Federal Court  Cour fédérale

Date: 20111115

Docket: T-1251-10

Citation: 2011 FC 1309

Vancouver, British Columbia, November 15, 2011

PRESENT: The Honourable Mr. Justice O'Reilly

BETWEEN:

TOASTMASTER INC.

Applicant

and

THE MINISTER OF NATIONAL REVENUE AS REPRESENTED BY THE ATTORNEY GENERAL OF CANADA

Respondent

REASONS FOR JUDGMENT AND JUDGMENT

I. Overview

[1] Toastmaster Inc. sought relief from the payment of interest on its income tax. The Canada Revenue Agency [CRA] imposed interest amounts because Toastmaster had been late in filing its returns for the years 2001, 2002, and 2005. The Minister of National Revenue denied Toastmaster's request and refused to exercise his discretion to grant the relief provided under s 220(3.1) of the *Income Tax Act*, RSC 1985, c 1 [ITA].

[2] Toastmaster argues that the Minister erred in his interpretation of the ITA and rendered an unreasonable decision. It asks me to set aside the Minister's decision and refer the matter back for reconsideration.

[3] However, I cannot find any basis for overturning the Minister's decision. In my view, the Minister's interpretation of the ITA was correct, and his decision was reasonable. I must, therefore, dismiss this application for judicial review.

[4] There are two issues:

1. Did the Minister err in his interpretation of the scope of his discretion to waive penalties and interest pursuant to s 220(3.1) of the ITA?

2. Was the Minister's decision to deny relief reasonable?

II. Factual Background

[5] Toastmaster is a U.S. resident corporation, incorporated in the State of Missouri, which produces and sells kitchen appliances and other household items. Toastmaster conducted business in Canada from 1999 to 2008.

[6] When it started up its operations in Canada, Toastmaster claims that it was advised by the accounting firm Deloitte & Touche that it did not have a Permanent Establishment [PE] in Canada, as defined in the Canada-U.S. Income Tax Convention [the Treaty]. As a result, Toastmaster believed it did not need to file federal or provincial tax returns in Canada.

[7] Between 2004 and 2006, Toastmaster and its corporate parent, Salton Inc., retained in-house tax personnel. The issue of whether Toastmaster had a PE in Canada was reconsidered and fresh tax advice was provided by PricewaterhouseCoopers LLP [PWC]. PWC concluded that Toastmaster indeed had a PE in Canada, and that Canadian federal and provincial returns should have been filed for taxation years ending in June 2000 through June 2006. PWC advised Toastmaster to submit a request to the CRA to file returns for these years through the Voluntary Disclosure Program [VDP].

[8] On July 24, 2006 an initial VDP request was sent by PWC on behalf of Toastmaster requesting review and assessment of the returns. Toastmaster claims that it believed at the time of this request that it was at, or close to, a net loss position for the taxation years in question.

[9] On March 28, 2008 the completed federal VDP submission, along with the returns and other required documents, was filed for the taxation years ending in June 2000 through June 2007. At the time of filing, loss carry-back and carry-forward requests were made to eliminate any taxes payable for the taxation years ending in June 2001 and June 2005, and Part I tax payable was reduced to $42,361 for the year ending in June 2002. A cheque was provided to CRA for this amount to ensure that all tax payable was paid in full.

[10] Toastmaster was issued Notices of Assessment for those taxation years, and no late filing penalties were imposed in keeping with the VDP request. However, subsequent Notices of Reassessment were issued on August 7, 2009 which assessed arrears interest pursuant to s 161(1) of the ITA for the 2001, 2002 and 2005 taxation years. Interest was assessed to be $346,718.17, $125,110.24, and $142,974.35 for the 2001, 2002 and 2005 taxation years, respectively. Toastmaster claims that arrears interest was assessed despite the fact that it owed only minimal amounts of tax at the time of filing given the significant loss carry-backs and carry-forwards that were available to it.

[11] PWC, on Toastmaster's behalf, filed a request for a cancellation of the interest on the basis that Toastmaster had acted quickly (once it became aware that it had a PE) to remedy its tax filing deficiencies, that only a minimal amount of tax was outstanding at the time of filing through the VDP, and that the balance due at the time of filing of the final VDP package was paid in full. Toastmaster also claimed that it was unable to pay the assessed arrears interest due to a lack of liquid assets.

[12] A Minister's delegate rejected Toastmaster's request. Toastmaster, through PWC, submitted a request for second level review with the Director, International Tax Services Office, complaining that the delegate had unduly fettered her discretion. The request for relief at the second level was denied.

III. The Minister's Decision

[13] The Minister's first decision was made by an official in the CRA's International Tax Services Office. The Minister's second decision was made by the Director, International Tax Services Office.

(a) First level decision

[14] The Minister's delegate observed that the taxpayer relief legislation grants the Minister, through his delegates, the authority to cancel all or part of a penalty and/or interest charges "where circumstances beyond the taxpayer's control" prevent the taxpayer from complying with the ITA. She then noted that the legislation allows for an adjustment where extraordinary circumstances such as natural disasters or a serious illness prevent a taxpayer from complying with the ITA, or where the charges result from the CRA's own actions.

[15] However, she also noted that under Canada's self-assessment system of taxation, it is a corporation's responsibility to file correct and complete tax returns, and to pay any outstanding amount by the required due date.

[16] The delegate found that Toastmaster had not shown that it was prevented from complying with filing requirements due to factors beyond its control, or that payment of the interest would cause it undue hardship. Accordingly, it would be inappropriate to cancel interest charges in these circumstances.

(b) Second level decision

[17] The Minister's delegate prepared a "Taxpayer Relief Fact Sheet" summarizing the circumstances:

- An outstanding balance had been allowed to exist and accrue interest, because tax became payable in June 2001 but was not remitted to the CRA until March 2008;
- Toastmaster had not exercised reasonable care, nor had it acted quickly to remedy any delays or omissions, given that:
    - The requirement to file a T2 return for a corporation is not dependent on having a PE in Canada, pursuant to s 150 of the ITA;
    - Toastmaster did not demonstrate that it had exercised a reasonable amount of care under the self-assessment system; and
    - There was no demonstration of extenuating circumstances to justify waiving the arrears interest assessed, because taxpayers are generally liable for errors made by third parties.
- The request for relief on the basis of financial hardship was not well-founded, because the definition of "hardship" for a corporation is where the continuity of business operations and the continued employment of a firm's employees are jeopardized. Since Toastmaster had already ceased operations at the time of its request, it would be of no material consequence to grant relief to an inactive corporation.

[18] This Fact Sheet formed the basis for the decision letter sent to Toastmaster. In the letter, the Minister's delegate noted that Toastmaster's account had been reviewed together with Toastmaster's submissions and the relevant legislation. However, it was also noted that there was no information that would change the first level decision, as the essential facts remained the same.

[19] Therefore, the Minister's delegate concluded that the arrears interest had been properly levied on Toastmaster.

IV. Issue One - Did the Minister err in his interpretation of the scope of his discretion to waive penalties and interest pursuant to s 220(3.1) of the ITA?

[20] Toastmaster submits that the Minister's delegates fettered the wide discretion accorded to them through s 220(3.1) of the ITA by limiting their analyses to the specific situations outlined in the Guidelines. In particular, Toastmaster says that the Minister's delegates unnecessarily relied on paragraphs 23 and 25 of the Guidelines, which provide:

> **23.** The Minister may grant relief from the application of penalty and interest where the following types of situations exist and justify a taxpayer's inability to satisfy a tax obligation or requirement at issue:
>
> (*a*) extraordinary circumstances
> (*b*) actions of the CRA
> (*c*) inability to pay or financial hardship
>
> **25.** Penalties and interest may be waived or cancelled in whole or in part where they result from circumstances beyond a taxpayer's control. Extraordinary circumstances that may have prevented a taxpayer from making a payment when due, filing a return on time, or otherwise complying with an obligation under the Act include, but are not limited to, the following examples:
>
> (*a*) natural or man-made disasters such as, flood or fire;
> (*b*) civil disturbances or disruptions in services, such as a postal strike;
> (*c*) a serious illness or accident; or
> (*d*) serious emotional or mental distress, such as death in the immediate family.

[21] Toastmaster submits that the wording of s 220(3.1) discloses no requirement to demonstrate "extraordinary circumstances beyond the taxpayer's control", contrary to paragraph 25(*a*) of the Guidelines. Toastmaster relies on *Nixon v Minister of National Revenue*, 2008 FC 917 at para 5, [*Nixon*], where the Court noted that s 220(3.1) gives the Minister broad, open-ended discretion, and

that the Guidelines themselves are non-binding. Toastmaster also notes that the jurisprudence has held that the Guidelines "are not intended to be exhaustive or to restrict the spirit or intent of the legislation": *Lalonde c Canada (Agence du revenu)*, 2008 CF 183 at para 9; *Nixon*, above at para 6; *Spence v Canada (Revenue Agency)*, 2010 FC 52 at paras 25-26, [*Spence*]. Toastmaster notes that in *Spence*, above at paras 30-31, Justice John O'Keefe determined that it is for the Minister to look beyond the Guidelines and apply the broad discretion he is afforded by the ITA. Toastmaster says that the Minister's delegates failed to consider its particular circumstances, failed to apply the broad discretion given under s 220(3.1), and allowed reliance on the Guidelines to impede the exercise of that discretion.

[22] At the outset, it is important to note that it is only the "second level" reconsideration decision that is, strictly speaking, the decision under review. The first level decision is beyond the scope of review on this application.

[23] In my view, having reviewed the record, the Minister's delegate did not fetter her discretion by considering herself bound by the Guidelines or other administrative policies. At the second level, she reviewed and considered all of the information and submissions available and referred to the Guidelines in the exercise of her discretion. I do not see any indication that the Minister treated the Guidelines as binding. In this way, the present case is distinguishable from *Spence*, above.

[24] Further, the Minister's delegate did not conclude that she could only grant relief if "extraordinary circumstances" were demonstrated or if any of the other specifically enumerated grounds in the Guidelines were made out. Rather, the second level decision letter, supported by the

second level Fact Sheet, shows that the Minister's delegate considered all of Toastmaster's submissions and explanations but found them to be wanting. The delegate clearly explained why she believed relief was not warranted, with reference to Toastmaster's positions on the issues.

V. Issue Two - Was the Minister's decision to deny relief reasonable?

[25] Toastmaster submits that given the broad authority available to the Minister under the ITA to grant relief, and Toastmaster's special circumstances, the decision to deny relief from the arrears interest was unreasonable.

[26] First, Toastmaster submits that the Minister's delegates failed to take into account the errors made by third parties acting on behalf of the taxpayer. While third party errors are generally not grounds for relief, the Minister's Guidelines at para 35 refer to the possibility of taking these errors into account in "exceptional situations".

[27] Second, Toastmaster says that the Minister's delegate failed to take into account the fact that it acted quickly to remedy its situation, and voluntarily brought the matter to the attention of the CRA by making submissions under the VDP.

[28] Third, Toastmaster says that the Minister's delegate failed to give adequate weight to the fact that Toastmaster had no previous compliance issues under the ITA.

[29] Fourth, Toastmaster submits that there are “unexplained discrepancies” between the first level of review and the second level of review that put the reasonableness of the decision in doubt. For instance, at the second level of review it was stated that the taxpayer “did not act quickly” to remedy any delay or omission (without explaining how Toastmaster failed to act quickly), while at the first level of review it was stated that Toastmaster did “act quickly” to remedy any delay or omission. Similarly, there were discrepancies at the two levels of review regarding whether or not Toastmaster had allowed a balance to exist and accrue interest.

[30] Fifth, Toastmaster asserts that at the first level of review it was noted that Toastmaster had been “negligent or careless in conducting [its] affairs under the self-assessment system” and “should have sought professional advice earlier”. However, Toastmaster says that it did seek tax advice from Deloitte & Touche at the time it began its Canadian operations and later sought tax advice from PWC. Thus, Toastmaster says that it exercised reasonable care and was not negligent.

[31] Finally, Toastmaster submits that it owed only $42,361 in taxes once the returns for the years in issue were filed, but was nonetheless assessed hundreds of thousands of dollars in arrears interest. Toastmaster says that the Minister’s delegates’ overly rigid application of the ITA led to an absurd result, especially considering the fact that Toastmaster found the error through its own due diligence and voluntarily brought the issue to the CRA’s attention.

[32] The Minister’s delegates were well aware of Toastmaster’s submissions with respect to the third party errors they claim were made by Deloitte & Touche. However, in an exercise of their discretion afforded to them under the ITA, they concluded that Toastmaster had not adequately

explained why its T2 returns had never been filed. Information that was publicly available at the time indicated that even if a corporation did not have a PE, it would still be required to file T2 returns. This failure indicated that reasonable care had not been exercised, especially in the absence of any obviously extenuating circumstances.

[33] It is true that Toastmaster voluntarily brought its situation to the CRA's attention through the VDP. However, it is arguable whether it did so "quickly". In one sense, it acted quickly once it discovered its problems, sometime between 2004 and 2006. On the other hand, with reasonable care, the problem would have been discovered many years earlier.

[34] As to Toastmaster's submission that the Minister's delegates failed to consider its prior compliance history, there was simply no prior compliance history for the Minister's delegates to consider – no returns whatsoever were filed for any taxation year prior to 2008.

[35] With respect to the alleged "discrepancies" between the findings made by the Minister's delegates at the first level and the second level, the first level decision is not the decision under review here. The findings at the second level superseded those at the first level. In any event, the existence of discrepancies does not lead to a conclusion that the second decision was unreasonable. The only question is whether those findings are supported by justified, transparent and intelligible explanations.

[36] Finally, with respect to Toastmaster's submission that the result is plainly absurd and harsh, I cannot agree. The Minister's delegates reasonably concluded that Toastmaster's situation was

brought about by its own unreasonable errors. By the time it filed its final VDP submission in 2008, its outstanding balance owing was not large, taking into account the application of eight years of loss carry-forwards and carry-backs, effectively reducing the amount of net tax owing. Much more tax would have been payable in Toastmaster's profitable years had timely filings been made. And it is on those amounts that arrears interest was applied.

[37] I would adopt the comments of Justice Paul Crampton in *Fleet v Canada (Attorney General)*, 2010 FC 609 at para 29, that "the law is well established that taxpayers are "directly responsible for the actions of those persons appointed to take care of [their] financial matters"…and that they "are expected to inform themselves of the applicable filing requirements"." [Citations omitted.]

[38] For these reasons I would conclude that the Minister's decision to decline to waive interest was a reasonable one, well within the range of possible, acceptable outcomes defensible on the facts and the law.

VI. Conclusion and Disposition

[39] The Minister's delegate did not fetter her discretion by considering herself bound by the Guidelines or other administrative policies. She explained why she believed relief was not warranted in this case, with appropriate reference to Toastmaster's positions on the issues, the legislation, and the Guidelines.

[40] Further, I can find no basis for concluding that the decision to deny relief from the arrears interest lacked justification, transparency or intelligibility or that it falls outside of the range of acceptable outcomes defensible on the facts and in law.

[41] I must, therefore, dismiss this application for judicial review, with costs.

JUDGMENT

THIS COURT'S JUDGMENT is that:

1. The application for judicial review is dismissed with costs.

"James W. O'Reilly"
Judge

Annex

Income Tax Act, RSC 1985, c 1	*Loi de l'impôt sur le revenu*, LRC 1985, ch 1
General	Disposition générale
161. (1) Where at any time after a taxpayer's balance-due day for a taxation year	**161**. (1) Dans le cas où le total visé à l'alinéa a) excède le total visé à l'alinéa b) à un moment postérieur à la date d'exigibilité du solde qui est applicable à un contribuable pour une année d'imposition, le contribuable est tenu de verser au receveur général des intérêts sur l'excédent, calculés au taux prescrit pour la période au cours de laquelle cet excédent est impayé :
(*a*) the total of the taxpayer's taxes payable under this Part and Parts I.3, VI and VI.1 for the year	*a*) le total des impôts payables par le contribuable pour l'année en vertu de la présente partie et des parties I.3, VI et VI.1;
exceeds	
(*b*) the total of all amounts each of which is an amount paid at or before that time on account of the taxpayer's tax payable and applied as at that time by the Minister against the taxpayer's liability for an amount payable under this Part or Part I.3, VI or VI.1 for the year,	*b*) le total des montants représentant chacun un montant payé au plus tard à ce moment au titre de l'impôt payable par le contribuable et imputé par le ministre, à compter de ce moment, sur le montant dont le contribuable est redevable pour l'année en vertu de la présente partie ou des parties I.3, VI ou VI.1.
the taxpayer shall pay to the Receiver General interest at the prescribed rate on the excess, computed for the period during which that excess is outstanding.	
Waiver of penalty or interest	Renonciation aux pénalités et aux intérêts
220. (3.1) The Minister's delegates may, on or before the day that is ten calendar years after the end of a taxation year of a taxpayer (or in the case of a partnership, a fiscal period of the partnership) or on application by the taxpayer or partnership on or before that day, waive or cancel all or any portion of any penalty or interest otherwise payable under this Act by the taxpayer or partnership in respect of that taxation year or fiscal period, and notwithstanding subsections 152(4) to (5), any assessment of the interest and penalties payable by the taxpayer or partnership shall be made that is necessary to take into account the cancellation of the penalty or interest.	**220.** (3.1) Le ministre peut, au plus tard le jour qui suit de dix années civiles la fin de l'année d'imposition d'un contribuable ou de l'exercice d'une société de personnes ou sur demande du contribuable ou de la société de personnes faite au plus tard ce jour-là, renoncer à tout ou partie d'un montant de pénalité ou d'intérêts payable par ailleurs par le contribuable ou la société de personnes en application de la présente loi pour cette année d'imposition ou cet exercice, ou l'annuler en tout ou en partie. Malgré les paragraphes 152(4) à (5), le ministre établit les cotisations voulues concernant les intérêts et pénalités payables par le contribuable ou la société de personnes pour tenir compte de pareille annulation.

FEDERAL COURT

SOLICITORS OF RECORD

DOCKET:	T-1251-10
STYLE OF CAUSE:	TOASTMASTER INC. v THE MINISTER OF NATIONAL REVENUE AS REPRESENTED BY THE ATTORNEY GENERAL OF CANADA
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