

May 1997

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Recommended Citation

Li, Jinyan (1997) "Taxpayers' Rights in Canada," *Revenue Law Journal*: Vol. 7 : Iss. 1 , Article 6.

Available at: <http://epublications.bond.edu.au/rlj/vol7/iss1/6>

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Abstract

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Keywords

taxpayers rights, Canada, tax, income tax

Cover Page Footnote

The author wishes to thank her colleague, Professor Tim Edgar, for his comments on the drafts of this article and her research assistant, Stephen Gillespie, a student at the Faculty of Law, University of Western Ontario, for his assistance throughout the preparation of this article.

TAXPAYERS' RIGHTS IN CANADA*



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This article provides an overview of taxpayers' rights in Canada. Following an overview of the sources of taxpayers' rights in Canada, it discusses basic rights of taxpayers during the process of tax administration, such as the right to information, to confidentiality, to privacy, and of appeals. It then examines taxpayers' rights under the Charter to equality, to freedom of conscience and religion, and to certainty of law. Finally, the article discusses the fairness legislation which was designed to provide relief to taxpayers in certain circumstances.

I INTRODUCTION

The protection of taxpayers' rights is an important part of the Canadian income tax system, which has been based on self-assessment since its inception in 1917.¹ The operation of the self-assessment system depends on taxpayers' voluntary compliance with the law and taxpayer honesty in preparing tax returns.² Taxpayer honesty is contingent, to a significant but unmeasurable extent, on the perception and reality that the system treats taxpayers decently and fairly. Taxpayers are more likely to comply with the law if they perceive the system as being fair and their basic rights are

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¹ Income War Tax Act 1917. The self-assessment system was adopted primarily because of its cost effectiveness.

² See Justice Wilson of the Supreme Court of Canada in *MacKinlay Transport Ltd v The Queen* [1990] 2 CTC 103 at 108; 90 DTC 6243 at 6246.

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clearly set out and respected.³ The self-assessment system also depends on the government's ability to verify information reported by taxpayers and to detect non-compliance. The responsibility for administering income tax is vested in the Department of National Revenue ("Revenue Canada") headed by a cabinet minister (the "Minister of National Revenue"). Revenue Canada has broad powers in the administration and enforcement of the Income Tax Act (the "Act").⁴ To ensure that taxpayers' perception of the fairness of the tax system is not undermined, the Act and other laws in Canada provide various measures to recognize the fundamental rights of taxpayers and to protect taxpayers against the misuse of the powers by Revenue Canada.

This article provides an overview of taxpayers' rights in Canada. It discusses these rights in two categories: the rights of taxpayers that are inextricably tied up in the administration of the Act and the powers of Revenue Canada; and the rights of all individuals recognized under the Canadian Charter of Rights and Freedoms (the "Charter")⁵ that can be invoked by taxpayers in tax cases. Following a brief review of sources of taxpayers' rights in Canada in Part II, Part III of the article discusses basic rights of taxpayers during the process of tax administration and enforcement. Part IV examines the rights of taxpayers under the Charter. In Part V, the article discusses the fairness legislation which was designed to provide relief to taxpayers in certain circumstances. The article concludes that the fairness legislation might be expanded to improve the fairness of the Canadian tax system. In general, Canadian taxpayers seem to consider that Revenue Canada is fair and that their rights are adequately recognized under the law.

II SOURCES OF TAXPAYERS' RIGHTS

Since its introduction, the Act has always recognized the basic right of taxpayers to privacy, to confidentiality, and to appeal the decisions of the administration. During the past two decades, there has been an increasing recognition of taxpayers' rights. In 1982, the

³ OECD, *Taxpayers' Rights and Obligations: A Survey of the Legal Situation in OECD Countries* (OECD 1990) at 10; Owens J, "Taxpayers' Rights and Obligations" 1990/11 *Intertax* 554-71; Roth JA, Scholz JT and Dryden Witte A (eds), *Taxpayer Compliance*, vol 1 (Philadelphia, University of Pennsylvania Press 1989) at 129-130.

⁴ Income Tax Act (RSC 1985 (5th Supp) c 1.

⁵ Part I of the Constitution Act 1982, being schedule B to the Canada Act 1982 (UK) 1982, c 11, proclaimed in force 17 April 1982.

Charter was enacted to guarantee fundamental individual rights in Canada, some of which are important rights to taxpayers. Since then, numerous amendments to the Act have been made to make the Act consistent with the Charter. In 1985, Revenue Canada released the Declaration of Taxpayer Rights aimed at improving the Department's credibility and taxpayers' perception of fairness in the tax system; it indicated a shift in attitude that was needed to create a climate conducive to providing better protection of taxpayers' rights. In 1991, the fairness legislation was introduced to provide the Minister with discretionary powers to waive interest and penalties and to extend the assessment period in certain circumstances.

At present, the fundamental rights of taxpayers are described in the Declaration of Taxpayer Rights, but this document has no legal authority and provides no real protection for taxpayers. The sources of taxpayers' rights in Canada are the Charter, the Act, other statutes, and the common law.

A The Charter

The Charter is the supreme law in Canada.⁶ Its effect on Canadian law and legal development has been profound. The area of taxation is no exception. Provisions in the Act have been challenged under the Charter, some of which have resulted in legislative changes. For example, the search and seizure procedure was revised in 1986, after the Supreme Court of Canada held in *Hunter v Southam*⁷ that a similar provision in another statute was unconstitutional. The Charter rights that have been invoked in tax cases include:

- the right to freedom of conscience and religion (s 2);
- the "right to life, liberty and security of the person and the right not to be deprived thereof except in accordance with the principles of fundamental justice" (s 7);
- the right against unlawful search and seizure (s 8);
- the right against self-incrimination (s 11(c));
- the right to be protected from double jeopardy (s 11(h)); and

⁶ Section 52(1) of the Constitution Act provides: "[t]he Constitution of Canada is the supreme law of Canada, and any law that is inconsistent with the provisions of the Constitution is, to the extent of the inconsistency, of no force or effect". Section 32(1) of the Charter provides that the Charter applies to the Parliament and government of Canada, as well as to the legislature and government of each of the provinces of Canada.

⁷ [1984] 2 SCR 145; 84 DTC 6467.

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- the equality rights (s 15(1)).⁸

The application of the Charter at various stages of the tax administration process will be discussed in Part III of the article. The equality rights, the right to freedom of conscience and religion, and the right to certainty in law are discussed separately in Part IV.

B Declaration of Taxpayer Rights

The Charter has not only resulted in the amendment of some provisions of the Act, providing taxpayers with greater protection, but has also caused changes in the relationship between taxpayers and Revenue Canada. The Declaration of Taxpayer Rights is Revenue Canada's response to the Charter. Although the document has no legal status, it is of great practical use in shaping the attitude of Revenue Canada in its dealings with taxpayers.⁹ It is widely circulated and appears in every income tax annual filing manual.

The Declaration of Taxpayer Rights states that, in dealings with Revenue Canada on income tax matters, taxpayers are entitled to complete and accurate information about the Act, to courteous and considerate treatment and to a presumption of honesty, unless there is evidence to the contrary. It advises taxpayers that fair handling of a complaint is one of their fundamental rights and that one of Revenue Canada's obligations is to help taxpayers exercise their rights. Furthermore, the document reiterates the rights of taxpayers under the Charter and other laws of Canada. Finally, the document declares that taxpayers are entitled to arrange their affairs to pay the least amount of tax allowed by law and that Revenue Canada is committed to applying the law in a consistent and fair manner and will be firm with those who evade tax.

C Taxation and other statutes

Canada does not have a separate tax administration or management statute. Administrative provisions and some taxpayer rights are found in the Act. For example, Part I (Divisions I and J) of the Act

⁸ Section 15 (1) of the Charter provides: "[E]very individual is equal before and under the law and has the right to the equal protection and equal benefit of the law without discrimination and, in particular, without discrimination based on race, national or ethnic origin, colour, religion, sex, age or mental or physical disability".

⁹ Scott Butler A, "Charter Challenges to Income Tax Provisions", *The Report of Proceedings of the Forty-Sixth Tax Conference, 1994* Conference Report (Canadian Tax Foundation 1995) 29 at 29.

governs returns, assessments and appeals; Part XV of the Act deals with the administration and collection of taxes and offences. Taxpayers' rights recognized in the Act include:

- the right to confidentiality (s 241);
- the right of appeal against the decision of Revenue Canada (s 169 and s 175);
- the right against unlawful search and seizure (s 231.1, s 231.2(2));
- solicitor-client privilege (s 232);
- the right to apply for waiver or cancellation of interest and penalties and other relief under the fairness legislation; and
- the right to withhold disputed amounts, to the extent allowed by law, until the dispute is resolved (s 179.1).

The Access to Information Act¹⁰ and the Privacy Act¹¹ provide the right to access information from the government and the protection of individual privacy, respectively. Subject to some restrictions discussed below, these statutes enable taxpayers to obtain all information from Revenue Canada in connection with a tax assessment and Revenue Canada's interpretation of the law.

D Common law

Some fundamental rights of taxpayers stated in the Declaration of Taxpayer Rights are not clearly set out in the Charter, the Act, or other statutes, but are based on principles developed in the common law. These rights include the right to certainty, the right to be informed by the tax administration, the right to be treated fairly, and the right to arrange their affairs to minimize tax liability.

III PROCEDURAL RIGHTS

This Part discusses the fundamental rights of taxpayers at various stages of tax administration and explains how these rights are recognised in the face of the extensive powers of Revenue Canada in administering the Act.

¹⁰ RSC 1985, c A-1.

¹¹ RSC 1985, c P-21.

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A Self-assessment and Revenue Canada's power to gather information

Under s 150(1) of the Act, taxpayers must file an annual tax return in prescribed form.¹² The returns generally require the reporting of all relevant income and expenses with some supporting documentation. Detailed records and books of account are not required to be filed with the returns, although they must be kept by taxpayers in accordance with s 230 of the Act.¹³ The records and books of accounts must be kept in such form and contain such information that the taxpayer's liability can be determined and provided to the Minister upon demand during audit or investigations. Taxpayers bear the burden of proof in appeals of assessment to the Tax Court of Canada.

Information gathering

In addition to tax returns, Revenue Canada obtains information from taxpayers in various other ways, such as information returns filed by taxpayers and third parties in respect of specific transactions.¹⁴ Revenue Canada uses these information returns to verify information reported by a taxpayer on the tax return and to detect non-filing of returns. Major information returns include returns dealing with:

- remuneration paid to employees;
- payments of dividends, interest or royalties to residents in Canada;
- payments of dividends, interest, royalties, rents and other amounts to non-residents of Canada;

¹² Under s 150(1) of the Act, every individual who is liable to pay tax in a particular taxation year must file a return for that year, and every corporation must file an annual return, regardless of whether any tax is payable. The Minister has the power under s 150(2) to demand the filing of a return by an individual who is not liable to tax.

¹³ The books of account must include an annual inventory kept as required in sections 1800-1802 of the Regulations. The records and books of account must be kept at the taxpayer's place of business or residence in Canada. If they are kept outside Canada or at some other place in Canada, the places where they may be kept can be designated by the Minister.

¹⁴ Section 221(1)(d) of the Act authorizes the Governor in Council to make regulations, among other things, to require any person to make information returns in respect of any information required in connection with assessments under the Act. Part II of the Regulations outlines the requirements for filing information returns in prescribed forms.

- accrued bond interest paid by a financial institution by virtue of the redemption, assignment or other transfer of a bond, debenture or similar security;
- membership in a partnership that carries on business in Canada;
- security transactions if the corporation is a trader or dealer in securities;
- transactions with related non-resident corporations;¹⁵
- offshore investments of Canadians in respect of specified foreign property (bank accounts, portfolio investments, real estate etc. with a total cost exceeding \$100,000), foreign affiliates, transfers to non-resident trusts, and distributions received from non-resident trusts.¹⁶

In addition, the Minister has the power to demand information or documents from a taxpayer or a third party. This power is generally used during audits or investigations of tax evasion or tax avoidance schemes and is discussed further below.

Right to confidentiality

Tax returns and other information obtained by the Minister can only be used for the purposes of the administration and enforcement of the Act. Confidentiality of taxpayer information has been considered an important part of the Canadian income tax collection system:

Parliament recognized that to maintain the confidentiality of income tax returns and other obtained information is to encourage the voluntary tax reporting upon which our tax system is based. ... By instilling confidence in taxpayers that the personal information they disclose will not be communicated in other contexts, Parliament encourages voluntary disclosure of this information. The opposite is also true: if taxpayers lack this confidence, they may be reluctant to voluntarily disclose all of the required information.¹⁷

¹⁵ Section 233.1 of the Act. Every corporation resident in Canada or carrying on business in Canada must file an information return in respect of transfer pricing transactions with each non-resident with whom it was not dealing at arms length at any time in the year.

¹⁶ On 5 March 1996, the government released draft legislation and forms that will provide Revenue Canada with information concerning offshore investments of Canadians. Four new information returns are required by the draft legislation. For further, see Nitikman J, "The New Foreign Property Reporting Rules" (1996) 44 *Canadian Tax Journal* 425-450.

¹⁷ *Slattery (Trustee of) v Slattery* [1993] 2 CTC 243 at 247-248; 93 DTC 5443 at 5445-5446.

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Section 241¹⁸ prohibits Revenue Canada from disclosing taxpayer information, except in certain specified situations. The purpose of s 241 was stated by the Supreme Court of Canada as follows:

[S]ection 241 involves a balancing of competing interests: the privacy interest of the taxpayer with respect to his or her financial information, and interest of the Minister in being allowed to disclose taxpayer information to the extent necessary for the effective administration and enforcement of the Income Tax Act and other federal statutes referred to in s 241(4). ... [A]ccess to financial and related information about taxpayers is to be taken seriously, and such information can only be disclosed in prescribed situations. Only in those exceptional situations does the privacy interest give way to the interest of the state.¹⁹

The scope of confidentiality under s 241 is limited to "taxpayer information", which is defined as:

information of any kind and in any form relating to one or more taxpayers that is (a) obtained by or on behalf of the Minister for the purposes of this Act, or (b) prepared from information referred to in paragraph (a) but does not include information that does not directly or indirectly reveal the identity of the taxpayer to whom it relates.²⁰

Disclosure of taxpayer information is prohibited under s 241(1) and s 241(2). Subsection 241(1) prohibits Revenue Canada from knowingly providing taxpayer information to any person, from knowingly allowing anyone access to such information, and from knowingly using it otherwise than in the course of administrative or enforcement duties under the Act, or for other purposes specified in this provision. It is only government "officials" who are subject to the prohibition.²¹ Breaches of the confidence are subject to penalties under s 239(2.2): a fine of up to \$5,000, or imprisonment for a term not exceeding 12 months; or both.

¹⁸ Section 241 has its origin in s 11 of the 1917 Income War Tax Act, which was re-enacted as s 81 of the 1927 Income War Tax Act. In 1948, the provision was re-enacted as s 121; in 1952, as s 133. In 1966, s 133 was substantially amended to prohibit communication of information to anyone and to create numerous exceptions. In 1970, s 133 became s 241.

¹⁹ *Slattery*, above n 17 at 248 and 5446.

²⁰ Section 241(10) of the Act. There has been no judicial interpretation of the meaning of the phrase "directly or indirectly reveal the identity of the taxpayer".

²¹ "Officials" include persons formerly employed as government officials: s 241(10) of the Act.

Subsection 241(2) provides that an official cannot be required, in connection with any legal proceedings, to give or produce evidence relating to taxpayer information. The leading case interpreting this provision is *Re Glover v Glover*.²² The Court held that s 241(2) was an "all-embracing section" which applied to any legal proceeding other than criminal and income tax proceedings. In a divorce action, Mrs Glover was awarded the custody of her two young children, but Mr Glover absconded with the children. When a decree nisi was granted, a judge of the Supreme Court of Ontario made an order directing, *inter alia*, that Revenue Canada provide the Court with particulars of the addresses of Mr Glover. The Minister moved to set aside the order, but this was denied by the trial judge. The Minister's appeal was allowed. The Court of Appeal of Ontario held that the address of a taxpayer was a necessary and integral part of the information received by the Minister for the purposes of the Act; such information could only be communicated to persons authorized to receive it by virtue of the exceptions in s 241; neither the court nor Mrs Glover was such a person.²³

The Act authorizes the Minister to disclose taxpayer information where a taxpayer's interest in privacy is outweighed by the public interest in administering the criminal justice system, the Act, or government programs. Section 241 permits disclosure in the cases of:

- criminal proceedings (s 241(3)(a));
- any legal proceeding relating to the administration or enforcement of, *inter alia*, the Act (s 241(3)(b));

²² [1980] CTC 531, 80 DTC 6262 (OCA), *aff'd* [1982] CTC 29, 82 DTC 6035 (SCC), *sub nom Glover v MNR*.

²³ It should be noted that it is only the production of returns by the Minister that is in issue, not the production by a taxpayer of copies of her or his own returns. There is nothing in s 241 to protect taxpayers from an order requiring them to produce such copies (if they still possess them), along with any other of their business or financial records that may be required of them. See *Re Tucar and Tucar* [1981] 32 OR 798 (Ont UFC). In this case, the applicant had brought an application for an increase in her maintenance payments and during the course of the proceedings discovered that all the respondent's financial records had been seized by Revenue Canada. To obtain these records, the applicant applied to the Court for an order directing production from the respondent and Revenue Canada. The Court decided that it did not have the power to direct Revenue Canada to furnish the records, but it did make an order (to which Revenue Canada consented) directing the respondent to authorize Revenue Canada to produce all financial records held by Revenue Canada that related to him.

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- imminent danger of death or physical injury to any individual (s 241(3.1));
- intra-governmental or inter-governmental transfer of specified information (s 241(4)).

The exception under s 241(3) applies only where the criminal proceedings were commenced by the laying of an information or charge. Any disclosure of taxpayer information before a criminal charge is laid is prohibited.²⁴ In other words, confidential information may not be used to initiate the criminal proceedings. Once the proceedings have been initiated and a charge has been laid based on evidence independently obtained, the confidential information may then be used to substantiate the case. In some cases, even after the commencement of criminal proceedings, a taxpayer may be successful in prohibiting Revenue Canada from disclosing her or his tax information by invoking s 7 of the Charter. In *Tyler v MNR*,²⁵ for example, the taxpayer was required by the Minister, pursuant to s 231.2 of the Act, to provide information (signed statements of income, assets, liabilities and living expenses) when the taxpayer was facing charges under the Narcotic Control Act and the Criminal Code for, among other things, possession of property and proceeds of property derived from trafficking in narcotics. The taxpayer argued successfully that the communication to the police of the information required by Revenue Canada while the charges were outstanding would deny him the right to silence under s 7 of the Charter. The Federal Court of Appeal issued an order prohibiting Revenue Canada from communicating to the police the statements obtained under s 231.2.

Subsection 241(3) permits disclosure of taxpayer information in legal proceedings relating to the administration or enforcement of the Act.²⁶ The meaning of "a proceeding relating to the administration or enforcement of" the Act was interpreted in *Slattery v Slattery*.²⁷ In that case, following a lengthy investigation, a taxpayer was

²⁴ In *MNR v Fawcett* [1988] 2 CTC 62, the Supreme Court of British Columbia granted the Minister's petition to have a search warrant quashed and documents seized thereunder returned, where the documents in question had been released to the police before a criminal charge had been laid.

²⁵ *Tyler v MNR* [1989] 1 CTC 153 (FCTD), 89 DTC 5044, reversed [1991] 1 CTC 13 91 DTC 5022 (FCA).

²⁶ Section 241(3) extends to legal proceedings relating to the administration and enforcement of Canada Pension Plan, Unemployment Insurance Act and other Act of Parliament or law of a province that provides for the imposition or collection of a tax or duty.

²⁷ Above n 17.

petitioned into bankruptcy by Revenue Canada (the only preferred creditor of the estate). The trustee in bankruptcy brought an action against the bankrupt's spouse for a declaration that certain assets registered in her name were assets of the bankrupt's estate or were held in trust for the estate. When the trustee sought to introduce testimony at trial from two Revenue Canada officials who had participated in the investigation, the spouse objected on the ground that such testimony was barred by s 241. The Supreme Court of Canada rejected her argument that the only proceedings covered by the exception in s 241(3) were those expressly provided for in Part XV of the Act dealing with administration and enforcement of the Act. The majority of the Court held that the words "relating to" in s 241(3) should be interpreted broadly. The bankruptcy proceedings had a "relation" or "connection" with the enforcement of the Act in that they were necessary for the collection of taxes owing by the bankrupt and, therefore, the proceedings taken by the trustee were proceedings "relating to the administration or enforcement of the Income Tax Act". The exception in s 241(3) was thus applicable and Revenue Canada officials could testify in the proceedings.

Disclosure of taxpayer information is also permitted by s 241(4)(b), which provides that "an official may provide to any person taxpayer information that can reasonably be regarded as necessary for the purposes of determining any tax, interest, penalty or other amount that is or may become payable by the person, or any refund or tax credit to which the person is or may become entitled under the Act or any other amount that is relevant for the purposes of that determination". In effect, s 241(4)(b) permits Revenue Canada to disclose certain information obtained from one taxpayer (third-party information) to another taxpayer, if the information is related to the basis of an assessment of the other taxpayer. Such disclosure is not mandatory.

A taxpayer's right to information from Revenue Canada is often in conflict with a third-party's right to confidentiality in respect of her or his information. The balancing of these competing interests is influenced by the public interest in encouraging and promoting voluntary compliance by guaranteeing confidentiality of taxpayer information. The state of law on this issue is somewhat unclear.²⁸ At issue in *Huron Steel Fabricators (London) Ltd v MNR*²⁹ was the

²⁸ See Innes W and McCart J, "Transfer-Pricing Disputes: Access to and Disclosure of Information" (1995) 43 *Canadian Tax Journal* 821-868.

²⁹ *Huron Steel Fabricators (London) Ltd v MNR* [1973] CTC 422, 73 DTC 5347 (FCA).

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production of tax returns of a defunct company which was not party to the action. The trial judge inspected the documents in question and found that no harm to any public interest would be caused by their disclosure. The decision was upheld on appeal. A similar result was reached in *Amp of Canada Ltd v The Queen*,³⁰ where the taxpayer applied for an order requiring the production of its competitors' financial statements and tax returns which had been used by Revenue Canada to calculate the taxpayer's costs for income tax purposes, and one of the competitors objected. The Court found that the taxpayer had brought itself within the principles of *Huron Steel* and ordered production. The Court did, however, impose some restrictions on the disclosure: the actual disclosure of materials was limited to counsel and expert witnesses retained by counsel; the material was to be used exclusively for the purposes of the litigation; and the materials were to be returned at the conclusion of the litigation.

The decisions in *Huron Steel* and *Amp* may be contrasted with *Crestbrook Forest Industries Ltd v The Queen*.³¹ In *Crestbrook*, the taxpayer, a corporation engaged in manufacturing and exporting wood pulp and newsprint, sought to have Revenue Canada produce, on discovery, certain documents and information that Revenue Canada had relied on in assessing the taxpayer. These documents and information had been obtained, on behalf of Revenue Canada, in the course of a survey on wood pulp. Newsprint exporters and others who participated in the survey did so on the understanding that the information provided would be kept confidential. The Federal Court of Appeal held that production of the information for discovery or at trial should not be permitted. The Court stated that, "where the Crown has obtained information in confidence from taxpayers on a voluntary basis and for a specific and defined purpose, it may not subsequently make use of that information for a different purpose, namely the reassessment of other taxpayers, in circumstances where such use will almost inevitably result in a breach of the Crown's undertaking of confidence".³²

The disclosure of third-party information is a critical issue in international transfer pricing disputes. These disputes generally

³⁰ *Amp of Canada Ltd v The Queen* [1987] 1 CTC 256, 87 DTC 5157 (FCTD).

³¹ *Crestbrook Forest Industries Ltd v The Queen* [1992] 1 CTC 100; 92 DTC 6187 (FCA).

³² *Ibid* at 101; 6188-6189. The Court also held that the information could not advance the litigation in any event. The issue whether or not Revenue Canada could continue to rely on the assumptions in its reassessment of the taxpayer was not before the court.

involve large corporations, significant amounts of tax, and many peripheral and complex factual issues. As illustrated in *Amp* and *Crestbrook*, Revenue Canada may rely on information obtained from third parties to assess the income of a taxpayer. It is, therefore, imperative for the taxpayer to know the case against them in challenging the assessment. On the other hand, the resolution of transfer pricing disputes, in particular, through the use of an Advance Pricing Agreement (APA),³³ increasingly depends on voluntary disclosure of information by taxpayers to Revenue Canada and the confidentiality of such information. The balancing of one taxpayer's right to privacy and another taxpayer's right to information from Revenue Canada remains a policy issue in need of clarification.

B Assessment

When a taxpayer has filed a return, the Minister is required, with all due dispatch, to examine the return, and to assess the tax owing for the year and any interest and penalties payable.³⁴ The Minister must send a notice of assessment to the taxpayer. Subject to the limitation periods (three years for individuals and Canadian Controlled Private Corporations and 4 years for large corporations), the Minister has the power to reassess or make additional assessments. There are no prescribed forms for the notice. In some cases, however, defects in the form of a notice may be sufficiently severe as to allow a court to vacate the assessment or reassessment.³⁵

³³ The purpose of the APA is to promote voluntary compliance by assuring taxpayers that the agreed to transfer pricing methodology used to establish transfer prices is acceptable. See Information Circular 94-4: International Transfer Pricing: Advance Pricing Agreement, dated 30 December 1994.

³⁴ Section 152(1) of the Act. The phrase "with all due dispatch" has been interpreted to mean "within a reasonable time", "with all due diligence": see *Jolicoeur v MNR* [1960] CTC 346, 60 DTC 1254 (Ex Ct). According to the courts, the "with all due dispatch" time limit purports a "discretion of the Minister to be exercised, for the good administration of the Act, with reason, justice and legal principles": see *MNR v Appleby* [1964] CTC 323 at 340, 64 DTC 5199 at 5209 (Ex Ct).

³⁵ In *McConnachie v MNR* [1991] 2 CTC 2072, 91 DTC 873, the Court held in obiter dicta that the Minister's assessments were technically deficient in a number of ways, with the result that they were uninformative, misleading and unacceptable. Although the validity of the assessments had not been challenged by the taxpayers, the Court suggested that it would have been prepared to vacate them on the basis that the assessment process had not been completed because the Minister had failed to provide the taxpayers with proper notice of the various assessments.

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During the process of assessment, taxpayers have the right to information, to fair treatment, to apply for an advance ruling, and to apply for relief under the fairness legislation. In practice, although these rights have been recognized by the courts, they have been rarely enforced against the Minister.

Right to information

The Act imposes no legal obligation on the Minister to provide details of an assessment.³⁶ It has been held, however, that a taxpayer has the right to know the facts and assumptions upon which an assessment or decision of the Minister is based and that the Minister has a duty to disclose such facts and assumptions. In *Johnston v MNR*,³⁷ after deciding that the taxpayer bore the burden of challenging the facts found or assumed by the Minister as a basis for the assessment, the Supreme Court of Canada held that the Minister had a duty to disclose to the taxpayer "the precise findings of fact and rulings of law which have given rise to the controversy".³⁸ The extent of disclosure is unclear; the provision of certain basic information seems sufficient.³⁹

Pursuant to the Privacy Act and the Access to Information Act, a taxpayer has the right to access any record under the control of Revenue Canada. Subject to some limitations, such as the confidentiality requirement under s 241 of the Act and the solicitor-client privilege under s 232 of the Act, where a taxpayer demands access to information obtained by Revenue Canada, the taxpayer will generally receive the complete file assembled by Revenue Canada, including inter-office memoranda and reports.⁴⁰

The Declaration of Taxpayer Rights informs taxpayers that, "you are entitled to complete and accurate information about the Income Tax Act, the entitlements it allows you, and the obligations it

³⁶ *Laurin v MNR* [1960] CTC 194, 60 DTC 1143 (Ex Ct); *Smerchanski v MNR* [1972] CTC 117, 72 DTC 6117 (FCTD). However, certain basic information must be provided in a reassessment: see *Leung v MNR* [1993] 2 CTC 284, 93 DTC 5467 (FCTD); *Wallace v MNR* [1991] 2 CTC 2341, 91 DTC 1134 (TCC), and *McConnachie*, above n 35.

³⁷ *Johnston v MNR*, [1948] CTC 195; (1948) 3 DTC 1182 (SCC).

³⁸ *Ibid* at 203 and 1183. See also *MNR v Wrights' Canadian Ropes Ltd* (1946) 2 DTC 927 (PC), 794 (SCC).

³⁹ *Stephens Estate v The Queen* [1987] 1 CTC 88, 87 DTC 5024 (FCA).

⁴⁰ See Mitchell WJA and Potvin J, "Canada" in *Protection of Confidential Information in Tax Matters*, (*Cahiers de Droit Fiscal International (Studies on Int'l Fiscal Law)* Vol LXXVIb) (Kluwer 1991) 239-251.

imposes on you". The government uses a variety of means to provide information to taxpayers. Proposed tax legislation and the government's interpretation and explanation of the legislation are generally set out in several sources. One important source is the Department of Finance explanations of draft and proposed legislation, called either Technical or Explanatory Notes. Other sources include: Notices of Ways and Means Motions that introduce legislation in the House of Commons; Parliamentary Debates and committee hearings and reports; White Papers on tax reform; and press releases of the Department of Finance. Materials published in these sources are stated to be for information purposes only, rather than official interpretations of legislation, but, in practice, these materials, especially the Technical or Explanatory Notes, offer significant insight to the intended operation of the legislation. Revenue Canada has issued interpretation bulletins, information circulars, advance income tax rulings, and pamphlets and booklets in respect of various aspects of the tax system.⁴¹ Such publications allow taxpayers the opportunity to plan transactions, if not with complete comfort, then with a reasonable expectation of how Revenue Canada will treat the transaction. They can also be an important factor in interpreting ambiguous provisions of the Act.⁴²

Right to Fair Treatment

If "fairness" is understood to include both procedural fairness and substantive fairness, the jurisprudence appears to have established that Revenue Canada is not bound by either procedural fairness or substantive fairness in making assessments.⁴³ Revenue Canada must make assessment pursuant to the provisions of the Act and has no discretion whatever as to the way in which it applies the Act.

⁴¹ Interpretation bulletins provide Revenue Canada's interpretation of the law and announce significant changes in the interpretation. Information circulars, on the other hand, are designed to inform the general public regarding procedural matters relating to the Act. Information circulars and interpretation bulletins provide a valuable source of information concerning Revenue Canada's practices and have enormous importance for tax planning.

⁴² See, in general, Sherbaniuk DJ, "Advance Rulings, Technical Interpretation and Interpretation Bulletins," *1976 Corporate Management Tax Conference Report* (Canadian Tax Foundation 1977) 86-106. See also discussions below in "Estoppel".

⁴³ See Hopkins NE, "Fair Play in the Tax System: An Analysis of Les Enterprise Ludco Ltee", *The Report of Proceedings of the Forty-Sixth Tax Conference, 1994 Conference Report* (Canadian Tax Foundation 1995) 2: 126-141 at 2:137.

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According to the Federal Court of Appeal in *Ludmer*, it is impossible to judge Revenue Canada's conduct by "varying and flexible criteria such as those dictated by the principles of natural justice".⁴⁴ In other words, in determining whether or not the decisions made by Revenue Canada are valid, one does not ask whether it has exercised its powers correctly or in an abusive fashion, but whether or not it has acted in accordance with the statute by which it is governed. The duty to act fairly applies only where Revenue Canada has discretion, such as under the fairness legislation.⁴⁵

With respect to substantive fairness, the courts have held that: Revenue Canada is not bound by its earlier assessments; there is no unfairness in assessing a taxpayer differently from one year to another; and no estoppel arises against Revenue Canada in relation to the discharge of its statutory responsibilities concerning the assessment of tax in accordance with the provisions of the Act.⁴⁶ Subsection 152(4) of the Act requires the Minister to assess each taxpayer independently each year. Any agreement by Revenue Canada to tax otherwise than in accordance with the Act would be a dereliction of its duty to enforce the Act.⁴⁷ Revenue Canada is not bound by the treatment it gives, or has given, to other taxpayers. The arguments by taxpayers that they had a legitimate expectation to be treated in a way similar to other taxpayers have been rejected by the courts on two grounds.⁴⁸ First, as mentioned above, the Minister must assess each taxpayer pursuant to the Act:

While it is understandable that the plaintiff considers it unfair that Revenue Canada appears to have treated taxpayers in similar circumstances differently, that

⁴⁴ *Ludmer v The Queen* 95 DTC 5311 (FCA) at 5317.

⁴⁵ The courts are reluctant to interfere with the Minister's decision in such cases. See "Civil Penalties and the Fairness Legislation", below.

⁴⁶ *Ludmer*, above n 44; *Admiral Investment Ltd v MNR* 67 DTC 5114; *Gelber v MNR* [1991] 2 CTC 2319; 91 DTC 1030 (TCC); *First Torland Investments Ltd v MNR* 69 DTC 5109; *Waxman Estate v The Queen*, 94 DTC 1216 (TCC); *Cohen v The Queen* [1980] CTC 318; 80 DTC 6250 (FCA); *Labelle v Canada* [1994] 1 CTC 2576, 96 DTC 1115 (TCC).

⁴⁷ *Ludmer*, above n 44.

⁴⁸ See *Sunbeam Corporation (Canada) Limited v The Queen* 62 TDC 7013, in which the taxpayer had been denied the right to calculate its federal sales tax using an extremely advantageous method which the Minister had extended to its competitors. In *Jasper v MNR* (unreported 1984, Court File No T-52-89); *Pattee v The Queen* [1995] 2 CTC 2977, 94 DTC 1774 (TCC); *Ludmer*, above n 44. In *Riddell v The Queen* [1995] 2 CTC 434, 95 DTC 5530 (FCTD), however, the Court held that Revenue Canada was bound to apply the Act in a fair and even-handed manner to the taxpayer.

cannot be the basis for the plaintiff's appeal. The plaintiff is either entitled on a reasonable interpretation of the words of subparagraph 110(1)(f)(iii) of the Income Tax Act, to the social assistance deduction or he is not. I have found that it is clear that he is not.⁴⁹

Second, it is a matter of procedural fairness. If an appellant were allowed to call as witnesses other taxpayers whom the appellant knew or suspected had been treated more favourably in similar circumstances,⁵⁰ Revenue Canada would be in an unfavourable position, since Revenue Canada would be prohibited by s 241 of the Act from presenting opposing evidence that would disclose secret taxpayer information it has in this connection. Depriving Revenue Canada of the right to present contrary arguments would violate one of the fundamental principles of the judicial system.⁵¹

Finally, the equality right in s 15 is of very limited use to taxpayers in challenging Revenue Canada's unequal treatment of taxpayers in similar situations. To invoke s 15, the discrimination or unfairness must be based on sex, race, age and other enumerated or analogous grounds.⁵² Since the differential treatment in the assessment process is generally based on grounds other than any of the enumerated or analogous grounds, taxpayers cannot rely on s 15 in these cases.⁵³

Advance income tax rulings

An advance income tax ruling is a written statement issued by Revenue Canada to a taxpayer as to how it will interpret specific provisions of the law in the context of a definite transaction or transactions that the taxpayer is contemplating.⁵⁴ Such rulings have been issued by Revenue Canada since 1970 and have become an important and necessary part of the administration of the Act. In an average year, Revenue Canada completes about 800 rulings. The advance ruling procedure was intended to:

⁴⁹ *Hokhold v The Queen* [1993] 2 CTC 99 at 106; 93 DTC 5339 at 5344 (TCC).

⁵⁰ In practice, such a witness may be hard to find, especially where Revenue Canada is within the normal assessment period in auditing that person.

⁵¹ *Ludmer*, above n 44.

⁵² *Andrews v Law Society of British Columbia* [1989] 1 SCR 143.

⁵³ See *Hokhold*, above n 49.

⁵⁴ See Read RJL, "The Income Tax Advance Rulings Service", *The Report of Proceedings of the Forty-Fourth Tax Conference*, 1992 Conference Report (Canadian Tax Foundation 1993) 6: 1; Chang J et al, "Private Income Tax Rulings: A Comparative Study", *Tax Notes International*, 27 February 1995, 738-771; Sherbaniuk, above n 42.

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- foster and encourage the self-assessment system;
- contribute to good relations between Revenue Canada and taxpayers;
- provide certainty before transactions are entered into;
- provide more consistency in the application of the law;
- minimize controversy and litigation; and
- achieve a more coordinated system.⁵⁵

The advance ruling system is entirely the creation of Revenue Canada and is essentially discretionary. According to Information Circular IC 70-6R2 (dated 28 September 1990) which sets out Revenue Canada's policy on advance rulings, Revenue Canada considers itself bound by a ruling as long as the law, as constituted at the time the ruling is issued, remains unchanged. Note, however, IC 70-6R2 itself is not law and is not binding. In practice, no advance ruling that has been provided to and acted upon by a taxpayer seems to have ever been repudiated by Revenue Canada. "The system would fall apart if [it] ever did so".⁵⁶

According to IC 70-6R2, a ruling is binding on Revenue Canada unless it is invalid or revoked. A ruling may become invalid if there is a material omission or misrepresentation in the statement of relevant facts or proposed transactions submitted by the taxpayer. A ruling may be revoked where a transaction or series of transactions has not been completed and Revenue Canada decides that a ruling was in error. Generally, the revocation will not take effect retroactively.⁵⁷

A ruling is only valid with respect to the taxpayer who requests it and to whom it is issued.⁵⁸ With respect to the precedential value to third parties, Revenue Canada has issued a clear warning that other

⁵⁵ *Report of the Royal Commission on Taxation*, vol 5 (Queen's Printer 1966), (hereafter the "Carter Report") 138-9. Read, *ibid* at 6:1-2; and Sherbaniuk, above n 42 at 87.

⁵⁶ See Judge Bowman's comments on advance rulings in *Goldstein v The Queen* 95 DTC 1029 at 1034 (TCC).

⁵⁷ Read, above n 54 at 6: 6. If Revenue Canada intends to revoke a ruling, it will give the taxpayer notice and an opportunity to make representations as to why the ruling should not be revoked; IC 70-6R2, para 11.

⁵⁸ However, in certain circumstances rulings can be obtained on behalf of unnamed taxpayers, for example, subscribers to a share issue under a prospectus; IC 70-6R2, para 8.

taxpayers who rely on a published ruling⁵⁹ must exercise caution. A ruling may only be relied on if the facts are identical to those of the transaction in respect of which it was issued and the law on which the ruling was based has not changed.⁶⁰

Estoppel

The complexity of business life and tax legislation requires that taxpayers seek advice before entering into many kinds of transactions. When a taxpayer suffers damage as a result of relying on incorrect advice given by Revenue Canada officials or on an incorrect interpretation of the law as stated in interpretation bulletins and information circulars, the taxpayer often seeks to apply the doctrine of estoppel against the Minister. The Canadian courts have rarely sided with the taxpayer on this issue.

Under Canadian law, estoppel is not merely a rule of evidence; it is a rule of substantive law or a principle of justice and of equity.⁶¹ It applies to both taxpayers and the Crown, where the Crown's representation is in respect of a matter of fact, not opinions of law. The courts have held that estoppel has no role to play where interpretation of the law is involved, because estoppel cannot override the law.⁶² Since interpretation bulletins and information

⁵⁹ From time to time, Revenue Canada publishes selected advance rulings which it considers to be of general interest. Revenue Canada has recently announced that it plans to release all rulings in severed form; see *Tax Topics*, 16 May 1996 at 3.

⁶⁰ IC 70-6R2, para 25; Read, above n 54 at 6: 10.

⁶¹ *Goldstein*, above n 56 at 1034, which cited *Halsbury's Laws of England* (4th ed) Vol 16 at 840 and *Moorgate Mercantile Co Ltd v Twitchings* 1 QB 225 at 241 per Lord Denning.

⁶² In *Goldstein*, above n 56, the Court stated at 1034:

The principle of estoppel binds the Crown, as do other principles of law. Estoppel in pais, as it applies to the Crown, involves representations of fact made by officials of the Crown and relied and acted on by the subject to his or her detriment. The doctrine has no application where a particular interpretation of a statute has been communicated to a subject by an official of the government, relied upon by that subject to his or her detriment and then withdrawn or changed by the government. In such a case a taxpayer sometimes seeks to invoke the doctrine of estoppel. It is inappropriate to do so not because such representations give rise to an estoppel that does not bind the Crown, but rather, because no estoppel can arise where such representations are not in accordance with the law. Although estoppel is now a principle of substantive law it had its origins in the law of evidence and as such relates to

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circulars are not law, but simply Revenue Canada's interpretation of the law, they do not bind the Minister, the taxpayer, or the courts, and are only an important factor in interpreting the Act in the event of doubt as to the meaning of the legislation.⁶³ Therefore, estoppel does not apply against Revenue Canada where it assesses a taxpayer differently from what is stated in an interpretation bulletin or information circular.⁶⁴

Similarly, Revenue Canada is not bound by representations of law by its officials. In *Goldstein v Canada*, the taxpayer relied on communications with Revenue Canada and filed his 1990 and 1991 returns on the premise that certain losses sustained by him as a limited partner were not to be taken into account in determining his "earned income" for the purposes of s 146(1)(c) of the Act. In dealing with the taxpayer's argument that Revenue Canada was estopped from changing its interpretation of the provision, the Court stated:

The question of the interpretation of paragraph 146(1)(c) is a matter of law and I must decide it in accordance with the law as I understand it. I cannot avoid that obligation because the Department of National Revenue may previously have adopted an interpretation different from that which it now propounds. The question is not whether the Crown is bound by an earlier interpretation upon which a taxpayer has relied. It is more to the point to say that the courts, who have an obligation to decide cases in accordance with the law, are not bound by representations, opinions or admissions on the law expressed or made by the parties. ... [I]t is not in the interests of justice that the courts should be fettered by erroneous interpretations of the law by departmental officials.⁶⁵

It has also been established that Revenue Canada is not estopped from disallowing in a year expenses it had allowed in previous

representations of fact. It has no role to play where questions of interpretation of the law are involved, because estoppels cannot override the law.

⁶³ See *Harel v Deputy Minister of Revenue (Quebec)* 77 DTC 5438; *Nowegijick v The Queen* [1983] 1 SCR 29 at 37; *Bryden v Canada Employment and Immigration Commission* [1982] 1 SCR 443 at 450; *Matabi Mines Ltd v Ont (Minister of Revenue)* [1988] 2 SCR 175 at 189 and 195; *Vaillancourt v The Queen* 91 DTC 5408 (FCA); *Redclay Holdings Ltd v Canada* [1996] TCJ No 126 (TCC).

⁶⁴ See *Woon v MNR* 50 DTC 871; *Maritime Electric Co v General Dairies Ltd* AC 601; *MNR v Inland Industries Ltd* 72 DTC 6013; *Stickel v MNR* 72 DTC 6178; *Granger v EEIC* 3 FC 70; *Custom Glass Ltd v MNR* 67 DTC 5207.

⁶⁵ *Goldstein*, above n 56 at 1034.

years, or from assessing a taxpayer for withholding tax which it did not assess in previous years.⁶⁶ Nor is Revenue Canada bound by any undertaking or agreement with a taxpayer, because an agreement whereby Revenue Canada would agree to assess tax otherwise than in accordance with the Act would be an illegal agreement.⁶⁷ In *Taylor v The Queen*,⁶⁸ the taxpayer had misappropriated approximately \$500,000. After confessing to the police authorities, he was told by Revenue Canada officials that, if he made restitution, there would be a "wash"⁶⁹ and he would not be assessed for taxes, interest and penalties in respect of the misappropriation. Armed with what he believed to be Revenue Canada's undertaking, the taxpayer made restitution. Contrary to Revenue Canada's representation and while the taxpayer was serving a jail sentence for the theft, Revenue Canada assessed him for additional income that resulted from the misappropriation. The taxpayer appealed to the Tax Court of Canada alleging, inter alia, that the Minister was estopped from assessing interest and penalties. The Court concluded that, despite Revenue Canada's representation, the taxpayer's reliance, and the obvious detriment to the taxpayer, Revenue Canada was not estopped from assessing the taxpayer. The representation was not a statement of fact, but an opinion of law. Since the taxpayer had failed, knowingly, to report the misappropriated amounts as income, he had become liable for tax, penalties and interest on unpaid taxes, and the Minister could not "contract out" of the provisions of the Act by promising to forgo an assessment which was required by the Act.

Although, in theory, estoppel applies to both taxpayers and Revenue Canada, the nature of income tax cases is such that representations made by the taxpayer will almost always be in respect of a matter of fact, whereas representations made by Revenue Canada will usually be opinions as to the applicability of a statutory provision. The law of estoppel, therefore, will often operate to bind the taxpayer,⁷⁰ but not Revenue Canada.⁷¹ Where a

⁶⁶ See *Ludmer*, above n 44; *Vivian v The Queen* 95 DTC 664 (TCC).

⁶⁷ Similar decisions were reached in *Cohen*, above n 46; *Gibbon v The Queen* 77 DTC 5193 (TCC).

⁶⁸ 95 DTC 591 (TCC).

⁶⁹ *Ibid* at 594.

⁷⁰ For example, in *Hnatiuk v The Queen* [1976] CTC 632 (FCTD), the taxpayer was estopped by his original representation where Revenue Canada argued that the taxpayer had reported in his return that the partnership income was distributed in a particular way and it had relied on that representation in assessing the partners for the several years in issue.

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taxpayer has relied to her or his detriment on representations made by Revenue Canada, given that the doctrine of estoppel cannot be used, the taxpayer could challenge Revenue Canada for abuse of process or, alternatively, seek damages in a tort action against Revenue Canada. Neither of these options has proven successful.⁷² For example, in *Stecko v The Queen*,⁷³ the taxpayer alleged, inter alia, that an official of Revenue Canada had stated in a meeting with him that certain costs were deductible as current expenses and the same official selected him for an audit which resulted in the recharacterisation of the costs as capital expenditures. The taxpayer argued that Revenue Canada should be estopped from reassessing him because of an abuse of process. Cullen J of the Tax Court of Canada was troubled by the way in which the Revenue Canada official's presence seemed to hover over matters concerning the taxpayer, but he would not go so far as to say that there was anything sinister about his involvement or that he had in some way abused his power:

An action which is an abuse of process is, in my mind, frivolous, vexatious, or malicious. Although the assessments and subsequent judicial processes have surely proved time-consuming and onerous for the plaintiff, they are nothing more than an enforcement of the Income Tax Act.⁷⁴

⁷¹ As an aberration, in *R v Langille* [1977] CTC 144, the Federal Court - Trial Division held that Revenue Canada was estopped by the representation made by the Department of Labour on the basis that statement by the Department of Labour official was not an opinion of law but a statement of fact descriptive of the type of contract being offered to the taxpayer. In this case, the taxpayer purchased a Canadian government annuity. At the time he purchased it, the saleslady (an employee of the Department of Labor) told him that if he did not deduct the premium from his income, as he was entitled to do under the law at that time, he would not have to pay tax on the capital element of the annuity payments he received, but only on the interest component of those payments. If, on the other hand, he did deduct the premium, then he would be taxable on the full amount of the annuity payment. The taxpayer acted on this advice and elected not to deduct the premium and included only the interest element components of the payments he received. He was reassessed by Revenue Canada on the basis that the total amount of the annuity was taxable.

⁷² See Dickerson RWV, "Estoppel and the Crown", *The Report of Proceedings of the Twenty-Ninth Tax Conference*, 1977 Conference Report (Canadian Tax Foundation 1978) 668-673 at 672-673; Editorial note; "Does the taxpayer have any remedy when Revenue Canada breaks its word"? 95 *Dominion Tax Cases*, Report 16 at 10.

⁷³ 95 DTC 5215 (FCTD).

⁷⁴ *Ibid* at 5219.

There have been no cases in Canada in which a taxpayer has been successful in a tort action against Revenue Canada. It seems unlikely that a taxpayer could recover damages against Revenue Canada, in the absence of evidence of malice on the part of Revenue Canada officials.

C Audit and investigation

Sections 231 through 231.6 of the Act provide the Minister with the powers to:

- audit and inspect books and records kept by a taxpayer (s 231.1);
- demand information from a taxpayer or third parties (s 231.2);
- search premises for evidence and seize the evidence (s 231.3);
- authorize an inquiry (s 231.4); and
- demand foreign-based information (s 231.6).

The right of taxpayers to privacy is guaranteed by s 8 of the Charter. It is protected by restricting the audit and investigative powers of Revenue Canada. Sections 231 to 231.6 have undergone several major changes, each of which has resulted in more protection of the right to privacy. The most recent changes were in response to the enactment of the Charter. For example, when the search and seizure powers (now contained in s 231.3) were first introduced in 1948, they only required the Minister to believe that the desired search and seizure were necessary for any purpose related to the administration and enforcement of the Act. In 1972, the Act introduced a requirement of reasonable and probable cause and a requirement that an application to the court for a search warrant be supported by evidence under oath.⁷⁵ The former s 231(4) was held by the courts to violate s 8 of the Charter and was, therefore, invalid.⁷⁶ According to the Supreme Court of Canada, in order to satisfy s 8 of the Charter, prior judicial authorization must be obtained and the evidence presented by the Minister in applying for the authorization must establish that the Minister has reasonable grounds to believe:

- that an offence under the Act has been committed;

⁷⁵ SC 1970-71-72, c 63. This was derived from s 126(3) of the Income Tax Act, RSC 1952, c 148.

⁷⁶ See, for example, *MNR v Kruger Inc* [1984] CTC 506, 84 DTC 6478 (FCA).

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- that a document or thing that may afford evidence of the offence is likely to be found; and
- that the building, receptacle or place specified in the application is likely to contain such a document or thing.

These last two requirements were included in a 1986 amendment and are now contained in paragraphs 231.3(3)(b) and (c). Although drafted with the requirements of the Charter in mind, the 1986 amendment to s 231.3 was subsequently found to be inadequate.⁷⁷ The principal defect was its requirement that the judge must issue the warrant applied for by the Minister, depriving the judge of ultimate discretion as to whether the circumstances justified the invasion of privacy occasioned by the search and seizure. It was held that the exercise of judicial discretion in deciding whether to grant a search warrant was fundamental to the scheme of prior authorization required by s 8 of the Charter.⁷⁸ Subsection 231.3(3) was amended in 1994 to allow this discretion.

In determining whether a taxpayer's right to privacy is violated by the Minister's investigative powers, the courts consider whether the place being searched is a personal residence or business premise and whether the investigative power is "administrative" or criminal or quasi-criminal.⁷⁹ In general, the courts have held that the expectation of privacy in relation to business records in a self-assessment tax system is relatively low⁸⁰ and that the expectation of privacy with respect to a personal residence may be much greater than that in respect of business premises. The greater the intrusion, the higher safeguards will be required. Therefore, entry into a personal residence for audit purposes requires a warrant, but entry into business premises does not. The exercise of "criminal" investigative powers under s 231.3 requires a search warrant, whereas the exercise of administrative powers under ss 231.1, 231.2 and 231.6 does not normally require such a warrant.⁸¹

⁷⁷ In *Baron v Canada* [1993] 1 CTC 111, 93 DTC 5018 (SCC), the Supreme Court of Canada found s 231.3 to be unconstitutional by virtue of s 8 of the Charter and invalid in its entirety.

⁷⁸ *Ibid.*

⁷⁹ The finding that a search is reasonable or unreasonable based on the distinction between quasi-criminal and regulatory provisions was criticised for being artificial and difficult to apply. The penalties for non-compliance with both types of provisions are similar in many cases (see below). See *Butler*, above n at 29:8-9.

⁸⁰ See, for example, *McKinlay Transport*, above n 2.

⁸¹ An easing of Charter standards where the primary purpose of a search is simply to ensure that taxes are paid as and when due may be justified by the

Audit

Revenue Canada's audit and inspection powers are provided under s 231.1(1) of the Act: any person authorized by the Minister, for any purpose related to the administration or enforcement of the Act, may at all reasonable times enter business premises without a warrant and require the owner or manager of the premises to provide "all reasonable assistance" and answer "all proper questions".⁸² A small number of returns is selected for audit each year.⁸³ Revenue Canada's audit program is directed mainly at those categories of taxpayer who are more likely to have under-reported their income and large corporations.⁸⁴ Although there is no legal requirement for Revenue Canada to provide reasons for an audit, Revenue Canada's policy is to provide the taxpayer with an audit plan and to keep the taxpayer informed at all times of the progress of the audit.⁸⁵

A taxpayer's right to privacy is protected only where the premise or place of business to be entered for audit purposes is a dwelling house. In such a case, the auditor may not enter without the occupant's consent, unless a warrant has been issued by a judge.⁸⁶ The Minister's

requirement of a self-reporting and self-assessment income tax system. Where in the case of s 231.1, however, whose stated aim is the discovery and preservation of evidence for the purpose of a criminal proceeding, nothing less than the full panoply of Charter protection is appropriate. See *Baron*, above n 77. The powers under sections 231.1, 231.2 and 231.6 are considered administrative because they relate to the manner in which income tax is calculated and collected and their purpose is not to penalise criminal conduct but to enforce compliance with the Act.

⁸² Section 238(1) makes it an offence to fail to comply with s 231.1.

⁸³ About 1% of individual returns and 5% of corporate returns are audited each year; See Li J, "Withholding Tax on Domestic Interest and Dividends" (1995) 43 *Canadian Tax Journal* 553 at 586.

⁸⁴ Taxpayers whose income is not subject to source deduction, for example, self-employed individuals, corporations and trusts, are such taxpayers. Wage and salary earners, who comprise about 80% of the taxpaying population, are rarely audited; their taxes are deducted at source.

⁸⁵ The role, policy and practices of the tax audit are described in detail in Information Circular 71-14R3 of 18 June 1984. See also Ledoux G, "Tax Audits" *Report of Proceedings of the Forty-Fifth Tax Conference*, 1993 Conference Report (Canadian Tax Foundation 1994) 12:1-9; Brown RD, "Revenue Canada's New View of Tax Avoidance Activities" *Report of Proceedings of the Forty-Fourth Tax Conference*, 1992 Conference Report (Canadian Tax Foundation 1993) 5: 2-7.

⁸⁶ Section 231.3 was introduced in response to court decisions in *The Queen v Print Three Inc* [1985] 2 CTC 48, 85 DTC 5303 (Ont CA); and *Kruger*, above n 76. Before the amendment in 1994, s 231.1(3) was mandatory in

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application for a warrant must be supported by affidavit evidence that there are reasonable grounds to believe that the house is a place where relevant books and records are kept, and that entry into the house is necessary and has been or likely will be refused. If the judge is not satisfied that entry is necessary, he or she may order an occupant to provide an auditor reasonable access to any document or property or may make any other appropriate order.

Demand for information

Subsection 231.2(1) permits the Minister to demand any information or documents from any person (the taxpayer or any third party) for any purpose related to the administration or enforcement of the Act. This can be done by notice served personally, or by registered or certified mail. The notice must provide reasonable time for the production of the documents or information. Subsection 231.2(1) is frequently used by the Minister when investigating tax evasion or tax avoidance schemes; it gives the auditor access to the records of all parties involved in a transaction, including banks, lawyers (subject to solicitor-client privilege discussed below), and other third parties.⁸⁷

The issue of whether the former s 231(3) (which is substantially the same as s 231.2(1)) violated the right to privacy provided under s 8 of the Charter was considered by the Supreme Court of Canada in *McKinlay Transport Ltd v The Queen*.⁸⁸ In that case, the Court found that a demand for information under former s 231(3) constituted a seizure in the sense that it infringed on the recipient's right to privacy, but that such seizure was not unreasonable since a lesser degree of privacy was to be expected in matters relating to the Act. According to the Court, because the Act was based upon a system of self assessment, in supervising this regulatory scheme Revenue Canada must be given broad powers to audit taxpayers' returns and inspect all records that may be relevant to the preparation of these returns. Wilson J stated:

nature and required the judge to issue the warrant providing the supporting evidence was satisfactory. For the reasons discussed above in the discussion of search warrants, and in light of the *Baron* case, above n 77, s 231.1(3) was amended to allow the judge complete discretion in issuing the warrant.

⁸⁷ Under s 231.2, the Minister also has the power to demand information in respect of information sought by the foreign competent authority under the exchange of information provision of a tax treaty. See, for example, *Montreal Aluminum Processing Limited v AG of Can* 92 DTC 6567 (FCA).

⁸⁸ *McKinlay Transport*, above n 2.

In my opinion, subsection 231(3) provides the least intrusive means by which effective monitoring of compliance with the *Income Tax Act* can be effected. It involves no invasion of a taxpayer's home or business premises. It simply calls for the production of records which may be relevant to the filing of an income tax return. A taxpayer's privacy interest with regard to these documents *vis-à-vis* the Minister is relatively low. The Minister has no way of knowing whether certain records are relevant until he has had an opportunity to examine them. At the same time, the taxpayer's privacy interest is protected as much as possible since section 241 of the Act protects the taxpayer from disclosure of his records or the information contained therein to other persons or agencies.⁸⁹

Although s 231.2(1) has been held to be constitutional,⁹⁰ the intrusion into the privacy of a taxpayer by this broad provision is not unlimited.⁹¹ The Supreme Court of Canada, in *James Richardson and Sons Ltd v MNR*,⁹² held that the Minister could use s 231.2(1) to obtain information relevant to the tax liability of a specific person (or persons) only if the tax liability of such person (or persons) was the subject of a genuine and serious inquiry. Subsection 231.2(2) prohibits the Minister from demanding information or documents from third parties relating to "one or more unnamed persons", unless

⁸⁹ *McKinlay Transport*, above n 2 at 114 and 6251.

⁹⁰ Section 231.2(1) has been held constitutional in two recent cases: *Morena v The Queen* [1991] 1 CTC 78; 90 DTC 6685 (FCTD); *Djokich v Canada* 96 DTC 6214 (FCTD).

⁹¹ The courts have held that the former s 231(3) should not be construed as broadly as the language may suggest. Wilson J stated in *McKinlay Transport*, above n 2, that *Bank of Commerce v Attorney General of Canada* 62 DTC 1236 (SCC) establishes that: "(a) the test of whether the Minister is acting for a purpose specified in the act is an objective one and has to be decided on the proper interpretation of the subsection and its application to the circumstances disclosed; (b) the obtaining of information relevant to the tax liability of some specific person or persons whose liability to tax is under investigation is a purpose related to the administration or enforcement of the Act; (c) it is not necessary that the person from whom the information is sought be one whose liability to tax is under investigation; (d) the fact that the giving of the information may disclose private transactions involving persons who are not under investigation and may not be liable to tax does not invalidate the Requirement". Such reasoning was endorsed in subsequent cases, such as *James Richardson & Sons Ltd v MNR* [1982] CTC 239, 82 DTC 6204 (FCA), reversed on other grounds [1984] CTC 345, 84 DTC 6325 (SCC); *MNR v Sand Exploration Ltd* [1995] 2 CTC 140, 95 DTC 5358 (FCTD); *The Queen v Duncan* [1992] 2 CTC 360, 91 DTC 5615 (FCTD).

⁹² *James Richardson*, *ibid*.

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the Minister first obtains a judicial authorization under s 231.2(3).⁹³ The rationale for this provision is to prevent an overly intrusive "fishing expedition" by the Minister and to place an obligation on the Minister to act in the utmost good faith.⁹⁴

Demand for foreign-based information

Section 231.6 of the Act gives Revenue Canada "strong, comprehensive and far-reaching powers"⁹⁵ to secure foreign-based information or documents. Under this provision, the Minister has the power to compel a person resident in Canada, or a nonresident carrying on business in Canada, to produce any "foreign-based information or document". "Foreign-based information or document" is defined as any information or document available or located outside Canada which may be relevant to the administration or enforcement of the Act. The Minister's demand for information under s 231.6 is not limited to a demand for information issued in the course of assessing or reassessing the taxpayer.

A taxpayer is protected from the abusive use of this power through judicial review of the Minister's requirement. The onus is on the taxpayer to show that a demand is unreasonable.⁹⁶ Non-compliance with a demand under s 231.6 is subject to an evidentiary sanction under s 231.6(8). On a motion by the Minister, the information or document covered by the notice is inadmissible in any civil proceeding relating to the administration or enforcement of the Act. The purpose of this sanction is to prevent a person from selectively providing information or documents that are favorable to him or her, while refusing to provide information or documents that could assist the Minister.

⁹³ Section 231.2(3) provides for an ex parte application by the minister for authorization supported by affidavit evidence that: a) the person or group must be ascertainable; b) the requirement must be made to verify compliance by the person or persons in the group with any duty or obligation under the Act; c) it is reasonable to expect that the person or any person in the group may have failed or may be likely to fail to provide information that is sought in the requirement or otherwise to comply with the Act; and d) the information or document is not otherwise more readily available.

⁹⁴ *Sand Exploration*, above n 91.

⁹⁵ *Merko v MNR* [1990] 2 CTC 518 at 522; 90 DTC 6643 at 6647 (FCTD).

⁹⁶ *Ibid.*

Search and seizure

A taxpayer's right to privacy and the Minister's interest in ensuring compliance with the Act are balanced by the requirement of a search warrant under s 231.3. As discussed earlier, s 231.3 has been amended in response to various Charter challenges of the former s 231(1)(d), which permitted an auditor to seize any documents or other things found during an audit, and former s 231(4), which allowed the Minister to give an authorization to search and seize on approval by a judge. At present, the search and seizure powers under s 231.3 of the Act are more in line with the traditional criminal law search powers and s 489 of the Criminal Code and are less likely to be attacked under s 8 of the Charter.⁹⁷

Under s 231.3, the Minister, in order to obtain a search warrant, must make an ex parte application supported by information given on oath establishing the facts on which the application is based. The judge has the discretion to issue a warrant, if he or she is satisfied that there are reasonable grounds to believe that: an offence under the Act has been committed; a document or thing that may afford evidence of the offence is likely to be found; and the place specified in the application is likely to contain the document or thing. The warrant must be in writing and may authorize any person named in it to enter and search a place for any document or thing relating to the offence in question. The warrant must contain a reference to the offence for which it is issued; identify the building, receptacle or place to be searched; identify the person alleged to have committed the offence; and be reasonably specific as to any document or thing sought.⁹⁸ The person who executes the warrant may seize additional documents or things that are evidence of an offence under the Act.⁹⁹ When anything is seized it must be brought, as soon as practically possible, before the court, or a report in respect of the thing must be made to the court.¹⁰⁰

⁹⁷ Innes W, *Tax Evasion in Canada* (Carswell 1955) at 8-8.

⁹⁸ Section 231.3(4). There was no counterpart to this provision in the former s 231(4).

⁹⁹ Section 231.3(5) of the Act. The constitutionality of this provision has been upheld by the Federal Court of Appeal in *Solvent Petroleum Extraction Inc v MNR* [1989] 2 CTC 177, 89 DTC 5381, leave to appeal to SCC refused (1994) 171 NR 224 (note) (SCC).

¹⁰⁰ According to s 231.3(4), the warrant must refer to the specific offence in respect of which it is issued, identify the place to be searched and the person alleged to have committed the offence, and be reasonably specific as to the document or thing to be searched for and seized.

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Solicitor-client privilege

In the face of the extensive investigative and search and seizure powers, a lawyer has the right to claim solicitor-client privilege under s 232 of the Act, which deals with questions of solicitor-client privilege in respect of documents seized from the office of a lawyer pursuant to s 231.3 of the Act, or required of a lawyer pursuant to s 231.1 or s 231.2 of the Act. Section 232 does not necessarily deal with the question of documents found in the possession of a client or a third party, such as an accountant; these questions are governed by the common law.

"Solicitor-client privilege" is defined as "the right, if any, that a person has in a superior court in the province where the matter arises to refuse to disclose an oral or documentary communication on the ground that the communication is one passing between the person and the person's lawyer in professional confidence".¹⁰¹ The definition continues to specifically exclude accounting records, including supporting vouchers and cheques from the privilege.¹⁰² Solicitor-client privilege protects the solicitor's working papers (including drafts of documents and letters, notes, and internal memoranda, provided that they are produced during the formulation of legal advice to be given to the client), draft agreements, reorganization plans, and letters between client and solicitor relating to disputes or other legal issues.¹⁰³

Unless otherwise instructed by their clients, lawyers¹⁰⁴ have a responsibility to claim solicitor-client privilege with respect to

¹⁰¹ Section 232(1)(e) of the Act.

¹⁰² The statutory definition is co-extensive with the scope of privilege established in the case law, with the limited exception of a solicitor's accounting records being made specifically exempt from privilege. See *Re Kask* [1966] CTC 659; 66 DTC 5374 (BC SC); *Susuan Hosiery Ltd v MNR* [1969] CTC 353 at 359, 69 DTC 5278 (Exch Ct); *Re Sokolov* [1968] CTC 414, 68 DTC 5266 (Man QB); *Southern Railway of British Columbia Ltd v Canada* [1991] 1 CTC 432, 91 DTC 5081 (BSSC); *Zein v Canada* [1991] 1 CTC 413, 91 DTC 5052 (BCSC); *Gregory v Canada* [1992] 2 CTC 250, 92 DTC 6518 (FCTD).

¹⁰³ See *Re Kask*, *ibid*; *Re Sokolov*, *ibid*; *Brunner and Lay (Canada) Ltd v Deputy A-G of Canada* [1984] CTC 534.

¹⁰⁴ A lawyer means, in the Province of Quebec, an advocate, lawyer or notary, and in any other province of Canada, a barrister or solicitor: s 232(1)(c). A lawyer has a duty, where it is honestly believed that the right of privilege exists, to ensure that the right of privilege is not waived, or is not deemed to be waived, without first going through the procedure of

communications between them and the client. Section 232 provides a comprehensive procedure for the determination of claims of privilege in respect of documents required to be produced pursuant to s 231.2, or documents to be audited, examined or seized pursuant to s 231.1 and s 231.3.¹⁰⁵ Revenue Canada officers are prohibited from inspecting, examining, or seizing a document in the possession of a lawyer without providing the lawyer with a reasonable opportunity to claim privilege under s 232.¹⁰⁶ Where a lawyer is prosecuted for failure to comply with the Minister's requirement to provide information or to produce a document, the lawyer will be acquitted if it is established that:

- he or she had reasonable grounds to believe that the information or document in question was the subject of solicitor-client privilege; and
- the lawyer communicated to the Minister or some other person duly authorized by the Minister his or her refusal to comply with the requirement, together with a claim for solicitor-client privilege on behalf of a named client.

Such defence is available to a lawyer only when he or she is required to provide information under s 231.2, not in the case of an actual seizure under s 231.3.

Communications between accountants and their clients are not privileged under either s 232 of the Act or common law. The rationale for the absence of such a privilege seems to be that, unlike the solicitor-client privilege, the accountant-client privilege "is not founded upon a need to ensure an effective system of the administration of justice",¹⁰⁷ which is the basis for the solicitor-client privilege. However, it has been held that when an accountant is engaged by solicitors to obtain facts from a client, communications between the accountant and the client will be considered as communications between the solicitor and the client, and would be privileged.¹⁰⁸ Similarly, where an accountant acts as agent for the client, communications that are requested by the client and have

asking a court to clear the lawyer from such privilege. See *Lagasse v Canada* [1961] CTC 105, 61 DTC 1025 (Que Sup Ct).

¹⁰⁵ Section 232(3), (3.1), (4) of the Act.

¹⁰⁶ Section 232(12) of the Act.

¹⁰⁷ See *Baron v Canada* [1990] 1 CTC 84, 90 DTC 6040 (FCTD), reversed on other grounds, above n 77.

¹⁰⁸ *Susan Hosiery*, above n 102.

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come into existence for the purposes of obtaining legal advice can also be privileged.¹⁰⁹

At common law, the solicitor-client privilege is lost if the Minister can establish a prima facie case of fraud. A prima facie case of fraud must be based on a reasonable inference from documentary evidence; a mere pleading or allegation of fraud is not sufficient.¹¹⁰ The solicitor-client privilege is also lost where the privileged information has been disclosed to a third party. For the privilege to be lost, however, the disclosure must be deliberate and not inadvertent, or with the consent of the client. In *Cineplex Odeon Corp v Canada*,¹¹¹ the taxpayer's accountants, who were also its external auditors, had a tax accounting team and an audit team. The tax accounting team possessed documents, as the taxpayer's agent, for the purpose of obtaining legal advice. The documents were therefore privileged. In the ordinary course of business, the documents were provided to the audit team in connection with the external audit. The Court found that, although the audit team was required to act independently of the client and was therefore to be considered as a third party, the disclosure was made without regard to the client's privilege and without the client's knowledge of it, and was therefore inadvertent.

Right against self-incrimination

Section 11 of the Charter provides that: "[a]ny person charged with an offence has the right(c) not to be compelled to be a witness in proceedings against that person in respect of the offence". It has been accepted by the courts that s 11(c) affords protection against testimonial compulsion to an accused charged with an offence.¹¹² Where a taxpayer is required by the Minister under s 231.2(1) to furnish information in the course of a tax audit, since there is no offence at issue in such audit, there is no violation of s 11(c).¹¹³

¹⁰⁹ See *Cineplex Odeon Corp v Canada* [1994] 2 CTC 293, 94 DTC 6407 (Ont Gen Div).

¹¹⁰ See *Goodman & Carr v MNR* [1968] CTC 484, 68 DTC 5310 (Ont HC), *Edmonds v Canada* [1980] CTC 192, 80 DTC 6201 (Que SC), and *MNR v Canadian Bio-Mass Research Inc* [1989] 1 CTC 289, 89 DTC 5123 (FCTD).

¹¹¹ Above n 109.

¹¹² See *Thomson Newspapers Ltd v Canada* [1990] 1 SCR 425 (SCC) per Wilson J at 481 and Sopinka J at 601.

¹¹³ In *Tyler v MNR* [1991] 1 CTC 13, 91 DTC 5022, the applicant sought an order in Federal Court - Trial Division quashing requirements made by the Minister during the course of a criminal prosecution of the applicant, for narcotics violations. The trial judge refused the application and found,

D Collection of taxes

Income taxes are collected through withholding at source (principally wages and salaries and payments to non-residents) or instalment payments.¹¹⁴ The amount of taxes deducted at source from payments of wages and salaries and the instalment payments are credited to the taxpayer's account and a final estimate of tax payable is made in the tax return for the year. Where a taxpayer is assessed for unpaid taxes, interest and penalties, the taxpayer must make a payment forthwith upon mailing of a notice of assessment.¹¹⁵

Any taxes, interest, penalties and other amounts payable under the Act are debts due to Her Majesty and recoverable as such in court or in any other manner provided by the Act.¹¹⁶ If a taxpayer is unable to pay an amount assessed, the Minister may accept security for payment, or consider some compromises, such as the waiver of a penalty or interest under the fairness legislation, the modification of an existing reassessment or, in some cases, the application for a remission order under the Financial Administration Act.¹¹⁷ If payment is not made and no agreement is reached as to payment terms or compromise of the liability, subject to some restrictions, Revenue Canada can take collection actions. The Minister can certify that all or part of an amount payable has not been paid and register a certificate in the Federal Court of Canada.¹¹⁸ When registered, the certificate has the same force and effect as a judgment against a debtor in the amount specified in the certificate plus interest. The Minister may then pursue all available methods under the Act to enforce the judgment. Sections 223, 224 and 225 contain specific

inter alia, that the applicant's rights under s 11(c) of the Charter were not infringed. This reasoning was upheld by the Federal Court of Appeal. For a similar decision, see *Morena*, above n 90.

¹¹⁴ See Li, above n 83.

¹¹⁵ Section 158 of the Act.

¹¹⁶ Section 222 of the Act.

¹¹⁷ In certain circumstances, relief is available under the Financial Administration Act. For example, in *Dorso Optics Limited v MNR* 92 DTC 2132, the Tax Court of Canada found that the taxpayers were led by the Minister's previous assessment practice (1972-1977) to believe that they were not liable for withholding taxes on certain payments to a nonresident of Canada. Although the Minister was not bound by that practice, the Court recommended the Minister to consider recommending to the Governor in Council, pursuant to s 23(2) of the Financial Administration Act, that the amount of interest assessed in 1983 on the amounts the taxpayers had failed to withhold and remit be remitted to the taxpayers.

¹¹⁸ Section 223(2) of the Act.

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provisions permitting the Minister to enforce payment of taxes by means of garnishment and seizure of chattels and other property.

The Minister's ability to take collection proceedings is restricted by s 225.1: collection actions cannot be taken within the 90-day period after the day of mailing of the notice of assessment where the taxpayer uses the appeal procedures to object to, or appeal from, the assessment. An exception to this restriction is "collection in jeopardy", which applies where there are reasonable grounds to believe that the collection of all or part of the amount assessed would be jeopardized by a delay in collection. Prior judicial authorization is required for collection in such circumstances.¹¹⁹

A taxpayer can challenge the Minister's collection action through an appeal to the Tax Court of Canada or through judicial review at the Federal Court - Trial Division. Where an appeal is taken or is possible, a collection action can only be challenged through an appeal to the Tax Court of Canada in respect of the assessment. The Court may vacate, change or confirm the assessment, but will not award any injunctive or declaratory relief in respect of a collection action of Revenue Canada.¹²⁰ In other cases, a taxpayer could seek declaratory relief at the Federal Court - Trial Division on grounds of negligent conduct on the part of Revenue Canada officials, but the chance of success is minimal. In *City Centre Properties Inc v The Queen*,¹²¹ a bank guarantee was provided by a third party in favour of Revenue Canada guaranteeing payment of taxes owing by a corporation of which the corporate taxpayer was the successor. A Revenue Canada official negligently allowed the guarantee to expire and demanded payment from the taxpayer. The taxpayer contested Revenue Canada's entitlement to recover from them the outstanding taxes and interest and sought declaratory relief. In addition, the taxpayer claimed damages for negligence or breach of fiduciary duty arising out of a Revenue Canada official's conduct. The Federal Court - Trial Division found, inter alia, that: the relationship between Revenue Canada and the taxpayer was simply one of creditor and debtor, not one of fiduciary relationship; the official committed an error in allowing the guarantee to expire without taking action upon it, but such carelessness in the performance of his duty did not constitute negligence at common law

¹¹⁹ Section 225.2 of the Act.

¹²⁰ See *MNR v Parsons* [1984] CTC 354, 84 DTC 6447 (FCA); *Optical Recording Corp v The Queen* [1990] 2 CTC 524, 90 DTC 6647 (FCA); *BRL Biomedical Ltd v The Queen* [1992] 1 CTC 315, 92 DTC 6355 (FCTD).

¹²¹ 94 DTC 6209 (FCTD).

because he owed no duty to the taxpayer to enforce the guarantee. The Court did not award declaratory relief or damages, although it did express sympathy for the taxpayer's unfortunate position.

Declaratory relief may be awarded to a taxpayer in extreme cases where "objectively demonstrated failures or thoughtlessness on the public servants' part have so added to the suffering and pressure of his plight such that he has resorted like a wounded, cornered animal to calling them liars and other pejorative names".¹²² In *McPhail v The Queen*,¹²³ the taxpayer and Revenue Canada officials agreed on a proposal for payment of tax owing by the taxpayer and his corporation in monthly instalments. Revenue Canada subsequently effected various collection measures in contravention of such agreement and obtained judgment and a writ of fieri facias. The taxpayer moved to quash the writ. The motion was granted by the Court with the additional requirement that, while any money garnished or attached thereunder could be retained by Revenue Canada, no real or personal property of the taxpayer was to be sold thereunder. The Court also ordered that no new writ be issued until a further meeting (or meetings) had taken place between the taxpayer and Revenue Canada with a view to establishing an orderly and reasonable schedule for the taxpayer's payment of the tax arrears.

E Penalties

Civil penalties and the fairness legislation

Civil penalties are imposed under s 162 and s 163 of the Act for a variety of delinquent acts and omissions, such as the late filing of a tax return, the failure to file a return, the repeated failure to file a return, the failure to provide information in a prescribed form, the failure to report an item of income, and the making of a false statement or omission in a return. The penalties vary depending on the nature of the offence and whether it is a repeated offence. For example, the failure to file a return is subject to a penalty equal to 5% of the unpaid tax plus 1% of the unpaid tax per month (not exceeding 12 months) until the return is actually filed.¹²⁴ For repeated failures, these penalties increase to 10% and 2% per month (not exceeding 20 months), respectively. The penalty for false

¹²² *McPhail v The Queen* [1994] 1 CTC 259, 94 DTC 6198 (FCTD).

¹²³ *Ibid.*

¹²⁴ Section 162(1) of the Act.

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statements or omissions is the greater of \$100 and 50% of the amount of tax avoided because of the false statement.¹²⁵

In addition to penalties, s 161 of the Act provides that interest is payable at the prescribed rate on late or deficient payments of tax. The prescribed rate is the government of Canada Treasury-bill rate plus 4%.¹²⁶

Interest and penalties may be waived or cancelled by the Minister under the fairness legislation enacted in 1991.¹²⁷ The objective of the legislation was, in the words of the Minister, to "allow for common sense in dealing with taxpayers who, because of personal misfortune or circumstances beyond their control, are unable to meet our deadlines or comply with our rules".¹²⁸ According to Revenue Canada's guidelines,¹²⁹ applications for waiver or cancellation of interest and penalties may be granted under s 220(3.1) in the following circumstances:

- extraordinary circumstances beyond the taxpayer's control, such as natural or human disasters, civil disturbances or disruptions in services, a serious illness or accident, or serious emotional or mental distress which have prevented compliance with the Act;
- failures of Revenue Canada, such as processing delays, errors in material provided to the public, incorrect advice from Revenue Canada, errors in processing or delays in providing information; and
- situations where the taxpayer is unable to pay the amounts of interest or penalties owing.

¹²⁵ Section 163(2) of the Act.

¹²⁶ The prescribed rate of interest for the purposes of the Act is set out in Part XLIII of the Regulations and is determined in respect of each calendar quarter.

¹²⁷ See Part V below.

¹²⁸ See Revenue Canada, Taxation, "Jelinek Details Fairness legislation for Taxpayers" *Release* 24 May 1991.

¹²⁹ They are set out in Information Circular 92-2 dated 18 March 1992. Two other information circulars were issued in respect of other aspects of the Fairness legislation: Information Circular 92-1, "Guidelines for Accepting Late, Amended or Revoked Elections" 18 March 1992; Information Circular 92-93, "Guidelines for Refunds Beyond the Normal Three Year Period", 18 March 1992.

Application for waiver or cancellation of interest and penalties are made to the District Taxation Office in writing and are considered by a separate Fairness Committee within the District Taxation Office.

Under s 220(3.1), the Minister has complete discretion in considering a taxpayer's application. In exercising the discretion, the Minister is subject to a common law duty to act fairly, that is "a duty to observe the rudiments of natural justice in the exercise of administrative functions".¹³⁰ In a number of cases, taxpayers have sought judicial review of the Minister's rejection of requests for the cancellation or waiver of interest and penalties, but none has had any success.¹³¹ "Absent bad faith on the part of the Minister, a breach of the principles of natural justice or consideration of extraneous or irrelevant factors, there is nothing to warrant the Court's interference with the exercise of his discretion".¹³² According to these cases, where the taxpayer is afforded the full opportunity to make representations to the Fairness Committee, is made aware of the factors which the Fairness Committee will consider, and is given the right to have an unfavourable decision of the Fairness Committee reviewed by the Director of the District Taxation Office, the requirements of procedural fairness are satisfied.¹³³ Even if the Court, on judicial review, finds that the Minister has erred by failing to provide procedural fairness, it will simply remit the matter to the Minister for reconsideration.¹³⁴ Courts have consistently (and correctly) refused to usurp the Minister's jurisdiction by substituting their own decision for that of the Minister.

Criminal prosecution

The acts and omissions that are subject to civil penalties may also be the subject of criminal penalties under s 238 and s 239 of the Act. Under s 238, it is an offence to fail to file a return or to comply with specific sections, such as s 231.2 (furnishing of information upon the Minister's request). Offences under s 238 are strict liability offences; there is no requirement of mens rea, and the taxpayer may be

¹³⁰ *Floyd Estate v MNR* [1993] 2 CTC 322 at 322, 93 DTC 5499 (FCTD) at 5499.

¹³¹ See *Floyd Estate*, *ibid*; *Towers v The Queen* 94 DTC 6118 (FCTD); *Guimont v MNR* [1994] 1 CTC 353, 94 DTC 6227 (FCTD); *Catahan v MNR* [1995] 1 CTC 309, 95 DTC 5496 (FCTD); *Kaiser v MNR* 95 DTC 5187 (FCTD).

¹³² *Kaiser*, *ibid* at 5187.

¹³³ These procedures were followed in the cases cited in n 131 above.

¹³⁴ See *Baron and Baron v MNR* 96 DTC 6262 (FCTD).

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exculpated by proving that he or she acted with due diligence.¹³⁵ Under s 239, it is an offence to falsify records, or to evade compliance or payment of taxes in other ways. Offences under s 239 require mens rea. Upon conviction of an offence under s 238 or s 239, the taxpayer is punishable by a fine or both a fine and imprisonment with a maximum term of five years.

Suspected cases of tax evasion are investigated by the special investigation division of each District Taxation Office. Where the evidence obtained is considered by Revenue Canada to be sufficient to lay a criminal charge, the case is handed over to the Department of Justice for prosecution.¹³⁶ According to Information Circular IC 73-10R3, "[R]eferrals to the Department of Justice are based on considerations relating to the facts and evidence of the commission of offences and account is not taken of the prominence, influence, or position in the community of the person or persons concerned".¹³⁷

Subsection 239(2) allows the Attorney General of Canada to elect to prosecute upon indictment of the offences under s 239(1).¹³⁸ If this election is made, the accused will be entitled to a jury trial and, if convicted, will be subject to more severe penalties. The prosecutorial discretion under s 239(2) has been unsuccessfully challenged under the Charter. Section 11(f) of the Charter guarantees the right to a trial by jury in cases where the maximum term of imprisonment is five years or greater. In *Darbishire v R*,¹³⁹ where the accused was prosecuted by summary conviction, the Court rejected his argument that the failure of the Attorney General to make the election had violated his right under s 11(f) by depriving him of the right to a trial by jury. In *R v Century 21 Ramos Realty Inc*,¹⁴⁰ the Attorney General did not elect to proceed by indictment, and the accused argued that the decision to proceed summarily had violated their rights under s 15 of the Charter, since the right of appeal in a summary conviction proceeding was less extensive than that in a

¹³⁵ In *The Queen v JP Consultants Ltd* [1990] 2 CTC 514 (Man Prov Ct), where the taxpayer was convicted only after failing to establish that he, and the corporation of which he was a director or officer, had taken all reasonable steps to comply with demands served to file returns.

¹³⁶ Revenue Canada has described the circumstances in which it will lay charges for criminal offences in Information Circular IC 73-10R3, 13 February 1987.

¹³⁷ *Ibid* at paragraph 30.

¹³⁸ Section 239(2) of the Act.

¹³⁹ 83 DTC 5164 (Ont Co Ct).

¹⁴⁰ [1987] 1 CTC 340, 87 DTC 5158 (Ont CA), leave to appeal to SCC refused.

prosecution by indictment. That argument was also rejected by the Court:

The very purpose of a hybrid offence provision is to allow for a variation in the differing circumstances that are to be found from one case to another. An offence like tax evasion is such that in one case it will be appropriate, due to the greater seriousness of the act committed, to proceed by indictment, whereas in another less serious case, it will be appropriate to proceed by way of summary conviction. The hybrid offence provision in the Income Tax Act is thus a means by which the criminal law provides the Attorney General with sufficient flexibility to take the specific circumstances of each case into account and ensure that, in each case, the interests of justice are served. In fact, lack of such choice could lead to a contravention of s 15 in that persons who are *not* similarly situated would get the same treatment and, thereby be treated unfairly.¹⁴¹

Double Penalties

As indicated above, both civil penalties and criminal penalties can apply to the same offence. For example, a taxpayer may be charged and convicted of the offence of falsifying statements in a tax return under s 239(1). The same taxpayer may also be liable for a penalty under s 163(2) where he or she willfully or in circumstances amounting to gross negligence fails to report an amount of income. Double penalties apply where the civil penalty is imposed before the laying of charges under s 239. In practice, civil penalties are imposed by the Minister during the assessment process, so that when a criminal charge is laid, the taxpayer has often already been assessed for civil penalties. Revenue Canada generally decides to prosecute where it considers that a civil penalty is an inadequate punishment for the taxpayer's conduct. Double penalties can be avoided only in the unusual cases where the taxpayer has not been assessed for a civil penalty when the criminal charge is laid. In such cases, the punishment imposed on conviction for the criminal offence is the exclusive sanction; no civil penalty can be imposed for the same conduct.¹⁴²

The coexistence of criminal and civil penalties has been challenged, unsuccessfully, under the Charter.¹⁴³ Section 11(h) of the Charter provides that "any person charged with an offence has the right...if finally acquitted of the offence, not to be tried for it again and, if

¹⁴¹ Ibid at 359 (CTC).

¹⁴² Section 238(3) and s 239(3) of the Act.

¹⁴³ For more discussion, see Butler, above n 9 at 29:18-26; Innes, above n 97 at chapter 9.

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finally found guilty and punished for the offence, not to be tried and punished for it again". It has been held that s 11(h) applies only to criminal penalties; the civil penalties under the Act are administrative, not criminal or quasi-criminal in nature.¹⁴⁴ Therefore, the double penalties under the Act do not violate s 11(h) of the Charter. The rationale was explained by the Court in *Lavers v British Columbia (Minister of Finance)*:¹⁴⁵

In my view, the distinction in the severity of the respective penalties indicates that Parliament intended that the imposition of the statutory penalty following an assessment by the Minister would reflect a sufficiently significant monetary punishment to deter taxpayers from failing to comply with the Income Tax Acts and would thereby achieve the objective of this administrative procedure. It is also an incentive to diligence for those who might be grossly negligent but not truly criminal. On the other hand, the severity of the public sentence which could be imposed following a conviction under s 239 clearly points to Parliament's intention to provide a punishment designed to redress a public wrong. I do not consider this distinction in the nature and purpose of the two punishments to be diminished by the fact that all fines end up in the consolidated revenue fund, via the Receiver General of Canada. In the circumstances this is the only appropriate office to which such payments could be made. In summary, therefore, the penalty assessment, while not trivial, is not so severe as to amount to a "true penal consequence".

F Appeals

When a taxpayer disagrees with the Minister's assessment or reassessment, the taxpayer has the right to appeal to the Minister for review and thereafter to the Tax Court of Canada. In cases where the dispute concerns issues other than assessment or reassessment, the taxpayer can seek judicial review at the Federal Court - Trial Division (FCTD). A decision of the Tax Court of Canada or the FCTD can be appealed further to the Federal Court of Appeal and ultimately (with leave) to the Supreme Court of Canada.

Administrative appeal

The appeal procedures under the Act commence with the filing of a notice of objection to an assessment or reassessment pursuant to

¹⁴⁴ *Vespoli v R* [1986] 1 CTC 2591, 86 DTC 1404 (TCC); *Yes Hdgs Ltd etc 57 Alta LR 2d 227* (CA) (leave to appeal to SCC denied); *R v Georges Contr Ltd* (1988) 24 BCLR (2d) 175 (CA); *The Queen v GM Caseley* [1991] 1 CTC 211 (PEI SC).

¹⁴⁵ [1990] 1 CTC 265 at 288 (BCCA).

s 165(1) of the Act.¹⁴⁶ The notice of objection must be in writing and must set out the reasons for the objection and all relevant facts, and it must be served on the Minister within 90 days after the mailing of the notice of assessment.¹⁴⁷ Notices of objection are considered by the Appeals Branch of Revenue Canada, which "will carefully review the assessment in an impartial and objective manner".¹⁴⁸ After considering a notice of objection and all the relevant facts, the appeals officer may decide that the objection should be settled through an agreement with the taxpayer. If no agreement can be reached, the Chief of Appeals has the authority to confirm the assessment, vacate it, or vary it. Where an assessment is confirmed, the taxpayer will receive a formal notification by registered mail; if the assessment is vacated or varied, the taxpayer will receive a notice of reassessment by registered mail. Revenue Canada's practice is also to advise the taxpayer's adviser of its action. After Revenue Canada has reassessed or confirmed the reassessment, or if more than 90 days have passed without a reassessment or confirmation, the taxpayer can appeal to the Tax Court of Canada.

Appeals to Tax Court of Canada

The Tax Court of Canada (TCC) is a specialized court¹⁴⁹ and part of the federal judicial system. It replaced the Tax Review Board in 1983, which in turn replaced the Tax Appeal Board in 1971. The TCC is an inferior court of record¹⁵⁰ and has no inherent jurisdiction except that conferred specifically by statute. For example, although the Act confers exclusive jurisdiction on the TCC over matters arising from the Minister's assessment or reassessment under ss 169 and

¹⁴⁶ Filing a notice of objection is the first formal step in the appeal procedure. Taxpayers are generally given opportunities to make submissions before an assessment or a reassessment is issued.

¹⁴⁷ A taxpayer can apply for the extension of the time limits under ss 166.1 and 166.2 of the Act. Sections 165(1.11) to (1.4) provide special rules for objections by large corporations.

¹⁴⁸ Information Circular IC 807, "Objections and Appeals", dated 30 June 1980, para 12.

¹⁴⁹ Tax Court of Canada Act, SC 1980-81-82-83, c 158, proclaimed in force 18 July 1983 (the "TCC Act"). All appeals on matters arising under the Act, the Excise Tax Act, Petroleum and Gas Revenue Tax Act, etc lie to the Tax Court of Canada.

¹⁵⁰ *McMillen Holdings Limited v MNR* [1987] 2 CTC 2327, 87 DTC 585 (TCC).

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175,¹⁵¹ it excludes certain tax-related matters from the TCC's jurisdiction and requires that they be considered by a Federal Court or provincial superior court. Such matters include: authorization to take action under the collection in jeopardy provisions of s 225.2 and review of such action; authorization for entry to a dwelling under s 231.1; authorization of disclosure of third party information under s 231.2; and consideration of solicitor-client privilege claims under s 232.

There are two alternative procedures for appeals heard by the TCC: the informal procedure and the general procedure.¹⁵² The informal procedure applies to appeals under the Act where:

- the taxpayer has made the appropriate election; and
- the aggregate of all amounts in issue is equal to or less than \$12,000, or the amount of a loss in issue is equal to or less than \$24,000.¹⁵³

The rationale for the informal procedures is to reduce the cost of appeals and to increase the accessibility. Under the informal procedure, the taxpayer may appear in person or be represented by an agent who does not have to be a lawyer; no special form of pleadings or other formalities are required; the Court is not bound by technical rules of evidence; costs may not be awarded against the taxpayer, and there is a statutory timetable for the hearing and disposition of the appeal.¹⁵⁴ A decision of the TCC under the informal procedure cannot be appealed, although the decision is subject to judicial review by the Federal Court of Appeal.

The general procedure is used in all other cases.¹⁵⁵ Under this procedure: a taxpayer must be represented by a lawyer; the proceedings are more formal; the rules of evidence apply in full; costs may be awarded against the taxpayer, and there is no statutory time limit on the hearing and disposition of the appeal. A decision of the

¹⁵¹ Section 29 of the Federal Court Act prohibits judicial review under ss 18 or 28 when there is a specific statutory provision providing for an appeal from, *inter alia*, an action of the Minister.

¹⁵² See McMechan Robert and Bourgard Gordon, *Tax Court Practice* (Carswell 1995).

¹⁵³ Section 18.1 to s 18.28 of the TCC Act, above n 149.

¹⁵⁴ Section 18.14 to s 18.17 of the TCC Act, above n 149.

¹⁵⁵ That is, it applies where: the amount of tax and penalties in issue exceeds \$12,000; the amount of loss in issue is more than \$24,000; or the taxpayer has not elected for the informal procedure.

TCC under the general procedure can be appealed to the Federal Court of Appeal.

The burden of proof in an appeal lies with the taxpayer, who must establish that the factual findings upon which the Minister based the assessment are wrong.¹⁵⁶ Subsection 152(8) of the Act deems an assessment "to be valid and binding notwithstanding any error, defect or omission in the assessment". If the taxpayer appeals any penalty assessed by the Minister, on the other hand, s 163(3) of the Act provides that the burden of establishing the facts justifying the assessment of the penalty is on the Minister. The Minister's burden of proof concerning penalties does not alter the taxpayer's burden of showing that the Minister's reassessment was wrong.¹⁵⁷ The reason for the taxpayer to bear the burden of proof in a trial at the TCC is that the taxpayer almost exclusively possesses the facts.¹⁵⁸ The standard of proof for the taxpayer is the civil standard of the balance of probability.¹⁵⁹

The TCC may dispose of an appeal by:

- dismissing it; or
- allowing it and a) vacating the assessment, b) varying the assessment, or c) referring the assessment back to the Minister for reconsideration and reassessment.¹⁶⁰

The TCC cannot judicially review the actions of the Minister or her or his servants, or entertain actions against them on grounds of tort. This may cause a taxpayer significant problems where constitutional

¹⁵⁶ See *Johnston v MNR* [1948] CTC 195, 48 DTC 1182 (SCC).

¹⁵⁷ It has been confirmed in *The Queen v Taylor* [1984] CTC 436, 84 DTC 6459 (FCTD) that the reverse onus provision of s 163(3) applies only when a penalty is imposed. See also *De Graaf v The Queen* [1985] 1 CTC 374, 85 DTC 5280 (FCTD).

¹⁵⁸ Harris EC, "Civil Penalties under the Income Tax Act" 1988 *Corporate Management Tax Conference* (Canadian Tax Foundation 1989) at 9: 14.

¹⁵⁹ Where a taxpayer is prosecuted for a criminal offence under s 238 or s 239 of the Act, the prosecution is conducted in the provincial court system under the rules of criminal procedure of the Criminal Code. In a prosecution, it is the normal criminal rules as to the burden of proof that apply. Therefore, the burden of proving all elements of the offence charged rests on the Crown, and the standard of proof is proof beyond a reasonable doubt.

¹⁶⁰ Section 171(1) of the Act.

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or Charter issues are involved.¹⁶¹ Judicial review is available at the Federal Court - Trial Division, but is very limited.

Judicial review

By virtue of s 29 of the Federal Court Act¹⁶² the Federal Court has no jurisdiction to review the Minister's assessment. A series of cases have explored the question of whether a notice of assessment issued by the Minister may be so deficient or so lacking in statutory authority that it is not to be treated as an assessment under the Act and, therefore, is subject to judicial review. The courts have found, however, that the appeal procedure to the TCC applies in respect of any act of the Minister which was, or purported to be, an assessment, including collection proceedings.¹⁶³

Judicial review at the Federal Court - Trial Division is possible, if it involves actions of the Minister other than those in relation to an assessment, such as the exercise of discretion to waive or cancel interest and penalties under s 220(3.1). As discussed above, although the Minister is under a duty to apply the rules of procedural fairness in exercising the discretion, the duty is generally fulfilled where the taxpayer has been afforded the opportunity to make representations. Taxpayers have rarely succeeded in establishing the breach of duty of fairness in such cases.¹⁶⁴

¹⁶¹ See Butler AS, "Making Charter Arguments in Civil Tax Cases: Can the Courts Help Taxpayers?" (1994) 41 *Canadian Tax Journal* 847-880.

¹⁶² Section 29 of the Federal Court Act prohibits judicial review under s 18 or s 28 when there is a specific statutory provision providing for an appeal from an action of the Minister. Because s 169 and s 175 of the Act provide for an appeal to the TIC from the Minister's assessments, no judicial review is allowed.

¹⁶³ *MNR v Parsons* [1983] CTC 321, 83 DTC 5329 (FCTD), reversed [1984] CTC 352, 84 DTC 6345 (FCA); *Brydges v MNR* 90 DTC 6463 (FCTD); *Bechthold Resources Limited v MNR* 86 DTC 6065 (FCTD); *Greene v MNR* 95 DTC 5078 (FCTD), affirmed 95 DTC 5684 (FCA); *Optical Recording Laboratories Inc v The Queen* [1990] 2 CTC 524 at 530-531, 90 DTC 6647 at 6652 (FCA); *City Centre Properties Inc v The Queen* [1991] 1 CTC 143, 91 DTC 5083 (FCA).

¹⁶⁴ Above n 131 and n 133 and the accompanying text.

Alternative dispute resolution

The majority of tax cases instituted under the Act are settled, either in whole or in part.¹⁶⁵ This is so, despite court rulings stating that a settlement agreement does not generally bind the Minister. According to the courts, the Minister lacks the power to assess or agree to assess in a manner inconsistent with the Act:

[T]he Minister has a statutory duty to assess the amount of tax payable on the facts as he finds them in accordance with the law as he understands it. It follows that he cannot assess for some amount designed to implement a compromise settlement.¹⁶⁶

The Minister's obligation is to assess in accordance with the law. It would throw the administration of taxation in this country into chaos if the Minister were bound by every private deal he made, whether in accordance with the law or not.¹⁶⁷

The courts have also held that agreements between taxpayers and the Minister to resolve tax disputes by compromise are illegal; such agreements cannot be acted upon either by the courts or by the Minister. The rationale was stated in *Cohen v The Queen*:¹⁶⁸

The agreement whereby the Minister would agree to assess income tax otherwise than in accordance with the law would ... be an illegal agreement. Therefore, even if the record supported the appellant's contention that the Minister agreed to treat the profit here in question as a capital gain, that agreement would not bind the Minister and would not prevent him from assessing the tax payable by the appellant in accordance with the requirements of the statute.

A settlement, while not binding upon the Minister, is binding upon the taxpayer. In *Smerchanski v MNR*,¹⁶⁹ the Supreme Court of Canada held that a taxpayer, who had agreed to waive a right of

¹⁶⁵ Innes W, "The Art of the Deal, Part 3: Negotiating Settlements - The Litigation Process", *Report of Proceedings of the Forty-Sixth Tax Conference*, 1994 Tax Conference Report (Canadian Tax Foundation 1995) 32: 1-11 at 32: 1.

¹⁶⁶ *Re Galway v MNR* 74 DTC 6355 at 6357 (FCAT). See also *Canadian Marconi Company v The Queen* 89 DTC 5370 (FCTD), reversed 91 DTC 5626 (FCA); *Cohen v The Queen* 80 DTC 6250 (FCA); *Boger v MNR* 89 DTC 15 (TCC); and *Red Deer Adviser Publications Ltd v MNR* 89 DTC 520 (TCC).

¹⁶⁷ *Harvey v The Queen* 94 DTC 1910 at 1913 (TCC).

¹⁶⁸ *Cohen*, above n 46.

¹⁶⁹ [1976] CTC 448, 76 DTC 6247 (SCC).

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appeal from an assessment as part of a settlement agreement, could not later change his mind and exercise that right of appeal.

The jurisprudence does not, however, appear to bar the Minister and a taxpayer from "reaching an agreement to settle a tax liability on the basis of preferring one reasonable interpretation of the facts over another similarly reasonable but less favourable one (from the perspective of the taxpayer)".¹⁷⁰ Such agreements seem to be binding on the Minister. The courts have made it clear, however, that such agreements must always accord with the provisions of the Act that are applicable to that reasonable interpretation of the taxpayer's circumstances.

IV CHARTER RIGHTS

Section III of the article discusses the procedural rights of taxpayers during the process of tax administration. With the exception of the right of appeal, these rights are not expressed in the Act as rights of taxpayers, but rather as obligations of Revenue Canada or limitations on Revenue Canada's powers in the administration of the Act. For example, a taxpayer's right to confidentiality is recognized under s 241 of the Act by restricting Revenue Canada from disclosing taxpayer information unless in authorized situations.

The rights under the Charter are substantive rights. They are clearly stipulated as rights and can be used by taxpayers to challenge not only the decision of Revenue Canada, but also provisions of the Act. Since the rights under s 7, s 8 and s 11 of the Charter have been discussed in Part III, this Part of the article examines other Charter rights, in particular, the equality rights in s 15, the right to freedom of conscience and religion in s 2, and the right to certainty of law which is an important aspect of the rule of law recognized in the Charter.

A Equality rights

The equality rights under s 15 of the Charter have been used by taxpayers to challenge numerous provisions of the Act, including:

¹⁷⁰ Burns BA and MacGregor IS, "Resolving Tax Disputes: A Justice Perspective", *The Report of Proceedings of the Forty-Sixth Tax Conference*, 1994 Conference Report (Canadian Tax Foundation 1995) 33: 1-33-16 at 33: 10.

- the provision dealing with deductibility of child care expenses in *Symes v The Queen*;¹⁷¹
- inclusion of child support payments in the income of the custodian parent in *Thibaudeau v Canada*;¹⁷²
- tax credit for supporting a wholly dependent person;¹⁷³ and
- marital status and spousal equivalent deductions.¹⁷⁴

Canadian courts have held that the Act, like any other legislation in Canada, is subject to the Charter scrutiny.¹⁷⁵ However, because the very essence of the Act is "to make distinctions, so as to generate revenue for the government while equitably reconciling a range of necessarily divergent interests",¹⁷⁶ the courts have been reluctant in finding provisions of the Act contrary to the Charter. In *Symes*, for example, the majority of the Supreme Court of Canada held that s 63 of the Act, which restricts the amount of deduction of child care expenses, did not violate s 15 of the Charter. The Court rejected the taxpayer's argument that the restrictions had a disproportionate impact on women. It held that although women were more likely to bear the social costs of child care, there was no evidence that women were more likely to bear the financial costs of child care, and that s 63 affected only the financial costs of child care.

The Supreme Court of Canada also rejected a s 15 argument in *Thibaudeau*. In that case, a recipient of child-support payments challenged the validity of s 56(1)(b) of the Act, which required her to include the payments in her income. The taxpayer argued that s 56(1)(b) infringed on her right to equality, because it discriminated against separated custodial parents (mostly women) by forcing them to pay tax on support payments. The majority of the Court¹⁷⁷ rejected

¹⁷¹ *Symes v The Queen* [1994] 1 CTC 40, 94 DTC 6001 (SCC). Other cases challenging the constitutionality of the child care expense deduction include *Ross v The Queen* [1993] 2 CTC 2197, 93 DTC 560 (TCC); *Copeland v The Queen* [1993] 2 CTC 3046.

¹⁷² *Thibaudeau v Canada* [1995] 1 CTC 212; 95 DTC 5998 (SCC).

¹⁷³ In *Mercier v MNR* [1992] CTC 2506, the taxpayer challenged the provision in the Act that limited the credit to the support of a child under 18 on the basis of age discrimination.

¹⁷⁴ *Schachtschneider v The Queen* [1993] 2 CTC 178 (FCA).

¹⁷⁵ See, for example, *Symes*, above n 171 (per Iacobucci J) and *Thibaudeau*, above n 172 (per Gonthier J).

¹⁷⁶ *Thibaudeau*, above n 172 (per Gonthier J) at 392 (CTC).

¹⁷⁷ In both *Symes* and *Thibaudeau*, the majority consisted of male justices and the minority consisted of female justices.

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the argument and held that the provision could not be assessed in isolation from s 60(b) of the Act (which provides for a matching deduction for the payer) and from the family law system, under which support orders and agreements are made. The Court found that the deduction-inclusion system under the Act resulted in a reduction of tax for the majority of separated couples, and that, although some separated custodial parents did not benefit from the deduction-inclusion system, as a group, custodial parents did benefit. The Court concluded that the Act did not discriminate against separated custodial parents and that there was no breach of s 15 of the Charter.¹⁷⁸

B Right to freedom of conscience and religion

Section 2 of the Charter has been invoked to challenge some fundamental principles of taxation,¹⁷⁹ but no taxpayer has succeeded in convincing a court that the payment of tax is a violation of the right to freedom of conscience and religion. In *Schachtshneider v The Queen*,¹⁸⁰ a taxpayer argued that s 118(1)(b) of the Act violated her right under s 2 of the Charter, because her religion required her to be married in order to live together with her spouse, and she was thereby prevented from claiming a credit¹⁸¹ for her dependent child, a benefit that could be enjoyed by a parent who was not married. Her argument was dismissed by the Court:

Subsection 118(1) of the Income Tax Act does not directly or indirectly coerce anyone. It is not a form of control of any description which determines or limits anyone's course or religious conduct or practices. It does not impose a sanction on anyone. It simply does not engage freedom of religion and conscience in any fashion whatsoever. The incidental tax cost to the Applicant and her husband of continuing to cohabit in matrimonial status, occasioned by the birth of a child to the union, cannot be found capable of interfering with their religious belief or practice.¹⁸²

¹⁷⁸ Despite the favourable ruling in *Thibaudeau*, the government has introduced draft legislation to remove the deduction-inclusion system so that, in most cases, the custodian parent does not have to include the child support payment in her or his income. See Notice of Ways and Means attached to the March 1996 Budget.

¹⁷⁹ *Gaal v The Queen* [1993] 2 CTC 2242 (TCC); *Prior v The Queen* [1989] 2 CTC 280, 89 DTC 5503 (TCC); *Woodside v The Queen* [1993] 2 CTC 2348 (TCC).

¹⁸⁰ Above n 174.

¹⁸¹ Section 118(1)(b) of the Act.

¹⁸² *Schachtschneider*, above n 174 at 182.

The courts also rejected a taxpayer's argument that being required to pay income tax while the federal government spent money on national defence violated her s2 right on the grounds that it was contrary to her right to freedom of conscience as a Quaker.¹⁸³

C Right to certainty of law

Taxpayers do not have a separate right to certainty of law under the Charter. However, certainty of law or the subjection to known legal rules is a fundamental aspect of the rule of law.¹⁸⁴ Because the rule of law is a fundamental principle of the Canadian Constitution and is recognized in the preamble to the Charter, it could be said that taxpayers have the right to expect certainty in law.¹⁸⁵

Certainty in tax legislation and administration is an important concern for both taxpayers and the government. From a policy perspective, uncertainty may have deleterious consequences in a self-assessment system. When the law is uncertain, it is impossible for the taxpayer to know in advance what he or she can do within the law and it is therefore impossible to do any tax planning. In effect, uncertain law is retroactive law, because the effect of the law is known only after the event.¹⁸⁶ Uncertain law also penalizes those anxious to obey it and eventually creates contempt for the law. Uncertain law will thus erode the confidence of taxpayers in the system and their willingness to support and comply with the system.

Uncertainty may result from obscure law, the conferring of broad administrative discretion on Revenue Canada, inconsistent application of the law by Revenue Canada, or retroactive legislation. Although taxpayers can challenge the validity of uncertain legislation, attack Revenue Canada's exercise of its discretion, or seek to estop Revenue Canada, they have had little success in the courts.

¹⁸³ See *Prior*, above n 179.

¹⁸⁴ *Ref re Language Rights* [1985] 4 WWR 385 at 409, the Supreme Court of Canada stated, "The 'rule of law' is a highly textured expression... conveying, for example, a sense of orderliness, of subjection to known legal rules and of executive accountability to legal authority". According to the Court, the constitutional status of the rule of law is beyond question and cited the preamble to the Charter.

¹⁸⁵ See *Arnold*, below n 192 at 1128-1131; *Nathanson*, below n 192 at 9: 16-27; *Nitikman*, below n 192 at 1424-1427.

¹⁸⁶ See the *Carter Report*, above n 55, vol 2 at 14.

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Uncertain legislation

Given the complexity of the subject matter, it is not surprising that "taxing statutes are notorious for the use of elusive, puzzling and at times almost incomprehensible language".¹⁸⁷ Such language often creates uncertainty. The uncertainty may arise from the use of language that is so obscure as to be incapable of interpretation with any degree of precision or from the generality of the discretion conferred on the Minister.

With respect to legislation, no provision in the Act has been declared void for vagueness or uncertainty. Unless the words of a statute are so absolutely senseless as to provide little or no guidance for legal debate,¹⁸⁸ Canadian courts are bound to construe the language of the statute.¹⁸⁹ For example, in *454538 Ontario Limited*,¹⁹⁰ the Court found that, although s 55(2) of the Act (which provides a tax-free divisive reorganization of a corporation in certain circumstances) was vague and created problems in application, it was not void. The test seems to be: if a reasonably intelligent and, since the law is technical in nature, sufficiently well informed taxpayer, is able to determine the meaning of a provision and is capable of governing her or his actions in a manner which will comply with the statute, the provision in question will not be invalid for vagueness.¹⁹¹

Revenue Canada sometimes has wide discretion under the Act, especially under the anti-avoidance provisions, such as the general

¹⁸⁷ *454538 Ontario Limited and 454539 Ontario Limited v MNR* 93 DTC 427 (TCC).

¹⁸⁸ *R v Nova Scotia Pharmaceutical Society* [1992] 2 SCR 606 (SCC).

¹⁸⁹ The doctrine of vagueness is summed up by the Supreme Court of Canada in *Nova Scotia Pharmaceutical Society*, *ibid* at 638, as follows: "[a] law will be found unconstitutionally vague if it so lacks in precision as not to give sufficient guidance for legal debate. This statement of the doctrine best conforms to the dictates of the rule of law in the modern State, and it reflects the prevailing argumentative, adversarial framework for the administration of justice. See also *Moldowan v The Queen* 77 DTC 5213 (SCC) at 5214; *Osborne v Canada* [1991] 2 SCR 69 (SCC); *First Fund Genesis Corporation v The Queen* 91 DTC 5361 (FCTD) at 5369; *R v Print Three Inc* 88 DTC 6315 (Ont Prov Ct).

¹⁹⁰ *ibid* n 187.

¹⁹¹ *Ibid*. See also *The Queen v Cancor Software Corp* 92 DTC 6090 (Ont Ct (General Division)) which held that s 239 of the Act was not void for vagueness.

anti-avoidance rule (GAAR) in s 245 of the Act.¹⁹² The application of these provisions inevitably involves some uncertainty because of the nature of avoidance transactions and the inherent difficulty in distinguishing between abusive avoidance transactions and acceptable tax planning. However, as mentioned above, the uncertainty or lack of clarity of such provisions is not sufficient in itself to render them invalid,¹⁹³ as long as the administrative discretion conferred on Revenue Canada is subject to scrutiny by the courts. For example, in *Krag-Hansen v The Queen*, the Federal Court of Appeal held that the former s 247(2)(a)¹⁹⁴ was not invalid for vagueness and that it did not violate the rule of law because the taxpayer was given a full opportunity to contest the whole of the Minister's decision.¹⁹⁵

Retroactive legislation

In Canada, it is common for tax legislation to take effect on the date the legislation is announced (usually the date of the budget speech that announced the measure) notwithstanding that several months, or years, may pass before enactment. Retroactive legislation creates uncertainty as to the state of the law during the period between the date of announcement and the date of enactment. It may have the practical effect of creating a legal vacuum and can seriously

¹⁹² For a discussion of the legal validity of the general anti-avoidance rule (GAAR) in s 245, see Arnold BJ, "The Canadian General Anti-Avoidance Rule" (1995) 6 *British Tax Review* 541-556; Arnold BJ and Wilson JR, "The General Anti-Avoidance Rule - Part 1" (1988) 36 *Canadian Tax Journal* 829-887; "Part 2" (1988) 36 *Canadian Tax Journal* 1123-1185 "Part 3" (1988) 36 *Canadian Tax Journal* 1369-1410; Joel Nitikman, "Is GAAR Void for Vagueness?" (1989) 37 *Canadian Tax Journal* 1409-1447; Kellough HK, "A Review and Analysis of the Redrafted General Anti-Avoidance Rule" (1988) 36 *Canadian Tax Journal* 23-78; Nathanson DC, "The Proposed General Anti-Avoidance Rule" in *Report of Proceedings of the Thirty-Ninth Tax Conference*, 1987 Conference Report (Canadian Tax Foundation 1988) 9: 1-27; Sturrock CC, "Tax Reform and the Anti-Avoidance Proposals" in 1987 *British Columbia Tax Conference* (Canadian Tax Foundation 1987) tab 7; and Birnie DAG, "Living with GAAR" 1988 *Corporate Management Tax Conference* (Canadian Tax Foundation 1988) 5: 1-16.

¹⁹³ In *Schultz v The Queen* 93 DTC (TCC), affirmed by the Federal Court of Appeal, 95 DTC 5657, the Tax Court of Canada held that s 245(1) was not void for vagueness.

¹⁹⁴ Section 247 has been repealed by 1988 tax reform and replaced by similar rules in other anti-avoidance provisions.

¹⁹⁵ 86 DTC 6122. See also *Vanguard Coatings and Chemicals Ltd v The Queen* 88 DTC 6374 (FCA).

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undermine the rule of law, particularly when it is accompanied by a long waiting period. However, the courts have refused to interfere with the budgetary process.¹⁹⁶ In practice, uncertainty is often mitigated by the wide dissemination of budget speeches, draft legislation and commentaries on the draft legislation. Taxpayers and their advisers receive clear notice that their affairs will be subject to the new rules from the date of the announcement.

Under the Canadian Constitution, Parliament and the provincial legislatures have virtually unlimited discretion in establishing the effective dates of new tax laws.¹⁹⁷ Previously, the only requirement imposed by the Canadian courts on retroactive legislation was that the intended retrospective effect be clear and unequivocal.¹⁹⁸ Since the enactment of the Charter, the courts have continued to follow that principle and have held that retrospective tax legislation does not offend the rule of law,¹⁹⁹ or s 7 of the Charter.²⁰⁰ Retrospective taxing provisions do not violate a taxpayer's right to life, liberty and security of the person under s 7 of the Charter, because s 7 does not guarantee a right to the permanence of a statute, nor does it protect economic rights.²⁰¹

¹⁹⁶ *Turner v Canada* 149 NR 218 (FCA).

¹⁹⁷ Sherbaniuk DJ, "Retrospectively in Canadian Tax Legislation", *Report of Proceedings of the Thirty-Fifth Tax Conference*, 1983 Conference Report (Canadian Tax Foundation 1984) 727-759; Pullen KT and Kellough HJ, "Tax Treatment of Intercorporate Dividends, Grandfathering Provisions, and the Use of Press Releases," 1987 Corporate Management Conference Report (Canadian Tax Foundation 1988) 3: 1-61 at 3: 33-48.

¹⁹⁸ See *Gustavson Drilling (1964) Limited v MNR* [1977] 1 SCR 271. The courts seemed to encourage the implementation of retroactive tax measures when it was a matter of protecting public finances against unexpected monetary incursions. In *Air Canada v British Columbia* [1989] 1 SCR 1161, the Supreme Court of Canada held that, even if an Act imposing a tax was ultra vires, a subsequent amendment could retroactively impose the tax and authorize the retention of moneys unconstitutionally withheld before the amendment, in payment of taxes owing as a result of the amendment.

¹⁹⁹ See *Swanick v MNR* 85 DTC 630 (TCC); *Beesley v MNR* 86 DTC 1498; *Storey Group Homes Limited v MNR* 92 DTC 1295; *Beare v MNR* 91 DTC 411; *Alcan Aluminum Limited v The Queen* 94 DTC 6369.

²⁰⁰ In *Huet v The Queen* 95 DTC 5008 (FCTD), for example, the Court found that a taxpayer's rights had not been violated by a retroactive provision in a taxing statute. See also *Hokhold v The Queen* 93 DTC 5339 (TCC); *La Chambre des Notaires du Quebec v Harltrecht* [1992] RJQ 947 (Ct App).

²⁰¹ *Attorney General of Quebec v Irwin Toy Limited* [1989] 1 SCR 927 (SCC).

V THE FAIRNESS LEGISLATION

The fairness legislation was released in 1991 with much fanfare by Revenue Canada. Although there was some disappointment that it had a fairly narrow scope and provided relief in only limited circumstances,²⁰² it has indeed made the tax system somewhat "simpler, easier and fairer" and Revenue Canada "kinder and gentler".²⁰³ The tax system has been made fairer under the fairness legislation in the following cases, where Revenue Canada has the discretion to:

- permit the amendment of returns for statute-barred years or permit the request for refunds after three years, where there is evidence to support the fact that the taxpayer was actually entitled to the deduction or credit;
- permit late filing of a return owing to illness or other unforeseen circumstances;
- permit the late filing of certain elections as set out in Regulation 600, provided that the penalty is paid and that there is no attempt to undertake retroactive tax planning;
- waive or cancel interest or penalties resulting from Revenue Canada's undue delay in processing the return or reassessment;
- waive or cancel interest or penalties in cases of financial hardship;
- waive a penalty for late remittance of source deductions of taxes if it is a first occurrence.²⁰⁴

Fairness in the tax system has also been improved by the fact that taxpayers have the right to apply for judicial review as to whether the Minister has acted fairly in exercising the discretion under the

²⁰² See Landau S, "The Fairness legislation in Practice" in *1994 Ontario Tax Conference* (Canadian Tax Foundation 1994) tab 15.

²⁰³ For further discussion, see Strain WJ, "The Fairness legislation: A Kinder, Gentler Revenue Canada?" *Report of the Proceedings of the Forth-Third Tax Conference*, 1991 Conference Report (Canadian Tax Foundation 1992) 8: 21-24; Nathanson DC, "The Fairness legislation, GAAP, GAAR" 1991 Ontario Tax Conference (Canadian Tax Foundation 1992) Tab 4; Beith RB, Fairness legislation, *Report of the Proceedings of the Forty-Fourth Tax Conference*, 1992 Conference Report (Canadian Tax Foundation 1993) 7: 1-11; Webb DP, "The Fairness legislation" 1992 Ontario Tax Conference (Canadian Tax Foundation 1993); Andrews DL, "A Package Full of Miracles?" *CA Magazine*, December 1992 (Canadian Institute of Chartered Accountants) 31.

²⁰⁴ See Landau, above n 202.

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fairness legislation.²⁰⁵ Taxpayers can raise fairness arguments also at the audit level, or seek fairness legislation relief during the litigation process.²⁰⁶

The appeal system has been made simpler and easier under the fairness legislation. Previously, under s 165(1) of the Act, a taxpayer was required, within 90 days from the date of the mailing of a notice of assessment, to serve on the Minister a notice of objection in duplicate, and in prescribed form, setting out the reasons for the objection and all relevant facts. The amendments to s 165(1), as part of the fairness legislation, made the latest filing date for the objection the later of: one year after the balance due date of the taxpayer for the year, and 90 days after the notice of mailing of the notice of assessment. In addition, the amendments no longer require that the notice be made in a prescribed form.²⁰⁷

In the meantime, Revenue Canada has become "kinder and gentler" in dealing with taxpayers. In fact, since the enactment of the fairness legislation, Revenue Canada has turned itself into a "service centre" and refers to taxpayers as "clients".

The fairness legislation has also raised several policy concerns. First, the fairness legislation is a high-sounding title for a handful of legislative provisions. Its scope is limited; it does nothing to improve substantive fairness in the tax system, nor does it provide relief to taxpayers who are unfairly treated in situations discussed in Part III of this article. For example, there are very limited remedies available to a taxpayer where thoughtless or even negligent conduct on the part of Revenue Canada officials has caused her or him expenses.²⁰⁸ The only ground to base an action against

²⁰⁵ See cases discussed in Part III.E above.

²⁰⁶ See Burns and MacGregor, above n 170; Calderwood J, "Negotiating Settlements: Revenue Canada" *Report of the Proceedings of the Forty-Sixth Tax Conference*, 1994 Conference Report (Canadian Tax Foundation 1995) 30: 1-8.

²⁰⁷ See *Wichartz v The Queen* [1994] 2 CTC 2345, 94 DTC 1703 (TCC).

²⁰⁸ Canadian courts have consistently refused to entertain actions framed in negligence (without more) against Ministers of the Crown or their servants. A recent example of this can be found in *Al's Steak House and Tavern Inc v Deloitte & Touche et al* (1995) 20 OR (3d) 673, where Morin J, of the Ontario Court (General Division), stated clearly that no action lies in negligence against the Attorney General or his Crown Attorneys with respect to prosecutions under the Income Tax Act. Morin J based his decision on the Supreme Court of Canada decision in *Nelles v Ontario* [1989] 2 SCR 170, which held that actions for malicious prosecution do lie

Revenue Canada for damages seems to be mala fides on the part of its officials, but mala fides is extremely difficult to prove.²⁰⁹ Second, there is a concern about the inconsistent application of the fairness legislation. The fairness committees in District Taxation Offices have been administering requests made by taxpayers, pursuant to the fairness legislation, on the basis of broad guidelines issued by the head office in the form of directives, and Revenue Canada does not monitor the circumstances in which relief is granted. Although coordination among some fairness committees has been established, there is still no mechanism to ensure that the legislation is applied consistently across the country.²¹⁰ Finally, there is a lack of public account for the amount of tax, interest and penalties forgiven by Revenue Canada under the fairness legislation.²¹¹

In conclusion, fairness of the Canadian tax system can be improved by addressing the above concerns about the fairness legislation. Substantive changes to taxpayers' rights seem unlikely at the moment, or in the near future. In general, Revenue Canada is perceived to be fair and there has been no public outcry for more procedural rights. Given the reluctance of the Canadian courts in applying the Charter in tax cases, taxpayers will continue to find it difficult to challenge provisions of the Act or decisions of Revenue Canada under the Charter.

against the Attorney General and his agents, but that proof of an improper purpose or motive is required.

²⁰⁹ In *Rollinson v The Queen* (1991) 4 TCT 6042 (TCTD), for example, the Court found the conduct of the customs officials involved (in improperly seizing and failing to care properly for the plaintiff's boat) sufficiently reprehensible to justify a substantial award of damages, including punitive damages. The court found in that case that the officials involved had certainly stepped over the line between zealous bona fides and unacceptable mala fides. See also *McGillivray v New Brunswick* (1994) 116 DLR (4th) 104; *Taylor v The Queen* 95 DTC 591 (TCC); *Collie Woollen Mills Limited v The Queen* 96 DTC 6146 (FCTD).

²¹⁰ For further, see Lanthier, above n 203.

²¹¹ See Canada, *Report of the Auditor General of Canada to the House of Commons 1994*, vol 16 (Supply and Services 1994) ch 29.