Federal Court Cour fédérale

Date: 20171026

Docket: T-345-17

Citation: 2017 FC 952

Ottawa, Ontario, October 26, 2017

PRESENT: The Honourable Mr. Justice Southcott

BETWEEN:

POMEROY'S MASONRY LIMITED

Applicant

and

ATTORNEY GENERAL OF CANADA

Respondent

JUDGMENT AND REASONS

I. Overview

[1] This is an application for judicial review of a decision made by the Minister of National Revenue or her delegate [the Minister] dated February 9, 2017, confirming the denial of a request for the re-appropriation of statute-barred credits from the Applicant's corporate income tax account to the debt in its harmonized sales tax [HST] account pursuant to section 221.2(2) of the *Income Tax Act*, RSC 1985, c 1 (5th Supp) [the Act].

[2] As explained in greater details below, this application is allowed, because the Minister's decision failed to take into account relevant circumstances raised by the Applicant in its re-appropriation request, surrounding the prospect of bankruptcy if the request was refused and the resulting possibility that the HST liability would not be paid.

II. Background

[3] The Applicant, Pomeroy's Masonry Limited, is a corporation which provides masonry services in the northeast Avalon Peninsula in Newfoundland and Labrador. It has five employees, including Mr. Michael Pomeroy, who is the corporation's sole director and shareholder.

[4] For the taxation years 2006 to 2010, the Applicant did not file corporate tax returns within the time frames required by the Act. As a result, the Canada Revenue Agency [CRA] assessed the Applicant as having taxable income in the 2006 to 2008 taxation years pursuant to s 152(7) of the Act, which resulted in it owing federal and provincial income tax, statutory penalties, and interest, totaling $97,727.56. In 2011 and 2012, CRA collected a total of $100,142.00 from the Applicant through a combination of payments made by the Applicant and the garnishment of third party payments. It applied this amount to the assessments.

[5] In 2011, the Applicant hired an accountant to remedy its noncompliance with the Act, and it subsequently filed the missing corporate tax returns in 2012. CRA then re-assessed the Applicant, issuing Notices of Reassessment on March 28, 2014, which resulted in credits to the Applicant applicable to the 2006 to 2008 taxation years totaling $83,960.92. However, under s

164(1) of the Act, the Minister cannot issue a refund unless a return is filed within three years of the applicable tax year-end. As the Applicant's returns for the 2006 to 2008 tax years were filed outside these periods, no refund of the credit balance was available to the Applicant.

[6] In the meantime, CRA also audited the Applicant for compliance with the HST provisions of the *Excise Tax Act*, RSC 1985, c E-15 [the Excise Tax Act]. On July 31, 2013, the Minister advised the Applicant that it was approximately $112,941.00 in arrears in its HST account.

[7] In January 2014, the Applicant retained a new accountant who issued to CRA written requests dated January 21, 2014, and April 4, 2014, that the Minister exercise her discretion under s 221.2(2) of the Act to re-appropriate the credit balance from the Applicant's corporate income tax account to its HST arrears. Section 221.2(2) permits re-appropriation of an amount, originally appropriated to a debt under the Act, to another debt that is or may become payable under certain other taxation statutes including the Excise Tax Act:

Re-appropriation of amounts	**Réaffectation de montants**
221.2 […]	**221.2** […]
Re-appropriation of amounts	**Réaffectation de montants**
(2) Where a particular amount was appropriated to an amount (in this section referred to as the "debt") that is or may become payable by a person under this Act, the *Excise Tax Act*, the *Air Travellers Security Charge Act* or the *Excise Act*, 2001, the Minister may, on application by the person,	**(2)** Lorsqu'un montant est affecté à une somme (appelée « dette » au présent article) qui est ou peut devenir payable par une personne en application de la présente loi, de la *Loi sur la taxe d'accise*, de la *Loi sur le droit pour la sécurité des passagers du transport aérien* ou de la *Loi de 2001 sur*

appropriate the particular amount, or a part of it, to another amount that is or may become payable under any of those Acts and, for the purposes of any of those Acts,	*l'accise*, le ministre peut, à la demande de la personne, affecter tout ou partie du montant à une autre somme qui est ou peut devenir ainsi payable. Pour l'application de ces lois:
(a) the later appropriation is deemed to have been made at the time of the earlier appropriation;	**a)** la seconde affectation est réputée effectuée au même moment que la première;
(b) the earlier appropriation is deemed not to have been made to the extent of the later appropriation; and	**b)** la première affectation est réputée ne pas avoir été effectuée jusqu'à concurrence de la seconde;
(c) the particular amount is deemed not to have been paid on account of the debt to the extent of the later appropriation.	**c)** le montant est réputé ne pas avoir été payé au titre de la dette jusqu'à concurrence de la seconde affectation.

[8] On April 16, 2014, CRA re-allocated $55,000 from the corporate income tax account to the Applicant's payroll source deductions account. The record before the Court indicates that CRA made this re-allocation because the $55,000 figure represented monies paid with the express intention that they be allocated to the payroll source deductions account, but which CRA had applied to the corporate income tax account in error. The remaining credit balance in the corporate income tax account then totalled $45,830.31. In a letter dated April 24, 2015, CRA conveyed to the Applicant the Minister's decision refusing to re-appropriate the remainder of the credit balance in the corporate income tax account to the HST account as the Applicant had requested.

[9] On September 10, 2015, the Applicant's accountant made a second request for re-appropriation of the credit balance to its HST account. By letter dated November 15, 2016, CRA advised the Applicant that $2951.20 of the statute-barred credits in the corporate income tax account had resulted from amounts previously offset from another program account and therefore were being returned to the HST account. This resulted in a remaining statute-barred credit of $42,879.11 in the corporate income tax account. On February 9, 2007, CRA issued a letter conveying the decision which is the subject of this application for judicial review, denying the request for re-appropriation of these remaining credits.

III. Issue and Standard of Review

[10] The Applicant challenges the lawfulness of the Minister's decision to deny the request for re-appropriation of the statute-barred credits. The parties agree that this is a discretionary decision. The Respondent argues that the standard of review applicable to such decisions by the Minister under s 221.2(2) of the Act is reasonableness (see *Cybernius Medical Ltd v Canada (Attorney General)*, 2017 FC 226 [*Cybernius*] at paras 35-36). While the Applicant's Memorandum of Fact and Law had expressed the same position on standard of review as the Respondent, the Applicant revised this position during oral submissions. The Applicant still raises arguments challenging the reasonableness of the Minister's decision; however, relying on *Clover International Properties (L) Ltd v Canada (Attorney General)*, 2013 FC 676 [*Clover*] at paras 15-18, it also argues that the Minister's decision involved an extricable question of law which should be reviewed on the correctness standard.

[11] In *Clover*, the Court was considering a decision by the Minister to the effect that s 221.2 of the Act cannot be applied to effect a re-appropriation which results in a refund that is statute-barred under s 164(1). Justice Strickland concluded that this decision represented an extricable question of law reviewable on a correctness standard. The arguments raised by the Applicant in the present case surround the extent to which the decision to deny the re-appropriation request turned on the fact that the $42,879.11 in credits were statute-barred and the absence of what the Minister considered to be extraordinary circumstances preventing the timely filing of the Applicant's tax returns. The Applicant submits in part that the Minister inappropriately relied on s 164(1) in determining the scope of the discretion available under s 221.2(2), representing an extricable question of law to which the correctness standard applies.

[12] I disagree that the Minister's decision can be characterized in this manner. I will canvass the Minister's decision in more detail below in the Analysis portion of these Reasons. However, for purposes of identifying the applicable standard of review, it is sufficient to note that the decision turned on consideration of the circumstances surrounding the timeliness of the Applicant's tax filings. These are factual matters. The decision evidences no explicit exercise in statutory interpretation and certainly no interpretation of s 221.2(2) which can be characterized as extricable from the factual matters considered in the decision.

[13] It is therefore my conclusion, consistent with that of Justice McVeigh in considering a decision involving factual matters in *Cybernius*, that the standard of review applicable to the Minister's decision is reasonableness.

[14] I would characterize the sole issue for the Court's consideration to be whether the Minister's decision is unreasonable.

IV. Analysis

[15] To understand the reasons for the decision under review, it is necessary to consider both the documentation leading to that decision and the documentation leading to the earlier decision of April 24, 2015. This can all be found in the Certified Tribunal Record. The Respondent's Record also includes an affidavit by Dennis Lim, an Accounts Officer with CRA, who explains that it was he who authored the April 24, 2015 letter which advised the Applicant that the request to re-appropriate the statute-barred credits was denied because there were no extraordinary circumstances which had prevented the timely filing of its returns. Consistent with that reasoning, the record also includes a document prepared by Mr. Lim, entitled Request for Re-appropriation of T2 Statute Barred Credits – Recommended Resolution, in which the recommended resolution is set out as follows:

> - From the review and all the entries from the SUDS and ACS, it doesn't really show that there were any extraordinary circumstances as to why owner didn't file on time. He was just always behind doing his tax returns.
>
> - He gave his information for the 2008 TYE to his accountants 6 months prior to it being statute barred. Being that he was probably not the accountant's only client and that he also had to work on previous tax years for the owner, the owner wasn't able to file that return within 3 years.
>
> Due to these reasons, re-appropriation is not recommended and a letter (Ministerial review not exercised) should be sent.

[16] That document also includes a section entitled “Headquarters review”, which contains the entry “Request is denied.” While it appears that Mr. Lim was not the ultimate decision-maker, the record does not demonstrate any further substantive analysis by whoever at CRA headquarters ultimately made the first decision on behalf of the Minister. As such, I regard Mr. Lim’s recommendation document and his subsequent letter as capturing the reasons for the first decision refusing the Applicant’s re-appropriation request.

[17] Mr. Lim’s affidavit explains that the Applicant’s second request was reviewed by David Nuytten, an account officer with CRA. Mr. Nuytten also prepared a recommendation document, entitled 2nd Request for Re-appropriation of T2 Statute Barred Credits – Recommended Resolution. This document records Mr. Nuytten’s observation that nothing had changed on the account, or in the applicable guidelines, since the first review. It also records that Mr. Nuytten agreed with the original recommendation, followed by a note that the additional documentation provided with the second request did not provide any new information which would overturn the initial decision. The section entitled “Headquarters review” then states as follows:

> If the taxpayer did not supply information that supported extraordinary circumstances that prevented him from filing his return(s) on time; then, we agree with your determination to deny this request.

[18] Again, the record before the Court does not identify who at CRA headquarters made the ultimate decision on behalf of the Minister or who authored the subsequent letter dated February 9, 2017, conveying to the Applicant the decision to deny its second re-appropriation request. However, I regard Mr. Nuytten’s recommendation document and the corresponding letter to capture the reasons for the decision. The substantive paragraphs of the letter read as follows:

> We will uphold the original determination, as the taxpayer did not supply additional information that supported any extraordinary circumstances that prevented him from filing the return within 3 years.
>
> The subsection 150(1)(a) of the Income Tax Act requires that a corporation files income tax returns. The Canada Revenue Agency is committed to making information available to assist taxpayers understand their tax obligations. Corporation's filing and payment requirements, as well as the limitation on receiving refunds if returns are not filed on time, are explained in the T2 Corporation Income Tax Guide, within our website www.cra-arc.gc.ca. This information can also be obtained through our toll–free enquiry line (800) 959-5525.
>
> Moreover, our records indicate that this corporation has a history of not filing corporation returns on time and that multiple requests were sent to the corporation by the Canada Revenue Agency to file outstanding returns. The Requests to File and Demands to File clearly state that a corporation must file a T2 Corporation Income Tax Return (unless they are a registered charity) for every taxation year, even if they are inactive or there is no tax payable. This also clarifies the requirement for a corporation to file returns. Although the corporation was made aware of its tax obligations, it failed to comply with these requests. This indicates that the corporation knowingly had not taken measures to correct the noncompliance within a reasonable timeframe.
>
> In conclusion, we will not re-appropriate the T2 statute-barred credits because we do not agree that the circumstances provided to explain why the corporation did not file its return within three years from the tax year-end was outside of the taxpayer's control and because the corporation did not take measures to correct the non-compliance within a reasonable timeframe.

[19] The Applicant submits that this documentation demonstrates that the first refusal decision, and the decision under review which upheld that decision, turned on the Applicant's failure to convince CRA that there were extraordinary circumstances which had prevented it from filing its returns within the three-year period which would have avoided refunds being statute-barred. The Applicant argues that the decision is unreasonable because the Minister failed

to take into account other factors relevant to the exercise of her discretion and fettered her discretion by relying on guidelines promulgated by CRA in connection with decisions under s 221.2.

[20] The guidelines to which the Applicant refers are dated December 2016 and entitled User Guide – Re-appropriation of T2 Statute-barred Credits [the Guidelines]. An Appendix to the Guidelines states that it provides guidance on the circumstances that should be considered when determining if ministerial discretion will be applied to allow the re-appropriation of statute-barred credits. That Appendix includes a section entitled "Extraordinary circumstances" which provides examples of various types of extraordinary circumstances beyond a taxpayer's control that may have prevented the filing of a return within three years of the tax year end. These include natural or human-made disasters, civil disturbances or disruptions in services, serious illness or accident, and serious emotional or mental distress.

[21] The Applicant argues that it was the Guidelines' focus upon the timeliness of the taxpayer's filings, and whether there were extraordinary circumstances explaining the lack of timeliness, which animated the Minister's decision to refuse the re-appropriation request. It challenges both the reasonableness of the policy itself and its application in the decision that is under review. The Applicant points out that the language of s 221.2(2) does not prescribe the reasons for the taxpayer's delinquency in its filing obligations as a factor, and particularly not an exclusive factor, governing the exercise of the Minister's discretion. The Applicant also argues that a requirement to show extraordinary circumstances for the late filing is inconsistent with the remedial purpose of s 221.2(2).

[22] In support of its submissions as to the purpose of s 221.2(2), the Applicant relies on language in a background section at the beginning of the Guidelines, which states the following:

> These revised guidelines have been developed with limited parameters to facilitate administration, ensure that statute-barred credits are not refunded to a taxpayer in the form of a cash disbursement; while at the same time, enabling corporate taxpayer's the ability to be selective in the use of their written-off statute-barred credits.

[23] The Applicant submits that a similar statutory purpose can be derived, at least implicitly, from *Cybernius*, a case which involved a fact pattern similar to the one at hand. At paragraphs 53 to 55, Justice McVeigh explained as follows her conclusion that it was unreasonable for the Minister not to exercise the discretion to permit re-appropriate of statute-barred credits:

> [53] Given that Cybernius is fully compliant, it is unreasonable for the Minister not to exercise their discretion to ensure the collection of the payroll source debt by using an existing tax credit. It would be counter to the purpose of the ITA for the Minister to do so, especially given the importance of source deductions in a number of Acts of Parliament.
>
> [54] The strongest support for the unreasonableness of the Minister's discretionary refusal is Justice Urie writing for the Federal Court of Appeal in *Optical Recording* at paragraph 27. Although in a slightly different context the proposition still stands:
>
> > The power which he is so given is to ensure that payment of the indebtedness by the debtor is ultimately secure. Normally the security provided would be monetary in nature. But the Minister's power is not limited to the statutory power to take security of that nature. He is empowered by virtue of his office, to manage his department, not exclusively from an administrative point of view but also from the point of view of what has in England been described as "management of taxes" which **I take it means that as a creditor he has the right to arrange payment for a tax**

> **indebtedness in such a manner that best ensures that the whole will ultimately be paid.** For example, if insistence on payment in full when due might jeopardize the solvency of the taxpayer, with consequent loss of potential for payment in full, and if the taxpayer can continue in business by giving him time to pay, in his discretion the Minister might arrange for payment in instalments with such security, if any, as he deems necessary. **Effectively, such a course protects the Revenue and, as well, the taxpayer's solvency and continued ability to pay taxes. It applies too to the taxpayer satisfying the Minister in Part VIII tax situations that the taxpayer will eliminate its liability by year end. Such a course of conduct ought to be encouraged, not discouraged.**
>
> [Emphasis added]
>
> [55] Having the tax debt paid is of utmost importance and the Minister has the discretion to make an arrangement to get it paid that may assist the taxpayer. In the end what matters is that the tax is paid.

[24] The Applicant takes the position that the purpose of s 221.2(2) is to provide a taxpayer with flexibility in the allocation of tax payments, where those payments have resulted in credits in a tax account that are statute-barred from being refunded, and to provide the Minister a means of facilitating payment of tax debts by re-allocating amounts from one tax account to another. The Applicant acknowledges that s 221.2(2) affords a discretion to the Minister, not an entitlement to the taxpayer. However, it argues that discretion should be exercised such that a taxpayer with statute-barred credits is permitted to have those credits re-appropriated absent factors that militate against such a result.

[25] I am not prepared to find that the Minister’s discretion must be exercised in the manner that the Applicant advocates. To reach such a conclusion would impose constraints on the

exercise of that discretion that cannot be derived from the statutory language. However, I do accept, as explained by Justice McVeigh, the importance of having tax debts paid. I agree that it is consistent with the overall purpose of the Act that s 221.2(2) be interpreted such that the retirement of outstanding tax debts is a factor, and indeed an important one, to be taken into account in the exercise of the Minister's discretion.

[26] Given this conclusion, having canvassed above the reasons for the decision impugned in the present case, I find the decision to be unreasonable. I agree with the Applicant that the decision was animated entirely, or almost entirely, by consideration of the Applicant's history of delinquency in its tax filings and whether there were extraordinary circumstances which explained or excused such delinquency. I am not prepared to conclude, as advocated by the Applicant, that these were not relevant considerations; however, they are certainly not the only considerations that should have been taken into account.

[27] The Applicant's written submissions in support of its re-appropriation requests explained that the Applicant is a small business employing five individuals and that, if CRA did not agree to allow the re-appropriation of the statute-barred credits to the company's HST liability, Mr. Pomeroy would not be able to pay CRA and would face the possibility of declaring bankruptcy. The submissions stated that Mr. Pomeroy had liens put on his current jobs and was struggling to keep his business going with this balance owing to CRA, making every effort to get his books and records up to date and his corporate tax filings current. As such, the written submissions identified not only hardship that would be sustained by the Applicant or its principal if the re-

appropriation request was refused but also the resulting possibility that the HST liability would not be paid.

[28] The record before the Court does not demonstrate that these factors were taken into account in the exercise of the Minister's discretion. The Respondent correctly argues that, in making discretionary decisions, the Minister has the freedom to find some factors more persuasive and afford them more weight than others, and that the decision to rely more heavily on CRA policies does not necessarily indicate that guidelines were raised to the level of law resulting in a fettering of discretion (see *Lambert v Canada (Attorney General)*, 2015 FC 1236 at para 30). However, my decision does not turn on the manner in which the Minister weighed relevant factors. Rather, it results from the fact that the record demonstrates no consideration or weighing at all of the Applicant's submissions as to the effect upon it, and its ability to pay its HST liability, that would result from its request being refused.

[29] The failure to consider these factors may be attributable to the Guidelines' emphasis on consideration of whether there were extraordinary circumstances which prevented the filing of returns within three years from the applicable tax year end. However, the Guidelines' section on extraordinary circumstances, and a subsequent section referring to CRA error or delay, are followed by a third, albeit brief, section entitled "Other circumstances". This section states that the CRA may also apply ministerial discretion if a taxpayer's circumstances do not fall within the situations described above and that each case must be reviewed based on its own circumstances. In my view, it is the Minister's failure to consider the other circumstances raised

by the Applicant, particularly when viewed through the jurisprudential lens provided by *Cybernius*, which makes the decision unreasonable.

[30] It is therefore my decision to allow this application for judicial review and order that the matter be returned to the Minister for redetermination.

V. Costs

[31] In their written submissions, each of the parties took the position that, if it was successful in this matter, costs should be awarded to it based on Column III of Tariff B of the *Federal Courts Rules*, SOR/98-106. However, at the hearing, the Applicant revised its position. It submitted that, if it was successful, it should be awarded costs on a solicitor-client basis. It took this position because, in its submission, the Respondent had failed to advance any compelling arguments in realtion to *Cybernius* and, having neither appealed nor distinguished that authority, had acted unreasonably in requiring the Applicant to proceed with this application for judicial review to obtain relief from the impugned decision. The Applicant requested an opportunity to make further written submissions in support of its position on costs, following receipt of the Court's decision on the merits of the application.

[32] At the hearing, the Respondent maintained the position that an award of party and party costs was appropriate and did not agree that there was a requirement for further written submissions, unless the Court was disposed towards the Applicant's request for an award on a solicitor-client basis.

[33] I advised the parties at the hearing that, once I had made my decision on the merits of the application, I would consider whether that decision and the reasons therefor warranted further submissions on costs. My conclusion is that no further submissions are required. While the Applicant has prevailed in this application and is entitled to costs, I find no basis to award those costs on a solicitor-client measure. As argued by the Respondent, every application for judicial review turns on its individual merits, particularly where a discretionary decision is at issue. While *Cybernius* was relevant to the outcome of this application, the outcome also turned on analysis of the circumstances of the present case, and in particular which factors were and were not taken into account by the Minister in arriving at the impugned decision.

[34] I therefore award the Applicant costs based on Column III of Tariff B of the *Federal Courts Rules*. While I encouraged the parties at the hearing to give consideration to an appropriate lump sum amount in the event party and party costs were awarded, the Respondent in particular was reluctant to depart from quantification based on the Tariff. My Order will therefore afford the parties an opportunity to agree on the quantification of costs based on the Tariff, failing which they will proceed to assessment.

JUDGMENT in T-345-17

THIS COURT'S JUDGMENT is that:

1. This application for judicial review is allowed and the matter is referred back to the Minister for re-determination.

2. Costs are awarded to the Applicant calculated based on Column III of Tariff B of the *Federal Courts Rules.* The parties shall confer with each other in an effort to reach agreement on the quantification of such costs and, within 30 days of the date of this Judgment, shall advise the Court in writing whether agreement has been reached on such quantification or whether an assessment of costs is required.

"Richard F. Southcott"
Judge

FEDERAL COURT

SOLICITORS OF RECORD

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