clients in tax dispute resolution and tax litigation, tax and estate planning matters, corporate-commercial transactions and estate administration. Howard Alpert has been certified by the Law Society as a Specialist in Estates and Trusts Law, and also as a Specialist in Corporate and Commercial Law.

A. REASSESSMENT PERIOD

Where a taxpayer is a corporation which is not a Canadian-controlled private corporation at the time of original assessment, the period for issuance of a Notice of Reassessment is four years from the original assessment pursuant to subsection 152(3.1) of the Income Tax Act (the "Act"). For individual taxpayers and Canadian-controlled private corporations, the reassessment period is three years. Where a taxpayer is an individual or a graduated rate estate, the Minister of National Revenue has discretion under subsection 152(4.2) of the Act to make a reassessment or redetermination beyond the three-year reassessment period at the request of such taxpayer in order to reduce the taxpayer's taxes payable or grant a refund to the taxpayer. The taxpayer's request must be made within 10 years after the taxation year in issue.

For example, the Minister would have the discretion to reassess a return after the three-year reassessment period where (i) a qualifying taxpayer who previously filed a return discovers that a deduction or non-refundable tax credit was inadvertently not claimed; (ii) refundable tax credits such as goods and services tax credits, provincial tax credits, or child tax credits were not claimed; or (iii) there has been an overpayment of taxes by a qualifying taxpayer due to payroll deductions by an employer. In addition, the Minister is able to issue a reassessment or a redetermination beyond the normal reassessment period applicable to a taxation year where such reassessment or redetermination flows as a consequence of an assessment or an appeal in respect of a previous taxation year.

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Subsection 152(4) of the Act provides that the Minister may assess or reassess the taxpayer at any time (that is, without regard to the normal reassessment period) if the taxpayer or the person filing the return has made any misrepresentation that is attributable to neglect, carelessness or willful default, or has committed any fraud in filing the return or in supplying any information under the Act.

B. CASE LAW

1. ***Seto et al. v. The Queen*, 2007 DTC 1647**

In this Tax Court of Canada case, the Court held that the Minister properly assessed the taxpayer beyond the normal reassessment period. The taxpayer's lack of record keeping, as required under the Act, indicated that he and his company acted with neglect or carelessness which resulted in income not being reported. Although there were no intentional actions taken to mislead or to portray a picture different from what existed, the taxpayer did not exercise reasonable care in the completion of his returns, pursuant to the provisions in paragraph 152(4)(a) of the Act.

The Tax Court disallowed the imposition of penalties pursuant to subsection 163(2) of the Act, even though the net worth assessment showed that the taxpayer underreported his income. The Court held that in addition to the difference resulting from the net worth assessment, the Minister must show that the penalties are justified by pointing to specific evidence or circumstances that amounted to gross negligence. While the negligence sufficient to trigger paragraph 152(4)(a) of the Act is a failure to use reasonable care, subsection 163(2) of the Act requires more: it requires gross negligence. In addition, the Court held that the difference between the net worth assessment and the net amount actually reported on the returns was not substantial.

2. ***Peek v. The Queen*, 2007 DTC 602**

In this Tax Court of Canada case, the taxpayer operated a cheque-kiting scheme from 1994 and 2000, during which he unlawfully obtained $602,000 from HSBC Canada. During the same period, the taxpayer operated an insurance scheme where he purchased numerous life insurance policies in his name and in the names of family members to obtain sales commissions that would exceed the premiums paid. The Minister reassessed the taxpayer beyond the normal reassessment period pursuant to subsection 152(4) of the Act, adding the unreported amounts from both unlawful schemes to his income. The taxpayer appealed the reassessment to the Tax Court of Canada.

The Court dismissed the taxpayer's appeal. Money obtained by fraud may be income in the hands of the wrongdoer. The money obtained by the taxpayer from the two schemes was characterized as income based on the taxpayer's extensive knowledge and experience in banking, the frequency of the transactions, the large amounts of the kited cheques and the lengthy duration of schemes. The taxpayer made a misrepresentation attributable to neglect or carelessness by failing to report any profit from his operations. Therefore, the Minister was justified in reassessing beyond the normal period in these circumstances pursuant to subsection 152(4) of the Act.

3. *Gallery v. The Queen*, 2009 DTC 1026

In this Tax Court of Canada case, the taxpayer was reassessed more than three years after the initial assessment and penalties were imposed pursuant to s.163(2) of the Act. The taxpayer had failed to include $400,000 payable to him pursuant to an employment contract. The taxpayer argued that: (i) the assessment was statute barred; and (ii) there was no basis for the Minister to apply penalties.

The taxpayer owned a numbered company S1, which sold its business and assets to another business, S2 that was controlled by K Co. S1 was then amalgamated with G Co. The taxpayer also entered into an employment contract with S2 whereby S2 agreed to pay the taxpayer $200,000 a year, and a onetime lump sum payment of $400,000. K Co. made a wire transfer of the $400,000 with instructions to deposit the money into G Co.'s account; however the money was deposited into the taxpayer's account. The taxpayer transferred the money to G Co.'s account, thinking it was related to the purchase of S1. S2 was able to deduct the $400,000 payment, but no T-4 was issued to the taxpayer for this amount. The taxpayer did not include the $400,000 lump sum payment in his 1996 tax return. More than 3 years after the initial assessment, the CRA reassessed the taxpayer in respect of the lump sum payment on the basis that it was employment income.

The taxpayer appealed the reassessment to the Tax Court of Canada. The taxpayer stated that accounting was not his strength and relied upon his accountants, P and J, to prepare his tax returns. P told the taxpayer that he was going to inquire into the $400,000 payment and made some preliminary notes indicating he believed the money was taxable in the taxpayer's hands, but transferred the file to J when he retired without further inquiry or without telling the taxpayer anything. J indicated he would look into the $400,000 payment but did not see P's notes. J concluded that the $400,000 payment was not taxable in the hands of G Co. but did not add the amount to the taxpayer's return because the taxpayer told J the money did not belong to him. Both accountants also provided evidence that the taxpayer was conservative and scrupulous.

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The Tax Court of Canada allowed the taxpayer's appeal in part. The Tax Court held that the Minister was entitled to reassess the taxpayer after the normal assessment period because the taxpayer had not exercised reasonable care in omitting to include the lump sum payment in income. The Court stated that a single payment of $400,000 was a large sum and one would expect a person to look into the matter until a satisfactory answer was found. The Court found that the taxpayer would have been quite able to determine the nature of the payment because: (i) the contract outlining the payment was quite clear and concise; (ii) the taxpayer could have asked the president of K Co., who was a friend, about the payment; and (iii) the taxpayer could have made further inquiries with his accountants.

The Court however held that the imposition of penalties was not justified under the circumstances as the taxpayer's conduct did not amount to gross negligence and referred the matter back to the Minister for reconsideration and reassessment.

4. *D'Andrea v. The Queen*, 2011 DTC 1234

In this Tax Court of Canada case, the taxpayer was appointed as a business manager of a corporation ("Group") that had 27 shareholders. Group purchased a property for $1,200,000 on December 7, 1989 ("Property"). In 1998, the Property was rezoned to allow a casino development. A new corporation ("Newco") was incorporated by 1075111 Ontario Inc, which was a company wholly owned by the taxpayer, and the Chippewas of the Thames Land Claim Trust ("Chippewas"), each owning 50% of the shares. Although the taxpayer knew that the property purchased by Group was worth not less than $3,755,000, the taxpayer caused the property to be transferred to Newco for $1,810,050 ("Purchase Price") on March 31, 1999. The taxpayer also made false representations to the shareholders of Group that he had no connection with Newco.

On July 11, 2002, the taxpayer was found guilty of fraud on the shareholders of Group by knowingly selling the Property for less than half of its value. On March 13, 2006, the Minister reassessed the taxpayer on the basis that the fair market value of the Property at the time of the sale on March 31, 1999 was no less than $3,755,000. Consequently, the Minister included the amount of $1,877,000 in the taxpayer's income pursuant to subsection 56(2) of the Act. The reassessment was also issued beyond the normal limitation period under subsection 152(4) of the Act and penalties were assessed under subsection 163(2) of the Act.

The Tax Court of Canada found that the Minister would be correct to include $1,877,000 in the taxpayer's income pursuant to subsection 56(2) of the Act, if the

Minister was able to satisfy the onus which is required to issue a reassessment beyond the normal limitation period pursuant to subsection 152(4) of the Act. The four preconditions necessary to invoke subsection 56(2) of the Act were met in this appeal as: (i) the transfer of the Property was to a holding company, Newco, which was owned 50% by the Chippewas and 50% by the taxpayer through a numbered company; (ii) the allocation of the Property from the Group to Newco was at the direction of the taxpayer; (iii) the transfer of the Property to Newco was for the benefit of a numbered company, which was wholly owned by the taxpayer; and (iv) if the Property had been transferred directly to the taxpayer and the Chippewas, 50% of the value of the Property would have been included in the taxpayer's income pursuant to subsection 15(1) of the Act.

Despite the fact that the taxpayer: (i) did receive an indirect benefit which should have been included in his income; and (ii) made a misrepresentation in filing his income tax return, the Tax Court of Canada allowed the taxpayer's appeal. The Minister was not entitled to reassess the taxpayer beyond the normal reassessment period because the Minister failed to satisfy the onus of demonstrating that the taxpayer's misrepresentation was attributable to negligence, carelessness or willful default. At the hearing of this appeal, counsel for the CRA: (i) did not ask questions about the taxpayer's failure to include the reassessed amount in his 1999 income tax return; (ii) elicited no evidence surrounding the taxpayer's filing of his 1999 tax return; and (iii) made no submissions with respect to subsection 152(4) of the Act. The Minister's reassessment beyond the normal limitation period pursuant to subsection 152(4) of the Act was ordered to be vacated.

Furthermore, a fraud conviction does not automatically fulfill the Minister's burden under subsection 152(4) of the Act. When a taxpayer has been assessed beyond the limitation period, the Minister cannot meet his onus pursuant to subsection 152(4) if its counsel fails to address the issue at the hearing. Since the taxpayer was not given an opportunity to offer an explanation for his actions, it was not clear whether the taxpayer's view of the transaction was so unreasonable that it could not have been honestly held. As such, there was insufficient evidence to meet the Minister's onus under subsection 152(4) of the Act.

5. *Cameron v. The Queen*, 2011 DTC 1166

In this Tax Court of Canada case, the taxpayer had worked in the construction trade for many years and had been purchasing real estate properties repeatedly for the purpose of selling them quickly for profit. On May 7, 2001, the taxpayer purchased a lot for $12,000 and constructed a residence for himself ("Charney Property"). The taxpayer lived at the Charney Property for around a year, rented it out to a third party for around

5 months, and sold the Charney Property on April 10, 2003 for $148,000. On December 3, 2007, based on the taxpayer's history of purchasing and reselling properties at a profit, the Minister reassessed the taxpayer beyond the normal assessment period pursuant to subsection 152(4) of the Act and included a gain of $70,800 as business income earned as a result of the sale of the Charney Property for the taxpayer's 2003 taxation year.

The taxpayer submitted that the assessment was incorrect pursuant to subparagraph 40(2)(b) of the Act because the gain resulted from the disposition of a house that was his principal residence. The Minister acknowledged that the taxpayer used the Charney Property as his residence, but submitted that: (i) the gain still constituted a gain in the nature of trade; and (ii) the taxpayer made a misrepresentation by treating the profit from the disposition of the Charney Property as a capital gain rather than a taxable income gain. The taxpayer further submitted that: (i) it is for the Minister to show that the taxpayer made a misrepresentation that is attributable to neglect, carelessness or willful default in order for the Minister to reopen the 2003 taxation year under subsection 152(4) of the Act; and (ii) since the issue in this case falls in a grey area, he should be given the benefit of the doubt.

The Tax Court of Canada vacated the assessment in favour of the taxpayer. According to ***Regina Shoppers Mall Limited v. The Queen***, 90 DTC 6427, when a taxpayer files an income tax return on what he believes to be the proper method, after thoughtful, deliberate and careful assessment, there can be no misrepresentation that would allow the Minister to assess outside the normal assessment period pursuant to subsection 152(4) of the Act. Additionally, the Act does not impose on taxpayers the duty to report in a manner which the Minister prefers, and if the taxpayer carefully considers his position and does not attempt to deceive the Minister, there is no misrepresentation.

The Tax Court of Canada held that the taxpayer's interpretation of the facts cannot be considered unreasonable. When the taxpayer built the residence on the Charney Property, he could not have anticipated that his mother would gift him a lot with a preferred location next to the river. This seems to be a likely motive for the sale of the Charney Property for personal reasons, as it is entirely reasonable for a majority of taxpayers to be tempted to move in order to take advantage of the benefits of living in a house near the shore of a navigable river.

Since the Minister failed to reassess the taxpayer within the three years from the date of the first notice of assessment, the Minister must accept the consequences of not having proven, on a balance of probabilities that the misrepresentation alleged is due to one of the circumstances that allow a reassessment to be made after the normal assessment period.

6. _*Chaumont v. The Queen*, 2010 DTC 1014_

In this Tax Court of Canada case, the taxpayer, who is a dual citizen of Canada and France, resided permanently in Canada. The Minister reassessed the taxpayer and included interest amounts of $1,260 and $2,200 to his income for 2004 and 2005 respectively. The interest amounts were derived from investments held by the taxpayer in France. The reassessment for 2004 was made beyond the normal reassessment period pursuant to subsection 152(4) of the Act.

The taxpayer claimed that under Article 24 of the Canada-France Tax Convention ("Convention"), income from one signatory of the Convention must be given the same tax treatment as income from other signatories. Since the interest income was not assessed in France, the taxpayer argued that it should not have been assessed in Canada either. The taxpayer further claimed that the Minister is not entitled to make a reassessment for 2004 pursuant to subsection 152(4) of the Act because the Minister failed to meet the onus required to assess beyond the normal assessment period.

The Tax Court of Canada allowed the taxpayer's appeal in part. The Court found that Article 24 of the Convention was inapplicable to the taxpayer's situation but held that the Minister was not entitled to make a reassessment beyond the normal limitation period for 2004 because the Minister failed to prove that the taxpayer misrepresented the facts by willful default, neglect or carelessness upon filing his income tax return. The burden of proof on the part of the Minister is substantially less demanding than the burden required by the Act to justify the imposition of a penalty, but still requires there to be an error, a willful default, a willful blindness, indifference, or even a somewhat reckless lack of care or prudence.

The Court found that the taxpayer, an engineer by training: (i) had no specific knowledge of taxation; (ii) drew on his skills and knowledge to argue the merits of his allegations rather than avoiding or evading his tax obligations; and (iii) obtained information which, in his opinion, validates his interpretation of Article 24 of the Convention. The Court found that the taxpayer's submissions were neither far-fetched nor unreasonable enough for it to be concluded that he made a willful default or mistake with the intent to escape from his Canadian tax obligations. Furthermore, there was no stubbornness or capriciousness on the part of the taxpayer, and the allegations involved a legitimate question and a principled concern that had a modicum of foundation. Despite the amounts in issue being relatively small, the taxpayer still took serious initiatives to assert his position. Thus, the court ordered that the reassessment for the 2004 taxation year be vacated.

7. *MacMillan v. The Queen*, 2008 TCC 56

In this Tax Court of Canada case, the Minister reassessed the taxpayer in 2004 pursuant to the provisions of subsection 152(4) of the Act in respect of his 1998 taxation year, which was statute-barred. The Notice of Reassessment included proceeds from the exercise and disposition of stock options in the taxpayer's income and also assessed the taxpayer for a gross negligence penalty pursuant to section 163(2) of the Act.

The taxpayer was previously employed by a company involved in the communications business and was granted employee stock options. In October 1997 the taxpayer resigned from his position with the company. In November 1997 the taxpayer entered into a written agreement with the company to sell and transfer his interest in the stock options for $140,000. The taxpayer testified that he had not been paid the $140,000 that had been promised when the agreement was signed but admitted that he had received payments of $27,500 and $5,600 in 1998.

In May 1998, the company exercised the taxpayer's stock options resulting in the receipt by the company of proceeds of disposition of approximately $380,000. The taxpayer did not report any income relating to the stock options when he filed his 1998 tax return because he believed that he had previously disposed of all of his interest in the stock options.

The Tax Court of Canada partially allowed the taxpayer's appeal. The Tax Court of Canada held that: (i) pursuant to subsection 152(4) of the Act the Minister was statute-barred from reassessing the taxpayer with respect to the income from the stock options because the taxpayer honestly believed that he had sold his interest in the stock options; (ii) however, the payments of $27,500 and $5,600 that were received by the taxpayer in 1998 can be reassessed and should have been included in the taxpayer's taxable income for the 1998 taxation year because the taxpayer's failure to report these amounts constituted a misrepresentation attributable to neglect, carelessness or wilful default; and (iii) there was no basis for imposing a penalty under subsection 163(2) of the Act, since the taxpayer did not commit "gross negligence" when he failed to include the above-mentioned payments in his 1998 income.

The Tax Court of Canada held that the Minister is required to demonstrate "gross negligence" with respect to the imposition of a penalty under subsection 163(2) of the

Act. This is a higher standard than the "neglect, carelessness or default" that must be demonstrated by the Minister in order to be able to reassess a taxpayer in respect of a statute-barred year pursuant to the provisions of 152(4) of the Act.

8. *Williston v. The Queen*, 2008 FCA 261

This Federal Court of Appeal decision affirmed the decision and reasoning of the Tax Court of Canada in ***Williston v. The Queen,* 2007 DTC 1485**. In the Tax Court of Canada case, the taxpayer appealed her reassessment for several consecutive years. The reassessment for 1998 was beyond the three-year limitation period. In that year, the taxpayer had attempted to deduct the cost of items which were clearly not connected to her telemarketing business, including a sink, unrelated bingo tickets, one meal only from a restaurant, and clothing which was obviously personal. Because these were misrepresentations attributable to neglect or carelessness, the Tax Court had no difficulty in permitting the reassessment for 1998 beyond the normal period.

However, the Tax Court found that the taxpayer did not intentionally act to not comply with the law; she was basically honest but misguided. In deducting rental losses and home office and other expenses, the taxpayer was merely aggressive in her expense claims. Therefore, the penalties for gross negligence were deleted.

The Federal Court of Appeal allowed the taxpayer's appeal in part to give effect to the Minister's consent to judgment to delete the gross negligence penalties.

9. *Boucher v. The Queen*, 2004 FCA 46

In this Federal Court of Appeal case, the Minister reassessed the taxpayer after the reassessment limitation period and imposed penalties. The taxpayer was a lawyer employed as a stockbroker who, during the course of one taxation year, misappropriated funds from the trading accounts of her clients and then failed to disclose this fraudulent income in her tax return.

Several years later, a newspaper article revealed the taxpayer's fraudulent activities, and as a result the Minister reassessed the taxpayer's tax return. The Minister found that the taxpayer understated her income by approximately $200,000 and imposed penalties. The taxpayer appealed the Minister's assessment and penalties on two grounds: (i) the Minister erred in assessing the taxpayer after the limitation period had expired; and (ii) the taxpayer's understatement of income was completely offset by the taxpayer's pre-existing non-capital losses (resulting in no taxes for the taxpayer), therefore no penalties should be imposed.

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The Federal Court of Appeal dismissed the taxpayer's appeal. On the first issue, the Court declared that the limitation period *does not apply* when there is: (i) an assessment or reassessment based upon a misrepresentation by the taxpayer; and (ii) the misrepresentation is attributable to neglect, careless or willful default. The evidence clearly indicated that there was a misrepresentation attributed to the willful default of the taxpayer given that the taxpayer, a lawyer by profession who was well-versed in tax law, not only failed to disclose her fraudulent income in the initial tax return but continually refused to disclose such income in her communications with the Minister. As such, the Minister did not err in assessing the taxpayer beyond the normal reassessment period. Leave to appeal to the Supreme Court of Canada was dismissed.

10. *Lloyd v. The Queen*, [2002] TCJ No 119

In this Tax Court of Canada case, the taxpayer, a professional engineer, was reassessed by the Minister for the taxation years 1989 to 1993, several years after the reassessment limitation period. The Minister found that the taxpayer had failed to report: (i) interest income in regards to the sale of a certain property; and (ii) certain shareholder benefits he obtained. As such, the Minister assessed penalties pursuant to subsection 163(2) of the Act. The taxpayer appealed the reassessment and the penalties imposed.

The taxpayer's appeal was allowed in part. In regards to the unreported interest income, the taxpayer argued that he was not grossly negligent as he was simply unaware there was a clause in the sales agreement that imposed interest on the installments paid by the purchaser of the taxpayer's property. The taxpayer claimed that he did not know that such interest income was even received during the years in question. The Court found the taxpayer's argument highly implausible given that the taxpayer was an educated man familiar with legal and accounting matters. Finding the taxpayer grossly negligent, the Court imposed penalties on the taxpayer for the years in which he received the interest income, except a year in which the taxpayer seemed to have accidentally included the interest income under the wrong heading.

In regards to the undisclosed shareholder benefits, the taxpayer argued that he was not grossly negligent in failing to report such benefits, as the Minister attributed the benefits on him only because certain expenses were disallowed to his company. The Court followed ***Robson et al. v. The Queen*, 2001 DTC 1039** and shunned the departmental mindset, which says when a corporation is disallowed an expense, then a matching tax consequence, such as a shareholder or employee benefit under subsection 15(1) of the Act, must be imposed upon the shareholders of the company as a kind of punishment for allowing their corporation to incur disallowable expenses. As such, the Court disallowed the imposition of penalties against the taxpayer for failing to report such income.

The final issue, being the issue of the Minister's reassessment beyond the limitation period, was also determined by the Court. The Court found that since there was clear evidence that the taxpayer received unreported interest income and the failure to report income was attributable to the taxpayer's neglect, the Minister was permitted to reassess beyond the normal reassessment period.

11. *Sarwari v. Canada,* 2009 TCC 357

In this Tax Court of Canada decision, the taxpayer appealed reassessments adding additional income for the 2000 and 2001 taxation years. Prior to the taxation years under appeal, the taxpayer transferred his mechanic business to an incorporated business. The taxpayer and his two brothers each owned one-third of the shares of the incorporated business. The taxpayer was convicted of dealing in stolen property, which attracted the attention of the CRA. The CRA completed a net worth analysis to determine if the taxpayer had any unreported income. For the 2000 and 2001 taxation years, the CRA determined the amount of unreported income to be $163,600.62 and $38,559.93, respectively. Penalties were also imposed pursuant to subsection 163(2) of the Act. Both reassessments were issued after the expiration of the normal reassessment period and so the onus was on the Minister to establish that the taxpayer had made a negligent or careless misrepresentation.

The Tax Court of Canada allowed the taxpayer's appeals in part, vacated the reassessment for 2000 taxation year and deleted the penalty imposed for the 2001 taxation year. For the 2000 taxation year, the Tax Court of Canada held that the Minister had failed to establish that the taxpayer made misrepresentations that were attributable to neglect, carelessness or willful default, or had committed fraud in filing his tax return pursuant to subsection 152(4) of the Act. The Tax Court found that many errors made by the auditor in the net worth analysis for the 2000 taxation year had a significant impact on the amount of unreported income. The Tax Court held that in 2001, the taxpayer had made misrepresentations that were attributable to neglect or carelessness, as he had not kept adequate records. The Minister was justified in reassessing the taxpayer for the 2001 taxation year. The Tax Court, however, deleted the penalties, as the taxpayer's conduct did not amount to gross negligence pursuant to subsection 163(2) of the Act.

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12. *Fontaine v Canada* 2013 DTC 1097

In this Tax Court of Canada case, the Minister reassessed the taxpayer for the 2003, 2004, and 2005 taxation years pursuant to subsection 152(4) of the Act. The taxpayer appealed, contesting the Minister's ability to make a reassessment after the normal assessment period for the 2003 and 2004 taxation years.

The taxpayer was the sole shareholder for System Gedoc Inc ("Gedoc"), a company operated by the taxpayer's spouse. The CRA auditor discovered that Gedoc did not have an established accounting system, and also noticed discrepancies in the balances at the beginning of the year and management fees paid out to the taxpayer. The taxpayer explained that she had not reported the management fees in her income tax returns because these amounts should have been recorded in the shareholder's loans account. However, no documentation regarding loans was submitted in the taxpayer's records. The unreported management fees amounted to more than half of the income reported over the period in question.

Pursuant to subsection 152(4) of the Act the onus is on the Minister to demonstrate that the taxpayer has made misrepresentations attributable to neglect, carelessness, or wilful default. Despite the fact that neither the taxpayer nor her spouse testified at the trial, based upon testimony by the CRA auditor, the Court found that there was still sufficient documentary evidence to justify a finding that the taxpayer had made misrepresentations through neglect, carelessness, or willful default.

The Tax Court of Canada noted that (i) the auditor did not receive any documentation establishing that Gedoc had made advances to the taxpayer as a shareholder, (ii) the bookkeeping was inadequate and (iii) the unreported income was a substantial amount in relation to the income actually reported. Based on these findings, the Tax Court of Canada held that the Minister had sufficient objective elements to prove neglect, carelessness or wilful default, and that therefore the Minister was justified in making a reassessment after the normal reassessment period.

13. *Ha v The Queen* 2011 DTC 1214

In this Tax Court of Canada case, the Minister used the net worth method to reassess the taxpayer's income for 2000, 2001, 2002 and 2003 respectively. The 2000 and 2001 taxation years were reassessed beyond the normal assessment year.

The taxpayer was a berry picker and fisherman. He was stopped and questioned by security personnel at the Vancouver International Airport, where he was found to have $40,000 cash in his possession. The RCMP did not have enough information to seize the cash, but remaining suspicious they sent a referral to the CRA. The CRA reviewed the taxpayer's income tax returns and determined that the amounts of income reported were likely not enough to support the taxpayer and allow him to save $40,000. For this reason the CRA reassessed the taxpayer on a net worth basis, relying on bank deposit analysis, bank statements, mortgage applications and mortgage statements.

The Tax Court held that the Minister was justified in reassessing the statute barred years. The Tax Court came to this conclusion because (i) the taxpayer did not have a credible explanation for the unreported income in 2000 and 2001; and (ii) while the taxpayer had an accountant prepare his tax returns, he admitted that he had not given his accountant complete information.

14. *Aridi v Canada* 2013 DTC 1123

In this Tax Court of Canada case, the Minister reassessed the taxpayer in 2009, outside the normal assessment period pursuant to subsection 152(4)(a) of the Act, in respect of the 2004 taxation year. The Minister added $83,465 to the taxpayer's taxable income, an amount related to the disposition of a one-half interest in a 96-unit rental building. In his 2004 tax return the taxpayer had reported a rental loss from an immovable and a capital loss from the disposition of shares; however he did not report the capital gain associated with the sale of the building.

The taxpayer, a civil engineer from Lebanon had used the services of his accountant since 1999. In filing his return for the year in question, the taxpayer gave all his documents to his accountant, spent two hours with the accountant and reviewed each document given to him. The accountant erroneously gave the taxpayer poor advice, that instead of reporting the capital gain in his 2004 income tax return, he could defer reporting the capital gain until a later year in which he disposed of the remaining half of the building. Following the advice of the accountant, the appellant attempted to defer the gain by using a rollover treatment, which had no legal or fiscal basis. It was a fabrication or an error on the part of the accountant, who presumably believed that by making an election under section 85 of the Act, the appellant could defer the capital gain realized until the other one-half of the building was disposed of.

The taxpayer argued that the error on his return was attributable to his reliance on his accountant's negligent advice, and that it could not be attributed to any neglect, carelessness or wilful default on his part. The Minister argued that the taxpayer was negligent because he did not ask sufficiently specific questions when he was reviewing his tax return. The Tax Court found that the taxpayer had acted as a wise and prudent

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person. The Tax Court held that the Minister had not discharged its burden of demonstrating taxpayer negligence and therefore allowed the taxpayer's appeal and ordered that the assessment be vacated.

15. ***The Queen v Last*, 2014 DTC 5077**

This Federal Court of Appeal case concerns an appeal by the Minister and a cross appeal by the taxpayer. Both appeals concern the decision of the Tax Court of Canada, regarding the Minister's reassessment of the 2000, 2001, and 2002 tax years.

The Minister's appeal concerned the Tax Court's judgment regarding transactions involving the shares of InternetStudieo.com Inc (ISTO shares) during 2002. On his tax return the taxpayer had declared the proceeds from the disposition of the shares to be capital gain. The Tax Court found that (i) the proceeds from the disposition of the shares were business income, and (ii) the taxpayer was entitled to additional deductions of $265,070 when calculating his income. In the result, the effect of the recharacterization of the ISTO share transaction did not increase the taxpayer's tax liability.

On appeal the Minister claimed that (a) the Tax Court erred and that the taxpayer's appeal should have been dismissed by the Tax Court, and (b) by subsection 152(9) of the Act, the Minister was allowed to advance a new argument in support of the assessed quantum of tax liability.

In response to the Minister's first claim, the Federal Court of Appeal found that (i) the proceeds of the disposition on the sale of the ISTO share were $601,136; (ii) treating the transaction as being on account of business income would increase the taxpayer's income by $300,565; (iii) the Tax Court had found that the taxpayer was entitled to additional deductions of $265,070; (iv) if the taxpayer's appeal had been dismissed, then the additional deductions would not have been established and the effect would be to increase the taxpayer's income by the difference between $300,565 and $265,070. The Federal Court of Appeal held that this result would be inconsistent with the principle that the Minister cannot appeal from her own assessment, and therefore rejected the Minister's argument.

In response to the Minister's second claim, the Federal Court of Appeal held that the Minister cannot use subsection 153(9) to reassess outside the time limitations contained in subsection 152(4) of the Act.

The taxpayer's cross appeal concerned the Tax Court's judgment regarding rental income for the 2000 and 2001 taxation years. The taxpayer had not reported the rental income on his tax return and the Minister had not included this income in the assessments. On this issue, the Tax Court found that the taxpayer's failure to report income was a misrepresentation based on carelessness, neglect or wilful deceit, and that as a result a reassessment to include this income was not statute-barred.

On cross appeal, the taxpayer claimed that the Tax Court erred by ordering the Minister to reassess the tax payable on the rental income under subsection 152(4) of the Act, when the Minister had not raised the issue of misrepresentations in either oral or written arguments.

In response to the taxpayer's claim, the Federal Court of Appeal found that the taxpayer had admitted that the rental income should be included in his income and that this admission was an implicit admission of misrepresentation. Based on this finding, the Federal Court of Appeal held that taxpayer's admission of misrepresentation entitled the Tax Court Judge to allow for reassessment under subsection 152(4) of the Act. The Federal Court of Appeal dismissed the taxpayer's cross-appeal

The taxpayer's application for leave to appeal to the Supreme Court of Canada was dismissed.

16. *Vine Estate v. The Queen*, 2015 DTC 5063

In this Federal Court of Appeal case, the Estate of Stanley Vine (the "Estate") appealed the Minister's reassessment on the basis that it was made after the expiration of the normal assessment period.

Stanley Vine passed away on July 1, 2003. Immediately before his death, Stanley Vine directly held a one-half interest in the Victoria Park property, which was a rental property. Pursuant to subsection 70(5) of the Act, there was a deemed disposition of his interest in the property immediately before his death. The Estate acknowledged that the deemed disposition of this property resulted in both recaptured capital cost allowance and a capital gain. The Estate retained an accountant to prepare the final tax return for Stanley Vine. The accountant omitted the deemed disposition of the Victoria Park property in the final return. The final return was assessed on June 7, 2004. The accountant later on realized the error during the preparation of an amended return for the purpose of requesting a loss carryback. They included the capital gain and the recaptured capital cost allowance of the Victoria Park property in the amended return, which was filed on September 28, 2004.

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On June 1, 2009, the final return of Stanley Vine was reassessed. In addition to other changes not in dispute, Stanley Vine’s share of the net income relating to the Victoria Park property was revised to reflect the recaptured capital cost allowance as reported in the amended return. The Estate appealed the reassessment on the basis that it was made outside of the normal assessment period.

The Federal Court of Appeal held that it is irrelevant that the Minister could have examined the amended return and discovered that the recaptured capital cost allowance was now being included. The omission in the original final return for Stanley Vine was still a misrepresentation for the purposes of subparagraph 152(4)(a)(i) of the Act.

The Federal Court of Appeal then held that the misrepresentation was attributable to the Estate’s neglect or carelessness, and the Minister was entitled to make the reassessment after the expiration of the normal assessment period pursuant to subparagraph 152(4)(a)(i). As a careful and prudent person, the executor of the Estate should have reviewed the return and noted that the Victoria Park property was not included. If questions were raised about why the property was missing in the return, the error relating to the unreported recaptured capital cost allowance would have been found. The Estate did not exercise the required degree of care in reviewing the original final return for Stanley Vine, and its appeal was dismissed.

17. ***Robertson v. The Queen*, 2015 DTC 1207**

In this Tax Court of Canada case, the taxpayer exercised US-based stock options in 2006 and 2007, and failed to report the options in his tax returns of the respective years as required. The Minister justified reassessing the taxpayer beyond the normal reassessment period on the basis that the taxpayer made misrepresentations attributable to neglect, carelessness, or wilful default.

The taxpayer testified that at the time he filed the 2006 and 2007 returns, his view was that United States law applied to the options because of their country of origin and therefore, he needed to report the options in his US tax returns, but not in Canada. The taxpayer could not recall asking his accountant about the correctness of his understanding of the law.

The taxpayer was an attentive, knowledgeable, and organized president and/or director of many different Canadian, US, and offshore companies. Stock options in his name were commonplace. The Tax Court of Canada held that a prudent person in the

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taxpayer's situation should have at least verified the issue of the taxation of the options with his accountant or another professional advisor. The Court noted that subparagraph 152(4)(a)(i) is not punitive in its purpose, but rather remedial. Since it is not concerned with establishing culpability, innocent and honest mistakes can lead to a finding of neglect, carelessness, or willful default.

The Minister met the onus of establishing misrepresentation attributable to neglect, and the taxpayer's appeal was dismissed.

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Please contact Howard Alpert directly at (416) 923-0809 if you require assistance with tax and estate planning matters, tax dispute resolution, tax litigation, corporate-commercial transactions or estate administration.