

Date: 20080728

Docket: T-1918-07

Citation: 2008 FC 917

Victoria, British Columbia, July 28, 2008

PRESENT: The Honourable Mr. Justice Campbell

BETWEEN:

DENNIS NIXON

Applicant

and

MINISTER OF NATIONAL REVENUE

Respondent

REASONS FOR ORDER AND ORDER

[1] In 2003, Mr. Nixon failed to report \$4,000 of income, and for the 2005 taxation year he again failed to report dividend income totaling \$183,988 paid to him by his company. As a result, the Minister of National Revenue (Minister) lawfully imposed a penalty totaling \$36,796 on Mr. Nixon for repeated failure to report income under the *Income Tax Act* R.S.C. 1985, c. 1 (5th Supp.) (*Act*). As Mr. Nixon felt the imposition of this penalty to be excessive given the circumstances of his failures to report, he made a first level request under the taxpayer relief provisions of the *Act* that the penalty be canceled. This request was rejected, and, as a result, Mr. Nixon's accountant made a

second level re-evaluation request on his behalf. However, this request was also rejected on October 3, 2007; it is this rejection (Decision) that is the subject of the present Application.

[2] The question for determination is whether the Decision is reasonable. It is agreed that the appropriate standard of review to apply to a Minister's decision under the taxpayer relief provisions is reasonableness (*Lanno v. Canada (Customs and Revenue Agency)* 2005 FCA 153, 2005 D.T.C. 5245). Counsel for the Respondent argues that, in order for the Decision to be found to be unreasonable, the decision must be found to be in error pursuant to s.18.1(4) of the *Federal Courts Act*. However, Counsel for Mr. Nixon argues that for the Decision to be reasonable, it must be judged on the standard of common sense. I find that both arguments find a place in the reasonableness standard for judicial review set by the Supreme Court of Canada in *Dunsmuir v. New Brunswick*, 2008 SCC 9, [2008] S.C.J. No. 9 at para. 47:

Reasonableness is a deferential standard animated by the principle that underlies the development of the two previous standards of reasonableness: certain questions that come before administrative tribunals do not lend themselves to one specific, particular result. Instead, they may give rise to a number of possible, reasonable conclusions. Tribunals have a margin of appreciation within the range of acceptable and rational solutions. A court conducting a review for reasonableness inquires into the qualities that make a decision reasonable, referring both to the process of articulating the reasons and to outcomes. In judicial review, reasonableness is concerned mostly with the existence of justification, transparency and intelligibility within the decision-making process. But it is also concerned with whether the decision falls within a range of possible, acceptable outcomes which are defensible in respect of the facts and law.

[Emphasis added]

That is, if the Decision is not defensible in respect of the facts of Mr. Nixon's case and the law with respect to the relief provisions applied to them, it is unreasonable. For the reasons which follow, I find that on the application of the *Dunsmuir* criteria, the Decision is not reasonable and must be set aside.

I. Penalty and Taxpayer Relief Provisions of the Act

[3] The penalty to be applied under the *Act* applicable to taxpayers who have failed to report income more than once in the previous three years is specific:

<p>163 (1) Every person who (a) fails to report an amount required to be included in computing the person's income in a return filed under section 150 for a taxation year, and (b) had failed to report an amount required to be so included in any return filed under section 150 for any of the three preceding taxation years is liable to a penalty equal to 10% of the amount described in paragraph 163(1)(a), except where the person is liable to a penalty under subsection 163(2) in respect of that amount.</p>	<p>163 (1) Toute personne qui ne déclare pas un montant à inclure dans le calcul de son revenu dans une déclaration produite conformément à l'article 150 pour une année d'imposition donnée et qui a déjà omis de déclarer un tel montant dans une telle déclaration pour une des trois années d'imposition précédentes est passible d'une pénalité égale à 10 % du montant à inclure dans le calcul de son revenu dans une telle déclaration, sauf si elle est passible d'une pénalité en application du paragraphe (2) sur ce montant.</p>
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However, by s. 220(3.1) of the *Act*, the Minister has authority to apply unfettered discretion to grant relief from the operation of s. 163(1) as well as other penalty provisions in the *Act*:

<p>220(3.1) The Minister may, on or before the day that is ten</p>	<p>220(3.1) Le ministre peut, au plus tard le jour qui suit de dix</p>
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<p>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, <u>waive or cancel all or any portion of any penalty or interest otherwise payable under this Act</u> 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.</p>	<p>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.</p>
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II. The Taxpayer Relief Guidelines: Information Circular 07-1 (IC 07-1)

[4] The Minister's authority to grant relief is delegated to various officials of the Canada Revenue Agency (CRA) pursuant to s. 220(2.01) of the *Act*, and a two-level review system has been developed to assess taxpayer relief requests. As might be expected in the situation where taxpayers will apply for relief from delegates of the Minister in a wide range of fact circumstances across Canada, to bring some uniform standard to the decision-making process, the CRA has published guidelines which state situations in which relief might be appropriate to grant. The most recent version of the guidelines is dated May 31, 2007 as IC 07-1 and these were applied to Mr. Nixon's application for relief (Guidelines) (see Respondent's Application Record Tab A).

[5] A detailed consideration of the Guidelines is important with respect to the present Application because it appears that the Decision was rendered under a misapprehension of their content. As set out above, s. 220(3.1) of the *Act* gives broad open-ended discretion to the Minister in granting penalty relief, and, of course, this discretion is available to the Minister's delegates in considering specific situations presented by applying taxpayers. The Guidelines are careful to state that this broad legally approved discretion is not affected by the Guidelines:

6. These are only guidelines. They are not intended to be exhaustive, and are not meant to restrict the spirit or intent of the legislation.

[6] The point that the Guidelines are not exhaustive of the circumstances that might warrant positive discretion to be exercised under s. 220(3.1) of the *Act* is important because it gives direction on how to treat the following statements:

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

24. The Minister may also grant relief if a taxpayer's circumstances do not fall within the situations stated in ¶23.

Extraordinary Circumstances

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.

[Emphasis added]

As can be seen, the situations suggested in paragraph 23, and the definition of what constitutes “extraordinary circumstances” in paragraph 25, are not meant to limit the discretion that can be applied. Paragraph 24 makes it clear that each application for relief must be decided on its own merits. For clarity, this point is repeated in paragraph 11:

11. The Minister does not have to grant relief under the taxpayer relief provisions. Each request will be reviewed and decided on its own merit. If relief is denied or partly granted, the CRA will provide the taxpayer with an explanation of the reasons and factors for the decision.

III. The Decision

[7] Mr. Nixon’s main ground for relief is that the failures to report income were unintentional and that the imposition of such a significant penalty is unfair in the circumstances. Mr. Nixon’s application was denied on the first level review which resulted in his request for a second level

evaluation. To assist the second level decision-maker to reach the Decision, a report was prepared by another official of the CRA which sets out the circumstances of the failures to report and contains some subjective evaluation of Mr. Nixon's arguments (Report). It is agreed that the Report constitutes part of the reasons for Decision.

[8] The Report contains the following observations:

Aside from these two omissions of income, the taxpayer otherwise has a good compliance history: no delinquent action has been taken; no late filing penalties have been assessed; and the tax debts for other years have been paid within a reasonable amount of time

[...]

The omissions penalties assessed [under ss. 163(1)] total \$36,796, which does seem harsh. Although ss. 163(2) gross negligence penalties are intended to be more severe, in Mr. Nixon's case I considered substituting a ss. 163(2) penalty as had such a penalty been assessed, the penalty amount would have been reduced to \$23,244, which is a savings of \$13,522, calculated as:

Federal tax payable - \$28,826.09 X 50%	\$14,413.05
Provincial tax payable - \$17,663.52 X 50%	<u>\$8,831.76</u>
ss. 163(2) penalties	\$23,244.78
Less: ss. 163(1) penalties already assessed	<u>\$36,797.60</u>
Decrease in penalties	\$13,552.82

Subsection 163(2) penalties apply to increases in income of more than \$5,000 and as such, the \$183,988 increase to Mr. Nixon's income would more than qualify in this respect. However, as the taxpayer has not requested this application or admitted to a wilful failure as required by TOM 19(15)2.2, I have not pursued this issue in light of our parallel Regional policy.

[Emphasis added]

(Report, Respondent's Record, p. 40 and 42)

However, despite the perceived harshness of the penalty, the Report concludes that Mr. Nixon's situation is not one which qualifies for relief:

In making this recommendation, I have reviewed the relevant paragraphs of IC 07-1 regarding extraordinary circumstances.

The taxpayer clearly had the ability to pay his 2005 tax debt including the ss. 163(1) omissions penalty without causing undue financial hardship; his after-tax income for 2005 and 2006 was \$579,302 and \$267,995, respectively; he was able to contribute a total of \$41,760 to his RRSPs in those years; and, he has paid a total of \$72,107 towards his 2005 T1 debt.

[...]

I recommend that the taxpayer's request to cancel the ss. 163(1) omissions penalties assessed to his 2005 T1 return be denied on the basis that losing his T5 slip and forgetting to report his dividend income is not an extraordinary circumstance to which the Taxpayer Relief provisions would apply.

[Emphasis added]

(Report, Respondent's Record, p. 42-43)

[9] It seems that the writer of the Report was sympathetic to Mr. Nixon's plea for relief. Indeed, that person went so far as to consider whether Mr. Nixon's failures to report could be dealt with under a different section of the *Act* which would result in a lesser penalty. Nevertheless, the way the Report reads, the writer felt bound to recommend that Mr. Nixon is not a candidate for relief because the facts of his case do not constitute "extraordinary circumstances".

[10] In conformity with the statements made in the Report, a key finding in the Decision is as follows:

While I appreciate that Mr. Nixon acted quickly to remedy the omission in his response to the matching letter that was sent to him in mid-December 2006 and the advance payment he made of \$50,000 prior to the issuance of the Notice of Reassessment in January 2007, after careful consideration, I must advise that I concur with the first level decision to deny the cancellation of the omissions penalties assessed to his 2005 T-1 return under the Taxpayer Relief provisions. Although I believe that the omission was unintentional, the reasons for the omission are not extraordinary circumstances for the Taxpayer Relief provisions would apply [sic] and the situation was not beyond his control.

(Rejection Letter, Applicant's Record, p. 6)

IV. Is the Decision Reasonable?

[11] My answer to the question is “no”. It is obvious that both the writer of the Report and the official who rendered the Decision concluded that, unless Mr. Nixon could prove that he did not report due to “extraordinary circumstances”, he did not qualify for relief. I find that this interpretation is contrary to s. 220(3.1) of the *Act* and is a misapprehension of the content of the Guidelines. The *Dunsmuir* test requires that the Decision must “[fall] within a range of possible, acceptable outcomes which are defensible in respect of the facts and law”. In my opinion, the Decision is not defensible because it is based on a misapprehension of the scope of the discretion authorized by s. 220(3.1) of the *Act*. As a result, the Decision must be set aside.

ORDER

Pursuant to s.18.1(3) of the *Federal Courts Act*, the decision under review is set aside.

Costs of the Application are awarded to Mr. Nixon.

"Douglas R. Campbell"

Judge

FEDERAL COURT
SOLICITORS OF RECORD

DOCKET: T-1918-07

STYLE OF CAUSE: DENNIS NIXON v. HMQ

PLACE OF HEARING: Victoria, BC

DATE OF HEARING: July 24, 2008

**REASONS FOR ORDER
AND ORDER:** CAMPBELL J.

DATED: July 28, 2008

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