Docket: 2003-2000(GST)G

BETWEEN:

CRANE CANADA INC. PLUMBING DIVISION,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on November 3, 2004 at Montréal, Quebec

Before: The Honourable Justice Gerald J. Rip

Appearances:

Counsel for the Appellant: Claude Desaulniers

Counsel for the Respondent: Martine Bergeron

JUDGMENT

The appeal from the assessment made under Part IX of the *Excise Tax Act* for the period from February 1, 1996 to August 31, 1999, dated June 22, 2000 and bearing number CG20276 is dismissed.

Signed at Ottawa, Canada this 14th day of December 2004.

"Gerald J. Rip"

Rip J.

Citation: 2004TCC816
Date: 20041214
Docket: 2003-2000(GST)G

BETWEEN:

CRANE CANADA INC. PLUMBING DIVISION,

Appellant,

and

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Respondent.

REASONS FOR JUDGMENT

Rip J.

[1] Crane Canada Inc. ("Crane") appeals from an assessment of tax levied under Part IX of the *Excise Tax Act* ("*Act*") (Goods and Services Tax) in which the Minister of National Revenue assessed a penalty in accordance with section 280 of the *Act*. Subsection 280(1) provides that:

> **280.** (1) Subject to this section and section 281, where a person fails to remit or pay an amount to the Receiver General when required under this Part, the person shall pay on the amount not remitted or paid
> (*a*) a penalty of 6% per year, and
> (*b*) interest at the prescribed rate,
> computed for the period beginning on the first day following the day on or before which the amount was required to be remitted or paid and ending on the day the amount is remitted or paid.
>
> **280.** (1) Sous réserve du présent article et de l'article 281, la personne qui ne verse pas ou ne paie pas un montant au receveur général dans le délai prévu par la présente partie est tenue de payer la pénalité et les intérêts suivants, calculés sur ce montant pour la période commençant le lendemain de l'expiration du délai et se terminant le jour du versement ou du paiement :
> *a*) une pénalité de 6 % par année;
> *b*) des intérêts au taux réglementaire.

[2] The facts are not in issue. No evidence was produced by either party. The appellant relied on the following facts set out in its Notice of Appeal:

> 3. The Appellant carries on business as a manufacturer of plumbing supplies, including toilet tanks (the "Business").
>
> 4. The Appellant is registered under the subdivision (d) of Division V of Part IX of the *Excise Tax Act* (Canada) (the "ETA").
>
> 5. The Business is a "commercial activity" as defined under the ETA.
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> 6. Certain toilet tanks manufactured by the Appellant at its manufacturing plant in British Colombia [*sic*] were alleged to be defective and consumers of such toilet tanks (the "Claimants") claimed to have suffered damages in connection therewith.
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> 7. The Claimants filed claims under their own property and casualty insurance policies (the "Insurance Claims") and/or were parties to a class action proceeding brought against the Appellant in the Supreme Court of British Columbia (the "Class Action").
>
> 8. In connection with the Insurance Claims and the Class Action, the Appellant entered into claims handling agreements with various insurers (the "Claims Handling Agreements").
>
> 9. Pursuant to the Claims Handling Agreements, the Appellant agreed to pay the insurers a percentage of the Actual Cash Value (the "ACV") of the costs of repairs incurred by policy holders of the insureds.
>
> 10. Claimants who required repairs as a result of an allegedly defective toilet tank contracted directly with the contractor providing the repairs and the repair contractor invoiced the Claimants.
>
> 11. The contractors' repair invoices were either paid by the Claimant who was then reimbursed by his or her insurance company or was paid directly by the Claimant's insurance company.

12. Pursuant to the Claims Handling Agreements, the insurers provided the Appellant with documentation in support of the percentage of the ACV of the repairs (which was calculated by reference to the cost of the repair including applicable GST billed by the contractor) for which the Appellant was liable to pay over to the insurer.

13. The documentation provided by the insurers to the Appellant clearly identified the portion of the settlement payments which represented the proportionate GST component of the ACV of the repairs.

14. The Appellant claimed input tax credits ("ITCs") in respect of the GST component of the settlement payments.

[3] The respondent admitted the facts described in paragraphs 3, 4, 5, 6, 7, and 14 and admitted the assessment was based on the facts alleged in paragraphs 8, 9, 10, 11, 12 and 13.

[4] The amounts paid to the insurers, the appellant originally claimed, were related to its commercial activities, the supply of toilet tanks, and therefore the appellant was entitled to input tax credits ("ITCs") in respect of the GST component of the settlement payments. The Minister denied the appellant's claim to ITCs on the basis that the insurers were not agents of the appellant for purposes of paying the contractors and therefore the appellant was not the recipient of property or services for use in its commercial activities. Appellant's counsel acknowledged that if Crane had paid the contractor directly, it would have been eligible for the ITCs. Because the amounts were paid to the insurers by way of damages, Crane was not a recipient and therefore had no right to ITCs.

[5] The only issue before me, therefore, is the penalty. The appellant argues it exercised due diligence and exercised reasonable precautions to avoid making any error in filing its GST return.

[6] In the appeal of *Pillar Oilfield Projects Ltd. v. Canada*, [1993] G.S.T.C. 49 soon after the introduction of the GST legislation, Bowman J. (as he then was), relying on the reasons for judgment of the Supreme Court of Canada in *R. v. Sault Ste. Marie*[1], held that paragraph 280(1)(*a*) of the *Act* creates a strict liability

[1] [1978] 2 S.C.R. 1299.

offence and that the only available defence is one of due diligence[2]. The taxpayer in *Pillar*, made a number of errors on its GST returns and, as a result, was assessed interest and penalties under paragraph 280(1)(*a*). The taxpayer appealed the penalties on the basis that errors were made in good faith and that they were understandable given the novelty of the GST. Bowman J. stated that due diligence requires "affirmative proof that all reasonable care was exercised to ensure that errors not be made[3]". A defence is available when the taxpayer reasonably believed in a mistaken set of facts which, if true, would render the act or omission innocent, or if he or she took all reasonable steps to avoid the particular event[4].

[7] The Federal Court of Appeal agreed that there is no bar to the defence argument of due diligence which a person may rely on against charges involving strict liability being put forward in opposition to administrative penalties: *Corporation de l'Ecole Polytechnique v. Canada*, 2004 G.T.C. 1148, 2004 F.C.A. 127[5]. In *Ecole Polytechnique*, Décary and Létourneau JJ.A. review the principles governing the defence of due diligence at paragraphs 28 to 45 inclusive. Paragraphs 28 to 31 are helpful in this appeal:

> [28] The due diligence defence allows a person to avoid the imposition of a penalty if he or she presents evidence that he or she was not negligent. It involves considering whether the person believed on reasonable grounds in a non-existent state of facts which, if it had existed, would have made his or her act or omission innocent, or whether he or she took all reasonable precautions to avoid the event leading to imposition of the penalty. See The Queen v. Sault Ste-Marie, [1978] 2 S.C.R. 1299, The Queen v. Chapin, [1979] 2 S.C.R. 121. In other words, due diligence excuses either a reasonable error of fact, or the taking of reasonable precautions to comply with the Act.
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> [29] The defence of due diligence should not be confused with the defence of good faith, which applies in the area of criminal liability, requiring proof of intent or guilty knowledge. The good faith defence enables a person to be exonerated if he or she has made an error of fact in good faith, even if the latter was

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2 Paragraph 11.

3 Paragraph 27.

4 Paragraphs 10-11.

5 See also *Canada v. Consolidated Canadian Contractors Inc.* [1999] 1 F.C. 209 (F.C.A.).

> unreasonable, whereas the due diligence defence requires that the error be reasonable, namely, an error which a reasonable person would have made in the same circumstances. The due diligence defence, which requires a reasonable but erroneous belief in a situation of fact, is thus a higher standard than that of good faith, which only requires an honest, but equally erroneous, belief.
>
> [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.
>
> [31] As soon as the defence of due diligence accepted for strict liability offences is raised, the question arises of whether the defence of error of law could also be relied on to avoid imposition of a penalty. That question does not arise only in connection with strict liability offences, although with the growth in regulations and the multiplication of statutory offences the field of strict liability has proven to be the most fertile for the emergence of this defence.

[8] In its Notice of Appeal the appellant claimed it committed an error of law in that it believed, based on a review of the GST legislation and policy statements and/or GST memoranda published by the tax authorities, that it was entitled to claim ITCs in respect of the GST component of the settlement payments.

[9] At trial, appellant's counsel argued that his client committed an error of fact. Unfortunately no witness was produced to describe the factual error[6]. There is no evidence that the appellant, or its employees responsible for filing GST returns, believed on reasonable grounds in the non-existence of certain facts, which, if they existed, would have made his or her act an innocent omission, or that the appellant, or its responsible employees, took all reasonable precautions to avoid the event that led to the imposition of the penalty.

[10] In any event, appellant's counsel argued that the appellant was a company who paid GST as a recipient of supplies and had a right to ITCs. Thus it was

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6 Appellant's counsel explained that the appellant closed its operations and counsel was unable to find any person who could testify as to the facts surrounding this appeal.

normal for the employee of the appellant who received an invoice to pay money, with the GST amount on the invoices from the insurers, to do as he or she usually does, that is, to calculate GST on supplies sold and request an ITC. It is reasonable to conclude, counsel submitted, that the person erred in fact in thinking the invoice was related to supply and paid the invoice in the course of the appellant's normal commercial activities. The appellant's employee innocently followed accepted procedures.

[11] Counsel referred to *Key Property Management Corporation v. Canada*, [2004] G.T.C. 199, 2004TCC210. In *Key Property*, the taxpayer provided management services to other corporations, each of which owned and operated rental properties. The Minister assessed the taxpayer on the basis that it was the employer of certain caretakers and maintenance personnel engaged to provide services to the buildings. Penalties were also imposed.

[12] The Minister's position was that since Key Property supplied the services of the personnel to the owner companies, it ought, therefore, to have collected GST from them. The taxpayer's position was that none of these people were its employees and it did not have to collect GST for their services.

[13] The taxpayer was successful in part, the superintendents were not employees, the other workers were. Bowie J. held that the taxpayer was entitled to additional ITCs. Since Key Property had trained its staff in GST matters, it had reasonably believed in the correctness of its position and the penalties imposed under section 280 were deleted.

[14] "An honest belief that a transaction is not subject to tax, if it is reasonably held, equals to due diligence", Bowie J. stated[7]. In the appeal at bar, appellant's counsel argued that his client erred on the facts; it had good reason to believe that it was paying GST because there was reference to GST on the invoice. The appellant, he says, made an innocent mistake of fact: the appellant paid the insurer and not the contractors; the appellant did not make payment in the capacity of recipient of a supply of property.

[15] As I mentioned earlier in these reasons there is a paucity of evidence. I do not know the practice adopted by the appellant in filing GST returns and claiming ITCs. I do not know the actions of the persons in charge of filing GST returns and I

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[7] Paragraph 22; see also paragraph 24.

do not know the thinking that went on in the minds of the appellant's employees when they prepared the GST returns and applied for ITCs. The appellant has not met the subjective and objective tests described in paragraph 30 of *Ecole Polytechnique*. A mistake was obviously made, but I do not know if the person who erred was mistaken as to a factual situation or if the mistake was reasonable in the circumstances.

[16] And even if the appellant erred in law when it applied for the ITCs, the defence of due diligence in attempting to understand and comply with the law is of no help. In *Ecole Polytechnique*, at paragraph 38, the Federal Court of Appeal stated that:

> [a]part from exceptions, ... reasonable mistakes of law as to the existence and interpretation of legislation are not recognized as defences ... to strict liability offences ... governed by the rules applicable in strict liability.

[17] There are two exceptions to this rule, the Court of Appeal noted, officially induced mistakes of law and invincible mistakes of law. Neither exception is present in this appeal. There is no evidence that the appellant's mistake was not impossible to avoid nor is there evidence the appellant relied on a mistaken legal opinion or advice of an official of the Canada Customs and Revenue Agency, as the tax authority was then named.

[18] The appeal is dismissed, with costs.

Signed at Ottawa, Canada, this 14th day of December 2004.

"Gerald J. Rip"

Rip J.

CITATION:	2004TCC816
COURT FILE NO.:	2003-2000(GST)G
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APPEARANCES:

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Counsel for the Respondent:	Martine Bergeron

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