Federal Court of Appeal | Cour d'appel fédérale

Date: 20140218

Docket: A-138-13

Citation: 2014 FCA 45

CORAM: **PELLETIER J.A.**
DAWSON J.A.
STRATAS J.A.

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

and

ACI PROPERTIES LTD.

Respondent

Heard at Winnipeg, Manitoba, on January 14, 2014.

Judgment delivered at Ottawa, Ontario, on February 18, 2014.

REASONS FOR JUDGMENT BY: PELLETIER J.A.

CONCURRED IN BY: DAWSON J.A.
STRATAS J.A.

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REASONS FOR JUDGMENT

PELLETIER J. A.

[1] In April 2003, AFT Properties Inc. (AFT) paid $1.95 million to ACI Properties Ltd. (ACI) pursuant to a series of contracts between the two companies. For purposes of tax filings, AFT deducted this payment in computing its business income while ACI recorded the payment as a capital gain on the disposition of an interest in a joint venture.

[2] In 2006-2007 the Minister audited both ACI and AFT. One of the issues in these audits was the proper characterization of the 2003 payment. While the auditor assigned to this task agreed with ACI's characterization of the payment as the proceeds of disposition of capital property, the Rulings Directorate of the Canada Revenue Agency, which exercises internal oversight, was of the view that the payment was income in ACI's hands and not a capital gain. In 2008, the Minister reassessed ACI accordingly. AFT's assessment was not disturbed.

[3] ACI's appeal from the 2008 reassessment is currently before the Tax Court of Canada. The sole issue in that appeal is the proper characterization of the $1.95 million payment. In the course of that appeal, the Minister brought an application for the determination of a common question pursuant to section 174 of the *Income Tax Act*, R.S.C. 1985 c. 1 (5th Supp.) (the Act). AFT consents to be joined in the reference should the Minister's application succeed. The proposed question is as follows:

> What is the proper characterization of the $1.95 million payment from AFT to ACI in April 2003? Was the payment in respect of management fees or other remuneration for services provided by ACI to AFT or was the payment for an interest that ACI had in a joint venture with AFT which was capital property that ACI disposed of to AFT? This is the sole issue to be determined in ACI's appeal.

[4] In a decision cited as 2013 TCC 101 (the Decision), Justice Bocock of the Tax Court dismissed the application on the basis that the Minister's prior assessment of ACI, without any evidence of doubt or ambivalence on her part, precludes her from seeking a determination of a common question under section 174 of the Act. The Minister now appeals to this Court.

THE LEGISLATION

[5] Section 174 of the Act, as it read as the material time, provided as follows:

174 (1) Where the Minister is of the opinion that a question of law, fact or mixed law and fact arising out of one and the same transaction or occurrence or series of transactions or occurrences is common to assessments or proposed assessments in respect of two or more taxpayers, the Minister may apply to the Tax Court of Canada for a determination of the question.	174 (1) Lorsque le ministre est d'avis qu'une même opération ou un même événement ou qu'une même série d'opérations ou d'événements a donné naissance à une question de droit, de fait ou de droit et de fait qui se rapporte à des cotisations, réelles ou projetées, relatives à plusieurs contribuables, il peut demander à la Cour canadienne de l'impôt de se prononcer sur la question.
(2) An application under subsection 174(1) shall set out (a) the question in respect of which the Minister requests a determination, (b) the names of the taxpayers that the Minister seeks to have bound by the determination of the question, and (c) the facts and reasons on which the Minister relies and on which the Minister based or intends to base assessments of tax payable by each of the taxpayers named in the application, and a copy of the application shall be served by the Minister on each of the taxpayers named in the application and on any other persons who, in the opinion of the Tax Court of Canada, are likely to be affected by the determination of the question.	(2) Une demande présentée en vertu du paragraphe (1) doit faire état : *a*) de la question au sujet de laquelle le ministre demande une décision; *b*) des noms des contribuables que le ministre désire voir liés par la décision relative à cette question; *c*) des faits et motifs sur lesquels le ministre s'appuie et sur lesquels il s'est fondé ou a l'intention de se fonder pour établir la cotisation concernant l'impôt payable par chacun des contribuables nommés dans la demande; en outre, un exemplaire de la demande doit être signifié par le ministre à chacun des contribuables qui y sont nommés et à toutes autres personnes qui, de l'avis de la Cour canadienne de l'impôt, sont susceptibles d'être touchées par la décision rendue sur cette question.

(3) Where the Tax Court of Canada is satisfied that a determination of the question set out in an application under this section will affect assessments or proposed assessments in respect of two or more taxpayers who have been served with a copy of the application and who are named in an order of the Tax Court of Canada pursuant to this subsection, it may
(a) if none of the taxpayers so named has appealed from such an assessment, proceed to determine the question in such manner as it considers appropriate; or
(b) if one or more of the taxpayers so named has or have appealed, make such order joining a party or parties to that or those appeals as it considers appropriate and proceed to determine the question.

(3) Lorsque la Cour canadienne de l'impôt est convaincue que la décision rendue concernant la question exposée dans une demande présentée en vertu du présent article influera sur des cotisations ou des cotisations éventuelles intéressant plusieurs contribuables à qui une copie de la demande a été signifiée et qui sont nommés dans une ordonnance de la Cour canadienne de l'impôt conformément au présent paragraphe, elle peut:
a) si aucun des contribuables ainsi nommés n'en a appelé d'une de ces cotisations, entreprendre de statuer sur la question de la façon qu'elle juge appropriée;
b) si un ou plusieurs des contribuables ainsi nommés se sont pourvus en appel, rendre une ordonnance groupant dans cet ou ces appels les parties appelantes comme elle le juge à propos et entreprendre de statuer sur la question.

(4) Subject to subsection 174(4. 1), where a question set out in an application under this section is determined by the Tax Court of Canada, the determination thereof is final and conclusive for the purposes of any assessments of tax payable by the taxpayers named by it pursuant to subsection 174(3).

(4) Sous réserve du paragraphe (4. 1), lorsque la Cour canadienne de l'impôt statue sur une question exposée dans une demande dont elle a été saisie en vertu du présent article, la décision rendue est finale et sans appel pour l'établissement de toute cotisation concernant l'impôt payable par les contribuables nommés dans la décision, en vertu du paragraphe (3).

ANALYSIS

Standard of review

[6] In *Canada v. Miller*, 2005 FCA 394, [2005] F.C.J. No. 1953 (Q.L.) (*Miller*), this Court pointed out that a Tax Court Judge faced with an application under section 174 has to address three questions. First, the judge must be satisfied that section 174 is applicable. While the use of the word "satisfied" suggests the exercise of some discretion, the judge's task is to identify the proper test for the application of the section and then to apply that test to the facts of the case before him.

[7] Since this is an appeal from the decision of a trial judge, the standard of review analysis set out in *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235 (*Housen*) applies. The application of a legal test to a set of facts is a question of mixed fact and law that is reviewable on the standard of palpable and overriding error unless an extricable question of law can be identified and, if so, the correctness standard applies to the determination of that question: see *Housen* at paragraphs 26 and 36. The determination of the test to be applied is an extricable question of law: see *Housen* at paragraph 31.

[8] The second question to be addressed by a Tax Court Judge in a section 174 application is whether, notwithstanding that the conditions for the application of section 174 are present, the application should nevertheless be refused. This flows from the use of the word "may" in subsection 174(3). This is a true discretionary decision and can only be set aside if the Tax Court Judge has acted on a wrong principle, in the sense of an error of law, or has exercised his discretion wrongfully in that he has considered irrelevant factors or failed to consider relevant factors: *Elders*

Grain Co. v. M/V Ralph Misener (The), 2005 FCA 139, [2005] F.C.J. No. 612 (Q.L.) at paragraph 13.

[9] The last question to be dealt with by the Tax Court Judge is the procedure to be followed in the determination of the common question. Subsection 174(3) distinguishes between cases where one or more appeals from an assessment are pending and those cases where no appeals are pending. In *Miller*, this Court said that this was clearly a matter of discretion related to procedure and costs. Once again, the standard of review would be that applicable to discretionary decisions.

Does section 174 apply to the facts of this case?

[10] The first question then is whether section 174 is applicable. The Tax Court Judge's analysis is based on the premise that there must be some doubt or ambivalence on the Minister's part as to the correct answer to the proposed question sufficient to justify a proposed assessment before section 174 can apply: see Decision at paragraphs 14-16. The Tax Court Judge found support for this premise in an earlier case, *Brenneur v. Canada*, 2010 TCC 610, [2010] T.C.J. No. 489 (Q.L.) (*Brenneur*) in which the Tax Court took the position that section 174 did not apply if there was no proposed reassessment. In that case, the Court found that a contingent intention to reassess a second taxpayer in the event that the position taken by the Minister with respect to a first taxpayer did not prevail was not a "proposed reassessment" for the purposes of section 174: see *Brenneur*, at paragraphs 34-35.

[11] The Tax Court adopted this interpretation in *Daruwala v. Canada*, 2012 TCC 116, [2012] T.C.J. No. 227 (Q.L.) (*Daruwala*), a case in which section 311 of the *Excise Tax Act*, R.S.C. 1985 c. E-15, a provision that mirrors section 174, was in issue. Expanding on the reasoning in *Brenneur*, the Court in *Daruwala* set out three questions, the answers to which were indicative of whether the conditions for the application of section 174 were present. Those questions were:

- Has the applicant provided the Court with evidence of independent communication by the taxing authority to the proposed assessee or some other reasonable indication that it may reassess the proposed assessee?

- What evidence has been submitted of an actual or proposed investigation, review or survey of the proposed assessee's affairs, history or file in the context or in pursuance of a proposed asssessment?

- What submissions have been made regarding the expected efficiencies to be gained from joining a proposed and actual assessment into a single question for the Court to determine prior to the otherwise pending hearing of the single appeal?

Daruwala at paragraph 11

[12] The Tax Court Judge then applied these questions to the facts of this case. In doing so, he applied the wrong test and erred in law. The conditions for the application of section 174 are set out in subsection 174(3) of the statute: there must be "a question set out in an application under this section [that] is common to assessments or proposed assessments in respect of two or more taxpayers who have been served with a copy of the application."

[13] The Tax Court Judge hearing the application must decide whether the question set out in the notice is one that is common to assessments or proposed assessments in respect of two or more taxpayers. This requires an inquiry into the legal or factual nexus between the taxpayers who are to be parties to the determination. This inquiry need not have arisen as a result of any doubt in the Minister's mind as to the position to be taken in assessing one or the other of the taxpayers in

respect of whom the question arises. While section 174 may apply where there is a pending assessment, a pending assessment is not a condition precedent to its application.

[14] The legislative history of section 174 supports this interpretation. The words "proposed assessments" were added to section 174 in 1978. The Technical Notes to the Way and Means motion that introduced the amendment explained that it was intended "to make clear that the questions may concern assessments or proposed assessments": see Joint Book of Authorities at tab 17 (my emphasis).

[15] Finally, a consideration of the purpose of the section leads to the same conclusion. Where a question is common to two or more taxpayers, equity between taxpayers, as well as the protection of the revenue, requires that they be assessed on a consistent basis. It is open to the Minister to reassess a second taxpayer (subject to issues of timing arising from the normal reassessment period) if an appeal by a first taxpayer results in a characterization of a common transaction that is inconsistent with the basis on which the second taxpayer has been assessed. This is clear from the words of subsection 152(4) which allow the Minister to "make an assessment, reassessment or additional assessment of tax for a taxation year" at any time within the normal reassessment period.

[16] Where the Minister proceeds with a reassessment of a second taxpayer following a successful appeal by a first taxpayer, the findings of fact and law as between the Minister and the first taxpayer are not binding on the second taxpayer. The contentious question must be decided afresh in proceedings between the Minister and the second taxpayer. This gives rise to multiple proceedings, and opens the door to inconsistent decisions and inconsistent assessments between

parties to a single transaction. Section 174 is designed to reduce those risks by establishing a procedure whereby all interested parties are participants in a single proceeding where the common question is decided.

[17] In *Brenneur*, the Tax Court held that references under section 174 were to be encouraged in appropriate circumstances because "they encourage the efficient use of the Court's resources, avoid the risk of inconsistent Court decisions and of separate proceedings, ensure that the Court hears relevant evidence, and ensure the collection of taxes that are properly due": see *Brenneur*, at paragraph 36. In my view, this accurately reflects the objectives that Parliament sought to achieve when it enacted section 174.

[18] I am therefore of the view that the Tax Court Judge erred in applying the wrong test to determine if section 174 applied to the facts of this case. Since all parties are agreed that the appeal presently before the Tax Court is a single issue appeal, and since AFT is the other party to the contracts giving rise to the dispute, it is clear that the proposed question is common to both ACI's and AFT's assessments for the taxation year in question. As a result, I find that the conditions for the application of section 174 are met.

Should an order be made under section 174 of the Act?

[19] While the Tax Court judge concluded his analysis after finding that a condition for the application of section 174 was not satisfied, some of the considerations he raised in disposing of that

question were perhaps relevant to the second question he was to address, namely, should he exercise his discretion to order that there be a determination of a common question?

[20] The Tax Court Judge identified several factors that could be seen to militate against the exercise of his discretion in favour of granting the Minister's application. Among these was the fact that the Minister assessed AFT on the basis that the payment to ACI was deductible as a current expense. At no time, in the many years leading up to the Minister's application, did the Minister express any uncertainty or "bone fide element of ambivalence or uncertainty" as to the correctness of its assessing position with respect to AFT. This raises the question as to why the Minister has chosen to seek a determination of a common question at this time.

[21] Counsel for ACI speculates that the Minister's section 174 application is simply an attempt to insure against an adverse result in the ACI appeal. He further speculates that the need for such insurance arises from the Minister's realization that ACI is in a position to "demolish" the assumptions pleaded in the Reply to Notice of Appeal.

[22] It should first be noted that subsection 174(1) of the Act sets out the factors with respect to which the Minister must be satisfied prior to making an application for determination of a common question. If the Minister is satisfied that those conditions are met, the Act allows him to make the application, subject only to considerations of bad faith and abuse of process that are absent here.

[23] It should also be noted, once more, that, apart from considerations related to the normal reassessment period, nothing prevents the Minister from reassessing a second taxpayer on the basis

of a successful appeal by a first party. As a result, there is nothing untoward about the Minister using section 174 to streamline that process.

[24] The line of reasoning suggested by ACI's counsel leads to the question of whether the Court should decline to make the order sought because its effect would be to deprive ACI of a tactical advantage in the litigation. Counsel believes that he will be able to demolish the Minister's assumptions and thereby shift the burden of proof to the Minister (see *Hickman Motors Ltd v. Canada*, [1997] 2 S.C.R. 336 at paragraph 94), a burden that he believes the Minister will be unable to discharge.

[25] The fact that steps taken by the Minister in a proceeding deprive the appellant of a tactical advantage is not, in and of itself, an abuse of process, as alleged by counsel for ACI. The public interest in income tax appeals requires that the Court be able to able to decide those appeals on the basis of the correct facts and in the most expeditious, least expensive way: see *Continental Bank Leasing Corporation et al. v. The Queen*, [1993] T.C.J. No. 18 (Q.L.), 93 D.T.C. In any event, the loss of a tactical advantage decried by counsel for ACI may, for the reasons set out below, be more apparent than real. That said, where a party invokes procedural measures in circumstances which do amount to abuse of process, the Tax Court, as master of its own procedure, may act so as to protect the integrity of its process. This is not such a case.

[26] As a result, I am of the view that ACI has not identified any issue that would justify the Tax Court judge in refusing to grant the order sought by the Minister.

What procedure should be followed in the determination of the common question?

[27] That leaves the last question to be considered by the Tax Court Judge, the procedure to be followed in the determination of the common question. Subsection 174(3) provides that where an appeal is pending, the other party or parties to the transaction may be added as respondents to that appeal. This is a discretionary matter. Given that Rule 21 of *Tax Court of Canada Rules (General Procedure)*, SOR/90-688 provides that an application under section 174 of the Act shall be initiated by an originating document using Form 21(1)(c), it is presumably open to the Tax Court Judge to have the common question determined in free standing proceedings subject to the directions of the Court as to the manner of proceeding. For that reason, the statement of the "facts and reasons on which the Minister relies and on which the Minister based or intends to base assessments of tax payable" may be significant to the Tax Court Judge's determination of the procedure to be followed.

[28] As the parties had not directed their attention to this question, we asked for further submissions on the question of the content of the notice required to be given under subsection 174(2) of the Act.

[29] It is apparent from the submissions made by counsel for ACI that he contemplates that the determination of the common question will occur in the course of a proceeding, distinct from the pending appeal, in which the Minister's assumptions will no longer be "in play". While paragraph 174(3)(a) appears to contemplate such a proceeding, this case falls under paragraph 174(3)(b) which provides that the third party may be joined to a pending appeal. Given that the Minister has asked that AFT be added as a party to ACI's appeal, it would seem to me that the logic of the section

would favour having ACI's appeal proceed in the normal course, the only unresolved question being AFT's role in the conduct of the appeal. The stated question can be answered in the judgment which disposes of ACI's appeal, an answer that will be binding on AFT pursuant to subsection 174(4) in any subsequent proceedings.

[30] Since ACI has not shown why the Minister's motion should not be granted, AFT should be added as a party to ACI's appeal, subject to such directions as the Court may make as to the conduct of the appeal in light of AFT's joinder. In those circumstances, the contents of the notice given by Minister appear to me to be adequate.

[31] Different considerations may apply where the Minister seeks to have the common question determined pursuant to paragraph 174(3)(a). Since that question does not arise on these facts, I leave it to be answered when it does.

[32] As a result, I would allow the appeal with costs, allow the Minister's motion for the determination of a common question on the terms requested by the Minister and return the matter to the Tax Court Judge for directions as to the conduct of ACI's appeal in light of AFT's joinder as a party.

"J. D. Denis Pelletier"

J. A.

"I agree
Eleanor R. Dawson J.A."

"I agree
David Stratas J.A."

FEDERAL COURT OF APPEAL

NAMES OF COUNSEL AND SOLICITORS OF RECORD

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