Date: 20080923

Docket: T-1528-07

Citation: 2008 FC 1073

Ottawa, Ontario, September 23, 2008

PRESENT: The Honourable Madam Justice Simpson

BETWEEN:

LINDSAY KERR

Applicant

and

ATTORNEY GENERAL (CANADA REVENUE AGENCY)

Respondent

REASONS FOR JUDGMENT AND JUDGMENT

[1] Lindsay Kerr, the self-represented applicant (the Applicant) seeks Judicial Review pursuant to section 18.1 of the *Federal Courts Act*, R.S.C. 1985, c. F-7 of a decision made on July 25, 2007 (the Decision) denying her request for a waiver under subsection 204.1(4) of the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) (the Act) of tax assessed under Part X.1 of the Act (the Part X.1 Tax).

CRA'S ERROR, THE EXCESS CONTRIBUTIONS AND THEIR WITHDRAWAL

[2] The Applicant received her Notice of Assessment for the 1996 taxation year on September 8, 1997. It advised her that her 1997 RRSP contribution limit was $8,121.00 (the Limit). This

number was incorrect and should have read $794.00 (the Error). The Error occurred because the Canada Revenue Agency (CRA) had incorrectly recorded the Applicant's 1996 pension adjustment. That number was keyed in as $814.00 on the Notice of Assessment when the correct figure was, in fact, $8,141.00.

[3] The Limit was approximately four times higher than it had been in earlier years and there had been no other significant changes in the Applicant's employment or income which would have explained the change. The Applicant suspected that an error had been made and informally canvassed colleagues at work and spoke with her banker. They all advised her that she could rely on the Notice of Assessment.

[4] On February 27, 1998, acting on this advice, the Applicant contributed $8,121.00 to her RRSP for the 1997 taxation year (the Second Excess Contribution). The Applicant had earlier made a $2,000.00 contribution to her RRSP on the understanding that taxpayers are allowed to over-contribute to RRSPs by up to that amount without penalty (the First Excess Contribution). This meant that the Applicant had made excess contributions in the amount of $9,327.00. This amount is calculated by taking $10,121.00 which is the total of the First and Second Excess Contributions less the $794.00 which was the correct RRSP contribution limit for the 1997 taxation year.

[5] CRA compounded the Error in early 1998, when it sent the Applicant a form T1028. It was a statement of her RRSP deduction limit and it incorrectly stated that the limit for 1998 was $7,754.00 (calculated by taking the incorrect Limit of $8,121.00 and subtracting the Applicant's

$367.00 Past Service Pension Adjustment for 1998). The correct limit for 1998 was, in fact, $427.00.

[6] The Applicant says, and counsel for CRA agreed at the hearing, that the record before the Court indicates that she was not told the correct amount of her RRSP deduction limit for the 1997 taxation year until she received a letter dated April 29, 2004. It was suggested that she knew the correct amount at an earlier date because she apparently reported it in November 2003, when she filed her 1997 income tax return. However, that return was not in evidence. Accordingly, I will treat April 29, 2004 as the date the Applicant received notice of the proper limit for her 1997 RRSP contribution.

[7] On April 29, 2004, CRA sent the Applicant a letter (the Withdrawal Letter) advising her that her actual RRSP deduction limit for 1997 had been $794.00. CRA also provided two completed versions of Form T3012A (the Forms) so that she could withdraw $8,121.00 and $1,206.00 from her RRSP on a tax-free basis. The first amount of $8,121.00 was incorrect. The form should have required her to withdraw $7,327.00 which was the Second Excess Contribution less the actual limit of $794.00. Further, there should not have been a second form in any amount.

[8] The Applicant was rightly confused about why she was apparently being required to withdraw any amount in connection with the First Excess Contribution. The Respondent now admits that this was an error and that the Applicant could have left the entire First Excess Contribution in her RRSP without penalty. However, the Forms made it impossible for the

Applicant to withdraw the Second Excess Contribution leaving in only the allowed amount and effectively required her to withdraw the entire First Excess Contribution.

[9] The Forms were sent to the Applicant so that the excess contributions could be withdrawn on a tax-free basis. Under subsection 146(8.2) of the Act, a taxpayer who has not used RRSP contributions as a deduction may be able to withdraw the unused contributions on a tax-free basis. The relevant portion of the subsection is reproduced below:

Amount deductible	**Montant déductible**
(8.2) Where	(8.2) Dans le cas où, à la fois :
…[the overpayment] may be deducted in computing the taxpayer's income for the particular year unless it is reasonable to consider that	le contribuable peut déduire ce [trop-perçu]… dans le calcul de son revenu pour l'année donnée, sauf s'il est raisonnable de considérer que :
(*e*) the taxpayer did not reasonably expect that the full amount of the premiums would be deductible in the taxation year in which the premiums were paid or in the immediately preceding taxation year, and	*e*) d'une part, le contribuable ne s'attendait vraisemblablement pas à ce que le plein montant des primes soit déductible au cours de l'année d'imposition de leur versement ou de l'année d'imposition précédente;
(*f*) the taxpayer paid all or any portion of the premiums with the intent of receiving a payment that, but for this paragraph and paragraph 146(8.2)(*e*), would be deductible under this subsection	*f*) d'autre part, le contribuable a versé tout ou partie des primes dans l'intention de recevoir un paiement qui, compte non tenu du présent alinéa et de l'alinéa *e*), serait déductible en application du présent paragraphe.

[10] The Applicant had a history of maximizing her contributions and there was no evidence to suggest that she used the Limit intending to rely on subsequent contribution room to eliminate the excess. Further, the fact that she made the First Excess Contribution demonstrated that she did not intend to over-contribute beyond the allowable amount (i.e. $2000.00). Because CRA decided to

offer the Applicant the opportunity to withdraw her over-contributions on a tax-free basis pursuant to subsection 146(8.2) of the Act (the Earlier Decision), CRA must have concluded in this case that the Applicant believed that the Limit had been correct when she made the Second Excess Contribution.

THE APPLICANT'S INCOME TAX RETURNS

[11] The Applicant did not file income tax returns for the 1997 to 2002 taxation years until November 17, 2003. However, CRA acknowledges that taxpayers who do not owe tax generally need not file returns unless CRA issues a demand under subsection 150(2) of the Act. The Applicant was never sent such a demand. Rather, she was sent a letter dated February 19, 1999 noting that she had not filed a return for 1997 and requesting that she do so. That letter advised that taxpayers "must file a tax return" in specific situations but none applied to the Applicant. In particular, she did not owe any taxes.

[12] The Applicant responded to this and other requests to file a return by phoning CRA. In many cases, she asked for extensions to file her income tax returns to which CRA agreed.

[13] On November 17, 2003, in response to arbitrary assessments for taxation years 1999 and 2000, the Applicant filed income tax returns for the 1997 to 2002 taxation years. No taxes were due and refunds were paid for all years.

PART X.1 TAX

[14] Taxpayers can be liable for Part X.1 Tax as long as an over-contribution remains in an RRSP. Under subsection 204.1(2.1), that tax is calculated as 1% per month of the cumulative excess amount. The cumulative excess amount, which is defined in subsection 204.2(1.1), is the amount of the excess contributions less $2,000.00. In the case of the Applicant, since she had made excess contributions of $9,327.00, the cumulative excess amount on which she was assessed Part X.1 Tax was $7,327.00.

[15] A taxpayer who has a cumulative excess amount must complete a T1-OVP Individual Tax Return for RRSP Excess Contributions (T1-OVP) for each taxation year in which the cumulative excess amount exists.

[16] Penalties and interest can accumulate on Part X.1 Tax if a taxpayer does not file T1-OVPs on time and/or pay the Part X.1 Tax when due. To date, the Applicant has been assessed and has paid $11,270.00 in Part X.1 Tax and associated penalties and interest in respect of the First and Second Excess Contributions.

[17] Under subsection 204.1(4), the Minister of National Revenue (the Minister) may waive the Part X.1 Tax if the over-contribution occurred because of a reasonable error and if reasonable steps were taken to eliminate the excess. The subsection provides:

(4) Where an individual would, but for this subsection, be required to pay a tax under

(4) Le ministre peut renoncer à l’impôt dont un particulier serait, compte non tenu du présent

subsection 204.1(1) or 204.1(2.1) in respect of a month and the individual establishes to the satisfaction of the Minister that

(*a*) the excess amount or cumulative excess amount on which the tax is based arose as a consequence of reasonable error, and

(*b*) reasonable steps are being taken to eliminate the excess,

the Minister may waive the tax.

paragraphe, redevable pour un mois selon le paragraphe (1) ou (2.1), si l'excédent ou l'excédent cumulatif qui est frappé de l'impôt fait suite à une erreur acceptable et que les mesures indiquées pour éliminer l'excédent ont été prises.

EARLIER DECISIONS ON THE PART X.1 TAX

The First Request

[18] On September 3, 2004, the Minister denied the Applicant's first request for a waiver of the Part X.1 Tax. It is unclear from the record when the Applicant made this request.

[19] The decision letter stated:

> Under Canada's self-assessment system of taxation, each individual is responsible for ensuring they do not contribute more to their RRSP than is allowable, based on their deduction limit. **This limit is provided on the Notice of Assessment each year.** It can also be obtained by contacting Canada Customs and Revenue Agency.
>
> …
>
> The information presented in your conversation has been taken carefully into consideration. I do sympathize with your situation and I can appreciate that the excess contribution was not made intentionally. However, **you were provided with the information required to contribute the correct amount to your RRSP.** The

> fact that you were not aware of the situation is not considered reasonable error.
>
> [my emphasis]

[20] However, in an internal report on the Applicant's situation prepared by Michael Young on July 16, 2007 (the Young Report), CRA acknowledged that:

> This response may be cause for concern. The Agency had originally provided an incorrect amount and (it appears) **we had never advised the taxpayer, in writing, that her revised 1997 RRSP deduction limit was $794.** We know that she was aware of the revised amount, having reported it correctly when filing her 1997 return in November 2003. **How she actually got that amount, though, is unclear.** It might have been disclosed in conversations but at this time, there are no case notes to verify this.
>
> [my emphasis]

The Second Request

[21] An administrative review of the previous decision was made September 20, 2005, which upheld the earlier denial. That letter stated:

> [Y]ou should have been aware that the amount in Box 52 of your T4 slip is required to be reported on your return. Under the self-assessment system of taxation, **it is every individual's responsibility to ensure that their return is properly completed.**
>
> I can assure you that careful consideration has been given to your situation. However, I have to advise you that there does not appear to be any circumstances that would warrant the waiving of the Part X.1 tax.
>
> [my emphasis]

[22] However, in the Young Report, CRA acknowledged that:

> This statement is of concern because, according to the copy of the 1996 return provided to us by the taxpayer, she **did** report the correct amount in box 206.
>
> Additionally, it needs to be noted that the letter fails to advise the taxpayer that she had the right to make application for judicial review under S. 18.1 of the Federal Court act if she did not agree with the decision. (She would not be told that until May 2006.)
>
> [emphasis in original]

The Third Request

[23] On June 8, 2006, the Applicant met with an official from CRA and was advised that the CRA would voluntarily conduct a third administrative review even though its normal practice was to conduct only two such reviews. The third review was to deal with interest and penalties (which are normally dealt with under the fairness provisions of the Act) as well as relief from Part X.1 Tax.

[24] The Applicant formally requested the third administrative review in a letter dated June 27, 2006. In her request, she wrote "[p]lease arrange for the third review to be conducted in another tax services office that is within commuting distance of my home address." The previous reviews had both been conducted by officials form the Toronto East Tax Services Office.

[25] The Applicant's request was acknowledged by letter dated July 7, 2006, which stated that "[y]our request will be addressed by the Toronto North Tax Services Office. However, the review was actually conducted by the Toronto Centre Tax Services Office and, as will be seen below, this

prejudiced the Applicant because there was a reasonable apprehension of bias on the part of the decision maker in that office.

[26] On February 22, 2007, the Applicant made written submissions. She also asked to meet "in person to clarify recurrent misconceptions, because of the complex history of my case the substantial correspondence that has amassed over the course of this lengthy dispute in my multiple attempts to resolve it."

[27] The Applicant made further written submissions in a letter dated March 13, 2007.

[28] The Applicant met with CRA officials on April 18, 2007. CRA's purpose at the meeting was "in order to advise [the Applicant] of the [negative] decision." However, CRA agreed that the Applicant could submit further information.

[29] The Applicant submitted further information on May 27, 2007. CRA responded in a letter dated May 31, 2007 which stated "[we] would ask that you allow until June 29, 2007 for the information to be reviewed, **at which time we will contact you to arrange another meeting.**" [my emphasis]

[30] However, no such meeting was held before the Decision was released on July 25, 2007.

[31] CRA says that is was unable to arrange the meeting due to scheduling conflicts during the summer months. It also stated that:

> The purpose of that further meeting was to advise the Applicant personally of CRA's decision and provide her with the letter outlining the reasons for the CRA's Decision. The intention of that meeting was not to allow for further documentation as the Applicant had, by now, had three opportunities to provide information and documentation to support her claims (these were the letter dated February 23, 2007, the letter dated March 14, 2007 and her most recent letter dated May 27, 2007).

OTHER REVIEWS

[32] It is noteworthy that CRA also denied two requests made by the Applicant under the fairness provisions of the Act.

THE DECISION

[33] The Decision on the third request took the form of a letter from Bruce Allen, the Director of the Toronto Centre Tax Services Offices, to the Applicant dated July 25, 2007. It was based on the Young Report which Bruce Allen approved on July 24, 2007.

[34] In spite of the Earlier Decision described in paragraph 18, *Supra*, CRA rejected the Applicant's argument that the excess contributions had resulted from reasonable error. CRA said:

> The Agency accepts that it erred in reporting an incorrect contribution limit for 1997; however it is our position that it was not that error that solely created or contributed to the amount owing. In conversations with Agency personnel, you have acknowledged that

> you found the contribution limit amount curious in comparison to the previous years' smaller amounts, and even sought the opinion of co-workers and your banker. It is regrettable that you chose to take their advice to maximize your contribution without confirming the amount with the Agency. **Despite having questioned the amount, you chose to make the maximum contribution anyway, thus taking it outside the realm of 'reasonable error'**.
>
> [my emphasis]

[35] In addition, CRA also held that the Applicant had not taken reasonable steps.

> On August 11, 1997 you filed your income tax return for the taxation year 1996. You did not file income tax returns again until November 17, 2003, when you filed all outstanding returns. The failure to file is, in itself, detrimental in that it allowed the error to go undetected; however, the delay created by the failure to file is equally detrimental in that penalties are calculated based on the duration of the lateness and interest is charged on any outstanding balance from the due date for payment until it is actually paid in full. **We must conclude that had you been compliant, filing income tax returns when required, the error would have come to light much earlier,** thus enabling you to take the reasonable steps necessary to warrant consideration of a tax waiver, or, alternatively, to make a compelling argument for the cancellation of penalties and interest.
>
> …
>
> Reasonable steps may include confirming that an excess amount existed and, within a reasonable period of time, reporting the excess by filing all required returns and applications. **Your decision not to file income tax returns by the required due dates, a lapse spanning six years, contradicts any argument of reasonableness.**
>
> [my emphasis]

[36] For the period prior to April 29, 2004, the Decision said, "I am reluctant to concede that during this period, all of the Agency's representatives you communicated with were unable to provide the proper direction." However, this conclusion is contradicted by the Young Report which

said "[i]t is highly unlikely that a Non-Filer / Non-Registrant agent could or would give advice relating to RRSP excess contributions".

DISCUSSION

Whether the Error was Reasonable

[37] The Act does not define 'reasonable error' and a review of case law did not lead me to a helpful definition. However, CRA's arguments are consistent with interpreting 'reasonable error' as imposing the same requirements as a due diligence defence.

[38] The Federal Court of Appeal in *Corp. de l'École-Polytechnique v. Canada*, 2004 FCA 127, 325 N.R. 64 has described the due diligence test as follows:

> **30** A person relying on a reasonable mistake of fact must meet a twofold test: subjective and objective. It will not be sufficient to say that a reasonable person would have made the same mistake in the circumstances. The person must first establish that he or she was mistaken as to the factual situation: that is the subjective test. Clearly, the defence fails if there is no evidence that the person relying on it was in fact misled and that this mistake led to the act committed. He or she must then establish that the mistake was reasonable in the circumstances: that is the objective test.

[39] CRA submits that the Applicant did not demonstrate due diligence. It says that the Applicant was familiar with RRSP deduction limits and was suspicious about why her limit would increase significantly without a clear reason. Under the circumstances, CRA says that, in order to demonstrate due diligence, the Applicant was obliged to contact CRA to confirm the Limit. Standing alone, this conclusion might be reasonable. However, by making the Earlier Decision and

allowing the tax-free withdrawal under subsection 146(8.2), CRA had, in effect, already conceded that the Applicant believed the Limit and made the Second Excess Contribution relying on that mistaken belief. Because of the Earlier Decision it was not reasonable for CRA to change its mind and later conclude that no reasonable error existed.

[40] Further, CRA publications consistently affirmed the reasonableness of the Applicant's belief by saying that a taxpayer is entitled to rely on the RRSP deduction limit contained in his or her notice of assessment. Guide T4040 RRSPs and Other Registered Plans for Retirement (RRSP Guide) says:

> **How much can you deduct?**
>
> The amount of RRSP contributions you can deduct [for the taxation year] is based on your … RRSP deduction limit, which appears on your latest *Notice of Assessment* or *Notice of Reassessment*, or on a T1028, *Your RRSP Information for* [year].
>
> You can also deduct amounts for contributions you make for certain income you transfer to your RRSP. The RRSP deduction limit does not include these amounts.

[41] As well, even the Withdrawal Letter suggested that if the Applicant was…"unsure of your current RRSP deduction limit, please refer to your most recent Notice of Assessment."

Whether Reasonable Steps were Taken to Eliminate the Excess Contribution

[42] The CRA concluded that reasonable steps had not been taken primarily because the Applicant was "not compliant [in] filing income taxes when required". However, as noted above

and as CRA conceded at the hearing, the Applicant was not sent a demand requiring her to file income tax returns. Therefore, she was compliant with all her filing obligations and this aspect of the Decision is without a factual foundation.

[43] The Applicant withdrew the entire Second Excess Contribution and $1,206.00 with respect to the First Excess Contribution on March 30, 2005. She did not withdraw the excess amounts promptly after she received the Withdrawal Letter because she was concerned that she was being required to withdraw too much money. CRA now agrees that her concern was valid and, in spite of several telephone calls to CRA, her concern was never addressed. She also misread the letter and thought she had until March 30, 2005 to make the withdrawals.

[44] However, contrary to the Applicant's view, there was no indication in the Withdrawal Letter about the timing of the withdrawal. As well, no sense of urgency was conveyed. The Withdrawal Letter nowhere states that the Excess Contributions should be withdrawn "immediately" or even "as soon as possible". All it says is that any excess "will remain subject to tax until the excess amount has been withdrawn from your plan".

[45] In view of its failure to suggest a proper time for the withdrawal or any urgency in that regard and in view of the fact that the Applicant was being told to withdraw an improper amount, it is not reasonable, in my view, for CRA to have concluded that the Applicant did not take all reasonable steps to remove the over-contribution because she did not make the withdrawal for eleven months.

[46] In the period from April 29, 2004 to March 30, 2005, the Applicant was delinquent in that she failed to file her T1-OVP forms in a timely way. But those forms dealt with the Part X.1 Tax and not with the withdrawal of over-contributions. For this reason, her delay in filing those forms should not have had any negative impact on the Decision. However, it does appear to have coloured CRA's approach to the Applicant's request for Part X.1 Tax relief.

Whether Third Review was Procedurally Fair

[47] CRA was obliged to conduct the third review in a procedurally fair manner. Information Circular IC-07-1 which is entitled Taxpayer Relief Provisions provides at paragraph 104 that:

> **CRA officials not involved in the first administrative review and decision would carry out the second administrative review.** They would prepare a decision report for the director or another delegated official for his or her consideration, including a recommendation on whether or not granting relief is justified. The final decision and notification of the decision to the taxpayer rests with the director or another delegated official, such as an assistant director.
>
> [my emphasis]

[48] CRA acknowledges that, although the Young Report was prepared in the Toronto Centre Tax Services Office, Cynthia Cox, an official from the Toronto East Tax Services Office who had been involved in the earlier reviews, reviewed and agreed with the Young Report. This happened despite the Applicant's request and CRA's assurances that the third administrative review would be conducted by an office which had not been involved in the earlier reviews.

[49] Bruce Allen likewise lacked complete independence. The Applicant says that, through a request under subsection 12(1) of the *Privacy Act*, she obtained a memorandum from Bruce Allen to Assistant Commissioner, Larry Hillier. Therein, Bruce Allen provided an update on the Applicant's file which, in my view, painted such an inaccurate picture of the Applicant's situation that it justifies a finding of a reasonable apprehension of bias. While the memorandum is not dated, the information it contained shows that it was prepared either before the third administrative review commenced or early in that process.

[50] The memorandum stated, in part:

> The taxpayer had a balance owing resulting from assessments relating to RRSP over-contributions from 1996 to 2005.
>
> [The excess contributions] had gone unaddressed because the taxpayer stopped filing returns after [the 1996 taxation year], and did not file income tax returns again until 2003 and only then after we had raised arbitrary assessments for certain years outstanding.
>
> …
>
> [I]n 1999, she had been given a time period in which to withdraw the over-contribution so as to avoid it being included in taxable income. She failed to do that.
>
> …

[51] These paragraphs make it appear that the Applicant over-contributed to her RRSP ten times. They also fail to mention that the Applicant never received a formal demand and, therefore, was not obliged to file tax returns before the arbitrary assessments were made. Lastly, there is no evidence in the Court record to support the allegation that the Applicant failed to respond when she was given time to withdraw the over-contribution.

[52] In addition, CRA told the Applicant that there would be a further meeting prior to the Decision being made and it was not held.

[53] These failures breached the duty of procedural fairness owed to the Applicant.

CONCLUSIONS

[54] The Decision is unreasonable and the process behind it was unfair.

[55] In light of the long history of this file and the multiple errors in the Decision and in the preceding reviews, I have concluded that this case is exceptional and is one to which *Wihksne v. Canada (Attorney General)*, 2002 FCA 356, 299 N.R. 211 applies. In that case, Justice Robert Décary of the Federal Court of Appeal said (at paragraph 10) that "the interests of justice cry out for directions putting an end to the process." In my view, because the Applicant did not know of the error in the Limit until April 29, 2004 and because she was asked to withdraw incorrect amounts, an outcome favourable to the Applicant on a further review is unavoidable. The Part X.1 Tax, with related interest and penalties, would certainly be set aside.

[56] Therefore, in accordance with paragraph 18.1(3)(b) of the *Federal Courts Act*, I am ordering that the Decision be quashed and that it be referred back to a different Minister's delegate of the Minister in the Toronto West Tax Services Office for re-determination in accordance with the directions in my judgment.

JUDGMENT

UPON reviewing the material filed and hearing the submissions of the Applicant and of counsel for the Respondent in Toronto on Thursday, May 15, 2008;

AND UPON reviewing post-hearing submission for the Respondent dated September 4, 2008 pursuant to the Court's Direction of July 30, 2008;

AND UPON determining that it was not necessary to receive submission from the Applicant in response to the Respondent's submissions of September 4, 2008;

NOW THEREFORE THIS COURT ORDERS AND ADJUDGES that, for the reasons given above, the Application is allowed and the request for relief from Part X.1Tax is to be re-determined by a different Minister's delegate in the Toronto West Tax Services Office. That delegate is hereby directed to conclude:

1. That the First Excess Contribution was a lawful over-contribution;

2. That the Second Excess Contribution was made as a result of reasonable error;

3. That reasonable steps were taken to eliminate the excess;

4. That all Part X.1 Tax arising from the excess contributions and related interest and penalties are to be reversed and the sum of $11,270.00 is to be repaid to the Applicant forthwith.

"Sandra J. Simpson"

Judge

FEDERAL COURT

NAME OF COUNSEL AND SOLICITORS OF RECORD

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APPEARANCES:

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MARIA VUJNOVIC	FOR RESPONDENT

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JOHN H. SIMS, QC TORONTO, ON	FOR RESPONDENT