

Federal Court



Cour fédérale

Date: 20110708

Docket: T-325-10

Citation: 2011 FC 840

Ottawa, Ontario, July 8, 2011

PRESENT: The Honourable Madam Justice Simpson

BETWEEN:

CHRISTIANE MEIER

Applicant

and

CANADA REVENUE AGENCY

Respondent

REASONS FOR JUDGMENT AND JUDGMENT

THE PROCEEDING

[1] Christiane Meier [the Applicant] seeks judicial review pursuant to section 18.1 of the *Federal Courts Act*, RSC 1985 c F-1, of a decision of the Canada Revenue Agency [CRA] dated January 22, 2010 [the Decision] in which CRA denied the Applicant's second-level request for relief from interest pursuant to subsection 220(3.1) of the *Income Tax Act*, RSC 1985, c 1 (5th Supp) [the Act]. The Applicant had based her request on financial hardship.

THE FACTS

[2] The Applicant is the single mother of three minor children. She works as a self-employed hairdresser and housekeeper. The family lives in the small community of Errington, British Columbia.

[3] In 2004, the Applicant and her husband invested \$95,700.00 with Daryl Klein and his company Kleincorp Mgmt. Inc. [Kleincorp]. However, they lost a total of \$44,100.00 when Kleincorp became insolvent in 2006 and was exposed as a Ponzi scheme.

[4] Kleincorp issued T5 statements reporting interest income allegedly paid to the Applicant. The T5s showed a total income of \$89,325.55, of which \$24,425.65 was allegedly paid in 2004 and \$64,926.90 in 2005. However, the Applicant did not receive these amounts. She was paid some interest but substantially less than the amounts shown on the T5 statements.

[5] On June 27, 2007, the Applicant contacted CRA seeking to revise line 121 of her 2004/2005 tax return to remove the interest reported by Kleincorp that was never actually paid. In a letter dated August 22, 2007, CRA denied her request for the adjustment.

[6] The Applicant and her husband divorced at some point between 2006 and August 2007. The Applicant sold her former matrimonial home in August 2007. However, there was no equity. Later, in November of that year, she sold a rental property for \$118,265.00. On February 13, 2008, she

used \$94,800.00 from that sale, as well as a \$40,200.00 mortgage, to purchase a trailer. She also paid \$4,000.00 to pay off a credit card she had shared with her former husband. The balance of the proceeds (\$19, 465.00) was used to support her family.

[7] In 2008, CRA audited the Applicant's taxes for the years 2004, 2005 and 2006. The audit revealed that the Applicant's husband's accountant, who had prepared her returns, had claimed approximately \$30,000.00 in business deductions which were not supported with documentation. The Applicant signed her tax returns without reading them. She says that she was not aware that the deductions had been claimed and acknowledges that they were not valid. CRA does not suggest that the Applicant knowingly filed a false return. On September 9, 2008, at the conclusion of the audit, a Notice of Reassessment was issued [the Reassessment] showing a balance of \$20,970.81 owing for 2005 and \$1,581.87 for 2006. These are the only tax debts the Applicant has ever incurred.

[8] Following the audit, the Applicant lost confidence in her husband's accountant and engaged her present accountant, Mr. McGorman. He filed a request for taxpayer relief on the Applicant's behalf on January 7, 2009, seeking to have the interest owed on her tax debt waived and/or cancelled on the basis of financial hardship.

[9] The Applicant has always filed her income tax returns on time and the only years in which her taxes were not paid in full were 2005 and 2006.

[10] The Applicant does not challenge the Reassessment. She seeks only interest relief.

THE FIRST LEVEL DECISION

[11] CRA denied the Applicant's request for taxpayer relief at the first level. The application was refused because CRA took the position that the debt resulted from the deductions that were disallowed and was not caused by Kleincorp's insolvency. Further, CRA found that the Applicant's 2005 tax return was first reassessed on October 17, 2006, and that she therefore could have used the proceeds of the sale of the rental property in November 2007 to pay the balance owing, which at the time was \$11,651.89. CRA further noted that the Applicant had RRSPs of approximately \$14,000.00 and was paying her creditors in full and on time, and therefore concluded that she had failed to demonstrate financial hardship. Finally, CRA said that taxpayer relief applications generally require the taxpayer to have a meaningful monthly payment plan in place, and that the Applicant had made no such arrangements.

[12] Following the first level decision, Mr. McGorman submitted a second level request on August 19, 2009. On September 25, 2009, CRA requested additional financial information from the Applicant, which she provided on October 24, 2009 along with a letter explaining her situation.

THE SECOND LEVEL DECISION

[13] CRA refused the second level request on January 22, 2010. The Decision was based (i) on the Applicant's failure to retire her debt following the sale of her rental property, (ii) on her failure to liquidate her RRSPs, and (iii) on her failure to agree to a payment plan.

[14] The Decision was supported by a CRA document entitled “Taxpayer Relief Fact Sheet”. It summarized the facts in the following manner:

Taxpayer is requesting interest relief for the tax years 2005 and 2006 based on financial hardship. The tp’s [sic] is a single mother of three and lives on a limited income. A significant portion of her savings was lost in an investment scam and her income leaves nothing left after the essentials. Tp sold a rental property for \$118,265, used \$94,800 towards her new home, paid off a \$4000 credit card she had jointly with her ex, and lived off the rest. She qualified for a \$40,200 mortgage. Tp’s rep said she could not pay CRA debt as she needed all the funds to buy the house and she cannot afford rent for a house. Tp does not pay off her credit cards, tried to borrow to pay CRA but was denied, and wants to return to school. She is self employed and not earning enough to live on and is in a dire financial situation.

[15] Mr. George Matthews, the author of the Fact Sheet, concluded that:

The Tp has not been negligent. However, she was careless in the fact she did not pay off her debt to CRA before paying other creditors and purchasing a house.

[16] He also said:

The I and E [the income and expense statement] does show a clear inability to pay anything towards the debt if you base it on income. She does however have assets she could liquidate to pay the debt such as RRSPs and equity in the home although she did try for a loan and was denied.

[17] Finally, the recommendation, which led to the Decision, read as follows:

Denied.
Tp cannot make payments on the tax portion of the debt therefore we cannot approve her request for interest relief. The tp had the opportunity to retire the debt after she sold her rental property but instead put the funds into a new home. She also has \$14,000 in RRSPs she could use to pay the debt in full.

[18] In his affidavit sworn on August 6, 2010, Mr. Matthews provided the following reasons for the Decision:

- a) the applicant does not qualify for relief on the basis of financial hardship or an inability to pay as she has not entered into a payment arrangement with the CRA to address the tax portion of her debt under the *Act*;
- b) the applicant has the funds to pay her tax debt in the form of using assets such as her RRSPs; and
- c) the applicant had the funds to retire her tax debt after the sale of her rental property [i.e. the property sold in November 2007] and this debt should have been addressed before purchasing her new home.

THE STANDARD OF REVIEW

[19] The standard of review applicable to taxpayer relief decisions is that of reasonableness, see *Canada Revenue Agency v Telfer*, 2009 FCA 23, 386 NR 212 at para 2.

DISCUSSION

[20] In my view, the Decision was unreasonable for the following reasons:

- (a) Although CRA acknowledged that the Applicant's Income/Expense and Net Worth Statement [the Statement] made it clear that she could not afford to make payments to reduce her tax debt, CRA used her failure to agree to a payment plan to justify the Decision.

- (b) The Statement also made it clear that the Applicant could not live on her monthly income. Her expenses exceeded her income by approximately \$1,700.00 per month. This made it obvious that she had to use her assets and credit to meet her family's needs. In these circumstances, it was not reasonable for CRA to criticize her for paying off her credit cards. It is clear that she had to keep them current because she was using them to pay for groceries and other necessities.
- (c) The Statement also shows that the Applicant and her family lived well below the poverty line. In 2008, the poverty line for a family of four in a small community was well above the Applicant's income of \$11,807.04. In these circumstances, it was unreasonable for CRA to suggest that the Applicant liquidate her RRSPs to pay her tax debt. It was clear that she would require that money to provide food and shelter for her children.
- (d) CRA also repeatedly criticized the Applicant for using the proceeds from the sale of her rental property to purchase a "house" or a "home". This "home" was a 1200 sq. ft. trailer to accommodate four people. In my view, this purchase was entirely reasonable as it represented the most cost effective method of putting a roof over the Applicant's family.
- (e) CRA suggested that she had equity in her "home" but at the same time was aware that she had applied unsuccessfully to increase her mortgage to pay her tax debt. This meant that CRA had really concluded that she should sell the trailer and rent space to accommodate her family even though the evidence showed that it would cost her far more than her mortgage payment of \$252.90 per month to rent shelter. Essentially, CRA thought that the Applicant should move from poverty to abject poverty and would not

forgive her interest unless she took that step. This position was, in the circumstances of this case, utterly unreasonable.

- (f) Finally, even though the tax debt arose because of the improper deductions, it appears that the Applicant has been taxed on interest income from Kleincorp that she has not actually received. This means that she had overpaid her taxes and that the Reassessment overstated her liability. It was unreasonable for CRA not to consider this fact when making the Decision.

CONCLUSION

[21] For all these reasons, I have concluded that CRA's Decision was unreasonable.

JUDGMENT

THIS COURT’S JUDGMENT is that the application for judicial review is allowed and:

- (i) The self-represented Applicant is to be reimbursed for her disbursements associated with the first and second level decisions including fees charged by Mr. McGorman to prepare and document her two requests for interest relief and any disbursements associated with her appearance in Court [such as gasoline]. She is also entitled to \$300.00 in recognition of the time she spent working with her accountant, preparing for Court and attending Court. If a total amount cannot be agreed, the Registry may be contacted and I will fix the amount to be paid.
- (ii) The Applicant’s request for interest relief at the second level is to be reconsidered by a CRA employee other than George Matthews. If necessary, the reconsideration may occur at a different CRA office.
- (iii) The Applicant is to be given reasonable time to update her request for interest relief by providing current information on the status of her tax debt and on the interest she actually received from Kleincorp so that CRA can determine whether she has been taxed on funds she did not receive. If that is the case, it would, at a minimum, have a bearing on the appropriateness of interest relief.

“Sandra J. Simpson”

Judge

SOLICITORS OF RECORD

DOCKET: T-325-10

STYLE OF CAUSE: Christiane Meier v Canada Revenue Agency

PLACE OF HEARING: Nanaimo, British Columbia

DATE OF HEARING: April 21, 2011

REASONS FOR JUDGMENT: SIMPSON J.

DATED: July 8, 2011

APPEARANCES:

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(ON HER OWN BEHALF)

Whitney Dunn FOR THE RESPONDENT

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