

TAXPAYER RELIEF APPLICATIONS - PART II

This issue of the Legal Business Report provides current information to the clients of Alpert Law Firm regarding taxpayer relief applications to the CRA and applications to the Federal Court for judicial review of taxpayer relief decisions by the CRA. Alpert Law Firm is experienced in providing legal services to its clients in tax and estate planning matters, tax dispute resolution, tax litigation, corporate-commercial transactions and estate administration.

This issue of the Legal Business Report focuses on recent Federal Court of Canada decisions involving judicial review of taxpayer relief applications in the following circumstances: (i) time delays on the part of Canada Revenue Agency (the “CRA”); (ii) serious illness; and (iii) exceptional circumstances.

A. TIME DELAYS BY THE CRA

1. *Cole v. Attorney General of Canada, 2005 DTC 5667*

In this Federal Court of Canada decision, due to litigation in the Federal Court regarding the taxpayer’s 1983 taxation year, the assessment for the taxpayer’s 1987-1988 taxation year was delayed. The taxpayer made a request for fairness relief from interest owing in respect of the taxpayer’s 1987-1988 assessment. The Minister refused to grant any relief to the taxpayer. The taxpayer applied to the Federal Court for judicial review of the Minister’s first level decision. The Federal Court granted the application for judicial review of the first level decision and referred the matter back to the Minister for reconsideration.

At the second level, the Minister granted some relief but stated that delays resulting from court proceedings are beyond the control of the CRA and are not taken into consideration in granting relief. The taxpayer made a second application to the Federal Court for judicial review of the second level decision.

The Federal Court granted the taxpayer’s application for judicial review. The Federal Court held that the fairness legislation does not restrict relief to situations involving delays within the Minister’s control. Delays in court proceedings, depending on the circumstances, could also be considered as grounds for granting fairness relief.

Accordingly, the Minister's fairness decision was quashed and the matter was again referred back to the Minister for reconsideration.

2. Telfer v. Canada Revenue Agency, 2009 DTC 5046

In this Federal Court of Appeal decision, the taxpayer filed Notices of Objection for the taxation years 1993 to 1999 inclusive (except 1995). With the taxpayer's consent, the CRA opted to hold the taxpayer's Notices of Objection in abeyance, as the issue raised therein was substantially similar to that in a case that was before the Tax Court of Canada at the same time. At the time of the decision, the CRA informed the taxpayer that interest would continue to accumulate on the unpaid balance. Approximately two years later, following the decision of the Tax Court in the similar case, the CRA and the taxpayer agreed on a settlement. The taxpayer applied for interest relief on the grounds of departmental delay and financial hardship. The Minister denied the request, and the taxpayer appealed to the Federal Court for judicial review.

The Federal Court allowed the taxpayer's application for judicial review. Applying **Cole**, the Federal Court held that even though the taxpayer was not a party to the proceedings that caused the delay, the delay can nevertheless be a basis for relief under the fairness provisions. The Federal Court held that although the taxpayer agreed to the delay and was informed that interest would continue to accumulate, it would not be fair to impose all of the interest on her. Therefore, the Federal Court allowed the taxpayer's application and referred the matter back to another agent of the Minister, noting that the taxpayer should only be required to pay half of the interest accrued during the waiting period.

The Federal Court of Appeal reversed this decision in favour of the CRA. The Federal Court of Appeal held that the trial judge should not have intervened with the Minister's decision, and made an error in law by utilizing a standard of correctness, instead of reasonableness. The Federal Court of Appeal found that when reviewing for unreasonableness, a court must examine the decision making process to ensure that it is: (i) rational; (ii) transparent; and (iii) falls within a range of possible outcomes. Applying the correct standard of reasonableness, the Federal Court of Appeal held that the decision of the Minister was reasonable because the Minister: (i) was aware of all the relevant facts; and (ii) did not exclude relevant facts from consideration.

An application for leave to appeal was denied by the Supreme Court of Canada.

3. **Lalonde v. Canada Revenue Agency, 2010 DTC 5139**

In this Federal Court of Canada decision, the taxpayer was reassessed for his 1992 and 1993 taxation years in connection with his investment in a tax shelter relating to flow-through shares in a mining company. On his 1992 and 1993 tax returns, the taxpayer claimed tax deductions of \$9,600 and \$12,000 respectively, in connection with the shares. In 1995, the CRA began an investigation concerning the exploration expenses of the mining company.

Following the investigation in 2000, the CRA sent notices of reassessment to the taxpayer for his 1992 and 1993 taxation years. There was no explanatory letter from the CRA accompanying the assessment and no subsequent correspondence between the CRA and the taxpayer. The taxpayer claimed to have contacted the CRA regularly for five years regarding the progress of his file, but was never able to obtain any information. This claim was not contradicted by the CRA. The Minister denied the taxpayer's fairness request on the basis that there was no undue delay on the part of the CRA.

In a Federal Court decision, cited at 2009 DTC 5025, the Federal Court allowed the taxpayer's application for judicial review. Applying the reasonableness standard of review, the Federal Court stated that the appropriate test is whether after a "somewhat probing examination", the reasons provided by the CRA, when taken as a whole, can support the impugned decision. The Federal Court held that although it is not necessary for every element of the reasoning in the decision to meet the reasonableness standard, the reviewing judge must be satisfied that the administrative decision-maker made a reasonable decision on the whole after (i) fully reviewing the taxpayer's file and (ii) taking all the relevant criteria into account. The Federal Court also held that where relief is denied or granted, the Minister must provide the taxpayer with an adequate explanation of the reasons for the decision, and how the relevant factors were applied.

The Federal Court held that the CRA did not provide a reasonable explanation for a large portion of the delays since December 2001. The delays were found to be mainly due to the actions of the CRA. Furthermore, the taxpayer was not informed within a reasonable time that his file had been suspended pending decisions to be rendered in similar cases. Thus, the matter was referred back to the Minister for redetermination.

On May 13, 2008, the Minister granted further partial relief from interest for certain periods, but refused to grant relief from all interest accruing in the 1992 and

1993 assessments after December 2001. The taxpayer applied again to the Federal Court for judicial review.

The Minister's delegate in the current case argued that the taxpayer knew he had a balance owing after he received his reassessments and that it was his fault if interest then accrued because he should have paid off his balance in order to avoid that accrual. This was despite the Federal Court's decision in 2009 that the delays in processing the fairness request primarily arose because of actions of the Agency.

The Federal Court again allowed the taxpayer's application for judicial review. The Federal Court held that the Minister's delegate misinterpreted and misapplied the Fairness Guidelines. While the Minister's delegate did not take into account all the factors in the guidelines, he also did not take into account the Federal Court's 2009 decision. Therefore, the matter was referred back to the Minister for redetermination.

B. SERIOUS ILLNESS

1. Lemerise v. Attorney General of Canada, 2010 DTC 5068

In this Federal Court of Canada case, the taxpayer filed his 2006 return nearly one year after the filing deadline. Consequently, the Minister imposed interest and penalties on the taxpayer for late filing. The taxpayer made a request for relief, seeking the cancellation of the interest and penalties. He claimed that he suffered from attention deficit hyperactivity disorder (ADHD), which was the reason behind the late filing, and that this was a situation beyond his control. However, the Minister denied this request, and also decided not to cancel the interest and penalties upon a second review. The taxpayer challenged this decision, arguing that his late filing was due to his medical condition and not because of negligence or carelessness.

The Federal Court dismissed the taxpayer's application for judicial review. In its decision, the Federal Court cited Young v. Canada, 98 DTC 6028, stating that taxpayers who cite their medical condition in support of a request for relief from penalties or interest have the burden of proving that their condition was a factor beyond their control and that the interest owed was primarily caused by this factor. In this case, the taxpayer submitted a note from his doctor; however, it contained insufficient information and did not explain how his medical condition would have prevented him from filing his tax return on time. The following are examples of the types of information that a court may be seeking in a doctor's note:

- (i) The recommended dosage;
- (ii) The possible effects the medication may have on the taxpayer;
- (iii) How long the taxpayer has been taking the medication;
- (iv) The taxpayer's general health (i.e. why the applicant performs well in some areas of activity and less well in others); and
- (v) In what way the medication may hamper the taxpayer in his ability to perform certain tasks, such as filing his annual tax return.

Furthermore, there were gaps in the taxpayer's past filings, in that he was able to file on time in some years but not others. Thus, the taxpayer's application for judicial review was dismissed.

C. EXCEPTIONAL CIRCUMSTANCES

1. Cooke v. Attorney General of Canada, 2010 DTC 5077

In this Federal Court of Canada case, the taxpayer carried on business in the real estate field. The taxpayer had a tax liability of over \$110,000. The taxpayer claimed that he was unable to pay the liability, penalties and interest claimed from him due to the major financial hardship and the state of his health. Based on these circumstances, the taxpayer made a request to the CRA to cancel the interest and penalties. The request was denied on the basis that the taxpayer had not proved financial hardship (i.e. an inability to provide himself with basic necessities and, within reasonable limits, to obtain other non-essential items). This decision was confirmed in a second review. The taxpayer applied to the Federal Court for judicial review.

The Federal Court dismissed the application for judicial review. The taxpayer submitted that the real estate crisis was similar to extraordinary circumstances as discussed in the Fairness Guidelines, as it was an event beyond his control. However, the Federal Court held that the real estate crisis was caused by a series of decisions made by businesspeople, and did not arise out of extraordinary circumstances such as the examples provided in the Fairness Guidelines (e.g. fires, floods, and other natural disasters).

The taxpayer also submitted that he was depressed as a result of the real estate market crisis. However, the Federal Court found that during the period under review, and notwithstanding the physician's note, the taxpayer had gone about his affairs. More importantly, during that period, the taxpayer made it a priority to pay certain creditors, to the detriment of the CRA. Thus, the Federal Court dismissed the taxpayer's application.

2. **CPNI Inc. v. Minister of National Revenue, 2013 FC 96**

In this Federal Court of Canada case, the taxpayer was a corporation, and requested relief from interest and penalties for the taxation years 2008 to 2010 on the basis of inability to pay. The taxpayer accrued operating losses in 2008, 2009 and 2010 and failed to remit withholding taxes on behalf of its employees. The taxpayer was developing a new product line aimed at the banking community, but its target customers were adversely affected by the mortgage lending crisis in 2008. The Minister cancelled the interest but refused to cancel the penalties. The taxpayer claimed that the financial crisis qualified as a "man-made disaster" under paragraph 25 of the Fairness Guidelines and that the penalties should have been cancelled on that basis.

The Federal Court dismissed the taxpayer's appeal. The Federal Court found that the taxpayer had not presented its argument that the financial crisis qualified as a "disaster" to the Minister in its first or second level review requests. Therefore, the Minister's failure to consider this argument could not be considered unreasonable. The Federal Court cited **Cooke v Canada (Attorney General)**, 2009 FC 1161, in which the Court held that the real estate slump in the 1990s was "caused by a series of decisions made by businesspeople" and "did not arise out of extraordinary circumstances such as the examples in the Guidelines". Agreeing with this analysis, the Federal Court held that in a market economy, financial fluctuations are not extraordinary.

The Federal Court also considered paragraph 28 of the Guidelines, which refers to "exceptional situations" and gives the following example: "when a business is experiencing extreme financial difficulty, and enforcement of such penalties would jeopardize the continuity of its operations, the jobs of the employees, and the welfare of the community as a whole, consideration may be given to providing relief of the penalties." The Federal Court found that the taxpayer failed to make any submissions regarding the continuity of operations, the impact on employees, or the impact on the welfare of the community. Therefore, the Minister was unable to consider whether the taxpayer's circumstances were related to an exceptional situation as contemplated by paragraph 28. On the whole, the Federal Court found that there was nothing unreasonable in the Minister's decision and thus dismissed the taxpayer's appeal.

D. REFUNDS BEYOND THE NORMAL THREE-YEAR PERIOD**1. Hoffman v. Attorney General of Canada, 2010 FCA 310**

In this Federal Court of Appeal decision, the taxpayer made a request for reassessment under subsection 152(4.2) of the Act, which allows the Minister to reassess beyond the normal three-year reassessment period in order to give taxpayers a refund or reduce taxes payable for a given taxation year. The taxpayer requested a recalculation of accrued interest relating to his 1998 taxation year, claiming that a \$35,000 payment made to the CRA in December 1998 was treated as if it had been made in 1999. The taxpayer also requested an increase of \$78,000 to his capital loss account or allowable business investment loss account to reflect the cost of his shares of a failed corporation, and a \$20,000 deduction for legal and accounting expenses.

The Court dismissed the taxpayer's appeal. The Court found that the Minister had thoroughly reviewed and considered the information the taxpayer had submitted, and that the Minister's decision was reasonable. Furthermore, given the adjustments sought, the nature and quality of the documentary evidence provided, and the confusing manner in which the taxpayer attempted to explain his claims, the Minister's determination that the claims were not proved well enough to justify a further reassessment was reasonable. Lastly, the Court found that the \$35,000 payment was in fact applied to the taxpayer's 1998 taxation year, and that the taxpayer's interest debt was therefore determined correctly.

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