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YOU CAN'T ALWAYS GET WHAT YOU WANT (BUT IF YOU TRY SOMETIMES, YOU MIGHT GET WHAT YOU NEED)[1]

— Joel Nitikman, Partner in the Tax Department of the Vancouver office of Fraser Milner Casgrain LLP

You Can't Get What You Want

One might think that it would go without saying, but obviously not, that the Tax Court of Canada is neither a court of equity nor a section 96 court. That is, it is not created, continued, or recognized by section 96 of the *Constitution Act, 1867*.[2] Rather, it is a "statutory court", created under the authority of section 101 of that Act. This means, among other things, that its powers are limited to those granted to it by the *Tax Court of Canada Act*, the *Income Tax Act* (the "ITA"), and other relevant statutes, and to those that are necessarily inherent in or implied by those statutes or that are necessarily incidental to the proper operation of itself as a court.[3]

Nothing in any of those powers permits the Tax Court to invalidate, vacate, or dismiss an assessment issued by the Minister of National Revenue (the "Minister") to a taxpayer merely because of the improper actions of the Canada Revenue Agency (the "CRA"). This was brought home forcefully to the taxpayer in *Ereiser v. Canada*, 2013 DTC 5036 (F.C.A.), February 4, 2013, which upheld an unreported, interlocutory judgment of Justice Hershfield of the Tax Court of Canada. To call the CRA's actions in this case Kafkaesque would be an understatement, yet the taxpayer still did not get what he wanted.

From at least 1996 to 1998, Mr. Ereiser carried on a business called "Kerrobert Satellite and Cellular". It appears he used proper due diligence to keep track of his financial affairs and file income tax returns. His reported net income in those three years varied from $20,000 to $68,000, but could have been less if he had deducted all available expenses.

In 2003, for reasons that are not clear, a CRA criminal investigator proposed to indict Ereiser on criminal tax evasion charges and to reassess him for tax, including gross negligence penalties, by suggesting that his income was really over $1.7 million.

It appears that the investigator tried to withdraw somewhat from his initial position, as he and other CRA investigators later suggested that Ereiser should plead guilty to criminal charges but with a reassessment such that his net amount of tax payable would be only $80,000, based on income of $28,000 per year.

As it happens, the CRA never prosecuted the taxpayer. In fact, the investigator conceded that the proposed reassessment was excessive. However, the CRA continued to tell the taxpayer that he should plead guilty.

The taxpayer did not plead guilty to anything. The Minister reassessed Ereiser without correcting the errors to which the investigator had already admitted. This was even more curious, given that the reassessment was issued by the investigator or his colleagues. Ereiser objected to the reassessments. In apparent breach of the Appeals Renewal

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a Wolters Kluwer business

Initiative, the investigators interfered with the objections by telling the Appeals Officer, falsely, that the taxpayer was under criminal investigation. Even after the investigators told the Appeals Officer that they had lied, the objections were not assigned to a different Appeals Officer.

It appears that the CRA either conceded or at least the Court simply assumed that the CRA never separated its audit and investigatory functions. Thus, the reassessments were based on evidence obtained in breach of the taxpayer's Charter rights.

The Appeals Officer appears to have confirmed the reassessments, although the basis on which he did so is not clear. The taxpayer appealed the reassessments to the Tax Court. In his Notice of Appeal, he prayed for the following relief:

> (a) The reassessments should be vacated because they were issued as the result of misfeasance in public office on the part of the investigators. The misfeasance in public office was the authorization of a grossly inflated reassessment to coerce a guilty plea to a criminal charge.
>
> (b) In the alternative, the reassessments should be vacated because each of them was made outside the normal reassessment period for the relevant year, and the Minister cannot prove by admissible evidence that the normal reassessment period did not apply.
>
> (c) In the further alternative, the reassessments should be vacated because Mr. Ereiser did not have unreported income in 1996, 1997 or 1998.

The Crown moved to strike out parts of the Notice of Appeal, including any portions dealing with the CRA's misconduct.

Hershfield J allowed the Crown's motion in part. Although a motion to strike a pleading should be granted only if it is "plain and obvious" that it has no chance of success, he struck out the portions seeking the vacating of the reassessments on the basis of misfeasance in public office. Hershfield J held that the Tax Court had no jurisdiction, inherent or otherwise, to deal with any CRA misconduct in the process leading up to an assessment. The Court's jurisdiction is limited by section 171 of the ITA, which permits the Court only to dismiss the appeal or allow it, and if it is allowed, to vacate the reassessment entirely, determine the amount to be paid by the taxpayer, or to order the Minister to reassess in accordance with the reasons for judgment.

On the other hand, Hershfield J also rejected the Crown's argument that the "plea bargain" put forward by the Crown to the taxpayer was a type of "without prejudice" negotiation and permitted the taxpayer to raise those facts, not for the purpose of vacating the reassessments directly, but with a view to proving that the Minister had not really made any assumptions relating to the amount of income earned by the taxpayer, thus affecting who carried the onus of proof on that issue.

Both parties appealed, but the Federal Court of Appeal dismissed both appeals.

With regards to the taxpayer's appeal, the Court of Appeal affirmed Hershfield J in holding that the Tax Court has no jurisdiction to vacate an assessment merely because the Minister issued it under conditions amounting to misfeasance in public office. Citing earlier jurisprudence from the Court of Appeal, Justice Sharlow held that:

> . . . the role of the Tax Court of Canada in an appeal of an income tax assessment is to determine the validity and correctness of the assessment based on the relevant provisions of the *Income Tax Act* and the facts giving rise to the taxpayer's statutory liability. Logically, the conduct of a tax official who authorizes an assessment is not relevant to the determination of that statutory liability. It is axiomatic that the wrongful conduct by an income tax official is not relevant to the determination of the validity or correctness of an assessment.

The Court of Appeal also held that wrongful conduct on the part of the CRA does not make evidence obtained by it inadmissible, unless the conduct relates to the gathering of the evidence. Here it did not.

Finally, the Court of Appeal dismissed the Crown's cross-appeal and held that Hershfield J was correct in holding that in this case, the CRA's misconduct may support an allegation that the Minister never did make any assumption as to the amount of income the taxpayer earned, thereby placing the onus of proving the amount of his income on the Crown.

The Rolling Stones Lived in England

It is very interesting to note that at the same time this case was being decided, the Upper Tier Tribunal ("UTT") in England came to exactly the same conclusion. In *Foulser v. HMRC*, [2013] UKUT 038 (25 January 2013), the taxpayer lost a case on a certain tax issue. A further hearing was to be held to determine the amount of tax owing. While

travelling to the First Tier Tribunal ("FTT") courthouse for that hearing, the taxpayer was arrested for tax evasion.

Ultimately, the taxpayer applied to the FTT to disbar Her Majesty's Revenue and Customs from taking part in the FTT proceedings, on the basis that to allow it to do so would amount to an abuse of process.

On appeal, the UTT held that there are two situations in which abuse of process may arise: first, a party may behave in a way which makes a fair hearing procedurally difficult or impossible. In that situation, even a statutory court has inherent, or (as it now seems to be called) implied, jurisdiction to control its own process so that the other party is granted a fair hearing. The UTT went so far as to hold that the FTT had the jurisdiction to debar a party from taking part in an appeal altogether if no lesser order would provide procedural fairness to the other party (although that would be an exceedingly rare case).

On the other hand, if the allegation is that a party's misconduct leads to a substantive unfairness against the other, such that the proceeding should be stopped for that reason and the assessment vacated, not because of some procedural difficulty, but on more or less equitable grounds, then the FTT (like the Tax Court of Canada) is a statutory court with no inherent or implied power to vacate the assessment or stop the proceeding. The taxpayer is limited to seeking judicial review in the UTT or the High Court (or in Canada, in the Federal Court).

But You May Get What You Need

This leads one to the decision in *JP Morgan Asset Management (Canada) Inc. v. Canada (National Revenue)*, 2012 DTC 5120 (F.C.), decided by Kevin R. Aalto, Esquire, case management judge. JP Morgan ("Canco") is a Canadian corporation which is resident in and carries on business in Canada. It is a subsidiary of a US corporation, JP Morgan Asset Management Holdings Inc. ("Holdings"), which itself is a wholly owned subsidiary of another US corporation, JP Morgan Chase & Co. ("JP Morgan US").

Holdings has a US subsidiary, JP Morgan Asset Management (Asia) Inc. ("JPAM"), which in turn is the parent of JF Asset Management Inc. ("JFAM"), a Hong Kong corporation.

Canco provides investment advisory services to its Canadian clients. Canco refers its Canadian clients to other companies in the JP Morgan group, including JFAM, to obtain investment advice services.

Canco's clients pay it fees. Canco pays 75% of those fees to other members of the group.

The Minister assessed Canco for Part XIII tax (the "Assessments") in respect of the fees it paid to JFAM for all its fiscal periods from December 31, 2002 to December 31, 2008.

Canco applied to the Federal Court for an order in the nature of *certiorari* quashing the Minister's decision to assess. Specifically, the Notice of Application prayed for the following relief:

> (a) an order in the nature of *certiorari* quashing the decision of the Minister to assess Canco under Part XIII;
>
> (b) alternatively, an order that the decision to issue the Assessments was an invalid and unlawful exercise of a statutory power exercised for an improper purpose, such that Canco is entitled to an order setting aside the Assessments.

The Minister argued that the application was a collateral attack on the Assessments and, hence, outside the Court's jurisdiction, pursuant to section 18.5 of the *Federal Courts Act* (and incidentally, exactly as described by the Court in *Ereiser)*.

The case management judge held that as the Assessments were under subsection 227(10) of the ITA, which says that the Minister "may" assess, and as Canco was asserting that the Minister had contravened his own policies in assessing, then based on *Canada v. Addison & Leyen Ltd.,* 2007 DTC 5365 (S.C.C.), the Federal Court retained the jurisdiction to review the Minister's decision to assess in these circumstances.

The case management judge referred to the Federal Court's earlier decision in *Chrysler Canada*. In that case,[4] the Court observed:

> [17] As argued by the Applicant it does not challenge the ability of the Minister to issue the Reassessments provided that those Reassessments are issued on the basis of a discretion that is consistent with the Prior Letters. Thus, the Application does not seek to challenge the correctness of the Reassessments which result in the alleged double taxation, it only seeks to judicially review the Minister's exercise of discretion in determining to issue the Reassessments contrary to the Prior Letters.

The case management judge held that the same reasoning applied to Canco's case, because Canco was seeking only

judicial review of the Minister's decision to assess, and that "no attack on the reassessments is in play".

The Crown has appealed this decision. Undoubtedly, the Crown will argue that as the Notice of Application specifically asks for the Assessments to be "set aside", the application cannot stand in light of section 18.5.[5] Canco will argue that the following paragraphs from *Johnston*[6] open the door for the remedy it is seeking:

> [55] It does not seem to me that the Supreme Court of Canada has ruled out a judicial review by the Federal Court of a decision to assess (or reassess) pursuant to subsection 152(4) of the *Income Tax Act* (which also refers to "the Minister may . . . make an assessment, reassessment or additional assessment") but rather has limited it to a remedy of last resort.
>
> [56] It therefore seems to me that while this Court has the exclusive jurisdiction to hear appeals from assessments (or reassessments) arising under the *Income Tax Act*, it would appear that the Federal Court has the jurisdiction to deal with determinations of questions of law or declarations related to whether an individual has been denied his or her exemption as provided by section 87 of the *Indian Act*. As a remedy of last resort, judicial review by the Federal Court of a decision by the Minister to reassess an individual pursuant to subsection 152(4) of the *Income Tax Act* based on a determination that the exemption under section 87 of the *Indian Act* does not apply, may also be available. However whatever remedies may be available at the Federal Court is not a matter for this Court to determine.

So Canco does not yet have what it wants. But at the moment, it has certainly gotten what it needs.

A number of tax lawyers from Fraser Milner Casgrain LLP write commentary for CCH's Canadian Tax Reporter *and sit on its Editorial Board as well as on the Editorial Board for CCH's Canadian* Income Tax Act with Regulations, Annotated. *Fraser Milner Casgrain lawyers also write the commentary for CCH's* Federal Tax Practice *reporter and the summaries for CCH's* Window on Canadian Tax. *Fraser Milner Casgrain lawyers wrote the commentary for* Canada–U.S. Tax Treaty: A Practical Interpretation *and have authored other books published by CCH:* Canadian Transfer Pricing *(2nd Edition, 2011);* Federal Tax Practice; Charities, Non-Profits, and Philanthropy Under the Income Tax Act; *and* Corporation Capital Tax in Canada. *Tony Schweitzer, a Tax Partner with the Toronto office of Fraser Milner Casgrain LLP, and a member of the Editorial Board of CCH's* Canadian Tax Reporter*, is the editor of the firm's regular monthly feature articles appearing in* Tax Topics.

For more insight from the tax practitioners at Fraser Milner Casgrain LLP on the latest developments in tax litigation, visit the firm's Tax Litigation blog at http://www.canadiantaxlitigation.com/.

Notes:

[1] According to Wikipedia, "You Can't Always Get What You Want" is a song by the Rolling Stones on their 1969 album *Let It Bleed*. Written by Mick Jagger and Keith Richards, it was named as the 100th greatest song of all time by *Rolling Stone* magazine in its 2004 list of the "500 Greatest Songs of All Time".

[2] 30 & 31 Victoria, c. 3 (U.K.).

[3] See the discussion on this point in *Canada (National Revenue) v. RBC Life Insurance Company*, 2013 FCA 50 at paragraphs 33–36, and its companion case *Canada (National Revenue) v. Lordco Parts Ltd.*, 2013 FCA 49. See also *HMRC v. Abdul Noor*, [2013] UKUT 71 (T.C.C.) (14 February 2013), which held that the FTT, as an appellate court with no supervisory jurisdiction, had no jurisdiction to consider a taxpayer's claim that he was entitled to value-added tax input tax credits on the basis of the equitable doctrine of "legitimate expectations".

[4] *Chrysler Canada Inc. v. Canada*, 2008 DTC 6452 (F.C.).

[5] See *Rusnak v. Her Majesty the Queen*, 2011 DTC 5099 (F.C.A.).

[6] *Johnston v. Her Majesty the Queen*, 2009 DTC 1198 (T.C.C.).

2013 FEDERAL BUDGET DATE — MARCH 21, 2013

The 2013 federal Budget is being tabled on Thursday, March 21, 2013 at approximately 4:00 p.m. The government's Budget documents will be posted on CCH's federal income tax News Tracker and GST News Tracker as soon as the embargo is lifted that day. CCH, in partnership with Fraser Milner Casgrain LLP, will be in the lock-up that day with a team of tax experts to provide commentary on the tax provisions contained in the Budget. This commentary, as well as the government's Budget plan, will be published in CCH *Special Report* No. 070H, which will be sent to all *Canadian Tax Reporter* subscribers (whether print, DVD, or online product) as part of the subscription. Additional orders may be placed by calling (416) 224-2248 (toll-free 1-800-268-4522), by faxing (416) 224-2243 (toll-free 1-800-461-4131), or by emailing cservice@cch.ca.