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SETTLEMENT OFFERS: *CIBC WORLD MARKETS INC. V. HER MAJESTY THE QUEEN*

— *Jacques Plante, Fraser Milner Casgrain LLP*

On January 10, 2012, the Federal Court of Appeal ("FCA") released its decision in *CIBC World Markets Inc. v. Her Majesty the Queen* (2012 GTC 1011, 2012 FCA 3). This unanimous judgment reduces the effectiveness of settlement offers under sections 403 of the *Federal Courts Rules* and 147 of the *Tax Court of Canada Rules (General Procedure)*.

In this matter, prior to the proceedings in the Tax Court of Canada ("TCC"), CIBC World Markets Inc. ("CIBC") sent an offer of settlement to the Minister. Under the proposed settlement, the Minister would issue a reassessment allowing CIBC to receive 90% of the input tax credits ("ITC") it claimed on its GST return. The offer had no expiry date and was available to be accepted until the judgment of the FCA was rendered. CIBC was unsuccessful at the TCC in arguing that it was entitled to make a second claim for ITCs using a different allocation methodology in respect of the same tax years to obtain ITCs at a higher level than those originally claimed. The TCC held that CIBC was not entitled to make such claims and CIBC then appealed to the FCA.

The FCA allowed the appeal and ordered the Minister to reassess CIBC such that 100% of the ITCs claimed by CIBC in its GST return would be reimbursed by the Minister. Consequently, CIBC requested the FCA to issue a direction to the assessment officer to award it costs at a normal level, in accordance with Tariff B of the *Tax Court of Canada Rules (General Procedure)*, plus disbursements and GST/HST for the period up to the date of the offer of settlement. CIBC also requested 80% of solicitor–client costs plus disbursements and GST/HST for the period starting from the date of the offer of settlement through to the date of the FCA's judgment.

The FCA began its analysis by rejecting the application for higher than normal costs in the FCA since the offer of settlement was only made before the TCC decision and was not reasserted while the appeal to the FCA was pending, despite the fact that the offer to settle was never withdrawn. The Court then limited the question at issue as to whether higher than normal costs should be awarded regarding the proceedings in the TCC.

Under Rule 147(1) of the *Tax Court of Canada Rules (General Procedure)*, the TCC may determine the amount of the costs of all parties involved in any proceeding. In order to determine these costs, the TCC may consider any offer of settlement made in writing.[1] Adverse cost consequences may be triggered when, based on the TCC's decision, it turns out that an offer to settle should have been accepted. However, the FCA stated that there is an implicit precondition to Rule 147(3)(*d*): only offers which, as a matter of law, could have been accepted can trigger costs consequences. For example, if the Minister could not accept an offer of settlement due to some legal disability, adverse cost consequences are not available to the offering party.

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The Minister's position is that it may only accept an offer of settlement that is supported by the facts and the law and that it was unable to do so in this case because it cannot accept any offer that would reflect an arbitrary compromise on quantum. In this case, accepting CIBC's offer to issue a reassessment allowing 90% of the ITCs claimed in its GST return would be a completely arbitrary compromise, as this was not a legally or factually possible outcome of the proceeding. In the Minister's view, if CIBC was correct, the TCC would have allowed the ITC amount it claimed in its entirety. Contrarily, if the Minister was right, the TCC would have dismissed the appeal.

The FCA agreed with the Minister's position that based on the facts and the law, it was not supportable for a judge to grant CIBC 90% of the ITCs it claimed since the issue was an "all or nothing" question of statutory interpretation; the FCA had to confirm or reject the Minister's assessment in its entirety.[2] The FCA stated that it was bound by its decision in *Galway*,[3] where Jackett C.J. affirmed that the Minister "cannot assess for some amount designed to implement a compromise settlement".[4] Furthermore, the FCA stated that the *Excise Tax Act* does not contain a provision allowing the Minister to make settlements solely on the basis of compromise and reiterated that there is no legislative provision that overrules *Galway*. Thus, the FCA found that, as a matter of law, the Minister could not have accepted CIBC's offer of settlement.

This judgment limits the effectiveness of Rules 403 of the *Federal Courts Rules* and 147 of the *Tax Court of Canada Rules (General Procedure)*. The objective of these sections is to create an incentive for litigants to seriously consider an offer of settlement. However, the principle stated in the present case allows the Minister to argue that it should not be penalized with additional costs from unaccepted offers of settlement where the offer of settlement cannot be supported by the facts as they were known at the time. This ignores the fact that in the majority of tax cases, some facts can only be revealed through testimony.

Also, amounts offered by taxpayers to the Minister to settle a case out of court are generally calculated based on an evaluation of the merits of the case. In this specific case, CIBC probably thought it had a strong case and offered the Minister a settlement for reassessment in order to refuse 10% of the ITCs it claimed. This appears to be a fairly common strategy by appellants in tax litigation cases as a taxpayer rarely offers the Minister a settlement that will have the effect of quashing the whole assessment, as it is anticipated that it will likely be refused by the Minister. However, pursuant to this decision, the FCA might have granted CIBC's motion for additional costs had the latter presented the Minister with an offer to settle that accepted 100% of the ITCs as it would not have been a compromise settlement.

The FCA's decision is interesting in light of a recent judgment in the Ontario Superior Court of Justice ("OSCJ"), *Omers Realty Corporation v. Minister of Finance (Costs)* (2012 ONSC 159). In *Omers*, the taxpayer claimed it had made a settlement offer that met the requirements of a Rule 49 offer when it offered to settle all the matters in dispute between the parties and not solely the matters before the Court.[5] The crux of the offer to settle was that tax would be paid on four of the 31 transactions in issue and the Minister would be required to vacate the assessments issued in respect of all of the transactions that were the subject of the pending appeals to the OSCJ (a total of 15 appeals). The taxpayer claimed that the Minister would have been in a better position if he had accepted the offer to settle as it would have resulted in $1.4 million being paid in tax to the Minister rather than no tax owing, which was the finding of the Court. The OSCJ found that the principle issue was whether the taxpayer was a Crown agency and that this was an all or nothing question to be answered by the Court. The OSCJ commented that "a settlement is supposed to be an accommodation which allows the parties to resolve their differences without going to court". Additionally, the OSCJ had concerns about parties using an offer of settlement in an all or nothing case as a form of intimidation because of the threat of increased costs being awarded by the Court.

Hence, it appears as though the jurisprudence is moving towards creating a clear requirement for a principled basis for settlement in order for such settlement offers to have any relevance to or impact on cost awards. The parties to a dispute will have to be careful when drafting settlement offers if they hope to trigger any additional cost consequences after a successful hearing.

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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.

Notes:

[1] *Tax Court of Canada Rules (General Procedure)*, Rule 147(3)(*d*).

[2] See also *Omers Realty Corporation v. Minister of Finance (Costs)*, 2012 ONSC 159, for a recent consideration of this issue under the Ontario *Rules of Civil Procedure*.

[3] *Galway v. Minister of National Revenue*, 74 DTC 6355 (FCA), 1974 1 F.C. 600 (C.A.).

[4] Ibid.

[5] *Rules of Civil Procedure*, Rule 49.

REQUIREMENT TO PROVIDE SOCIAL INSURANCE NUMBER/ BUSINESS NUMBER ON T5

The CRA was asked whether individuals and businesses are required to provide their social insurance numbers ("SIN") or business numbers ("BN") to an entity that is required to complete an information slip.

Under s. 162(7), every person who fails to file an information return as required by the Act or the *Income Tax Regulations* is liable to a penalty (see also s. 162(7.01) for late-filing penalties). Under s. 201(1) of the *Income Tax Regulations*, any person making payments to investors holding equity instruments must file the required information returns, namely, T5 slips and a related T5 summary. Subsection 237(1.1) requires individuals and businesses to provide their SINs or BNs upon the request of any person required to make an information return under the Act or the *Income Tax Regulations*. Under s. 237(2), the person who is required to make the information return must make reasonable efforts to obtain the necessary SINs or BNs, and under s. 162(6), any individual or business that fails to provide its SIN or BN is liable to a penalty.

See also Information Circular IC82-2R2 "Social Insurance Number Legislation That Relates to the Preparation of Information Slips" (November 20, 1992), CRA Document No. 2007-0240191C6 "RRSP registration — SIN requirement" (June 21, 2007), CRA Document No. 2005-0148331E5 "Disclosure of social insurance number" (November 2, 2005), and CRA Document No. 9414986 "Social insurance number requirement" (August 9, 1994).

— External Technical Interpretation, International and Trusts Division, November 14, 2011, Document No. 2011-0419251E5

VOLUNTEER REWARDS PROGRAM

The CRA was asked whether compensation received in the form of rewards points by a volunteer for services rendered is taxable under the Act.

A ski club offered a rewards program for its members who volunteer at the ski club. The number of rewards points allocated to a member depends on the type of activity or event held at the ski club and the shift, schedule, and position assumed by the volunteer. Generally, a member is awarded five rewards points for each hour of volunteer time. One reward point equals $1. Rewards points may be redeemed at the member's option for merchandise at the ski club store, extended trips and bus day trips offered by the ski club, lessons and programs offered by the ski club, and registrations at the ski club. Rewards points are non-transferable, non-refundable, and have no cash value.

The CRA stated that it recognizes that many tasks undertaken by volunteers are not performed entirely gratuitously. Some volunteers receive sums of money or gift certificates for goods or services in consideration for services rendered.

Generally, depending on the circumstances, an amount received by an individual as compensation for services will be taxable either as income from an office or employment or as income from a business.

Where an employment relationship exists between the volunteer and the organization, the compensation received by the volunteer would generally be taxable pursuant to s. 5 or 6 of the Act. The determination of whether the volunteer is an employee or an independent contractor is made with reference to a fourfold test developed in the case law, namely with reference to the control exercised by the entity, the tools used in performing the services, the chance of profit of the individual, and the individual's risk of loss in performing the services (see, for example, *Wiebe Door Services*, 1986 3 F.C. 553, *Sagaz Industries Canada Inc.*, 2001 SCC 59, and *Integrated Automotive Inc.*, 2011 TCC 468).

Where no employment relationship exists, compensation received by the volunteer in excess of a nominal amount for services rendered to another party may be business income. Subsection 81(4) provides an exemption from taxation for the first $1,000 received by an individual from a government, municipality, or other public authority for duties performed as a volunteer in certain emergency situations. There is no other provision in the Act that would operate to exempt from tax amounts received by a volunteer for services rendered. However, the CRA stated that, where the compensation paid to the volunteer is nominal, there will be no income tax consequences to the volunteer (i.e., the amount received would not be taxable).

In the CRA's view, to be considered nominal, the amount:

- would generally be less in comparison to what it would have cost to have the same duties performed by an employee or independent contractor;
- would not likely be enough to induce the provision of services by the volunteer (i.e., it would not influence the individual's decision to volunteer);
- would not reflect the fair market value of the services rendered; and
- would not reflect the amount of work performed or the quality of the services provided.

The CRA stated that this determination would be made on a case-by-case basis, considering all of the relevant facts.

See also CRA Document No. 2010-0353041E5 "Loyalty programs" (June 15, 2010), CRA Document No. 2008-0276851E5 "Volunteer firefighters" (July 7, 2009), CRA Document No. 2009-0323331E5 "Volunteer compensation" (December 1, 2009), CRA Document No. 2006-0178011E5 "Stipend paid to volunteers" (September 14, 2006), and CRA Document No. 2000-0005985 "Amounts received by volunteers" (March 13, 2000).

— *Internal Technical Interpretation, Ontario Corporate Tax Division, November 24, 2011, Document No. 2011-0400471E5*

NEW SMART CHART ADDED

A new Smart Chart called "Personal Income Tax Credits" has been added to the collection of Smart Charts that are located on CCH Online, accessed from the table of contents immediately following the *Canadian Tax Reporter*. The Smart Chart is an interactive tool that allows the user to create a customized chart showing only the information needed based on type, year, and jurisdiction. This new Smart Chart sets out the tax credits (refundable and non-refundable) that can apply to individuals across all the jurisdictions in Canada. The credits are organized by categories and contain information relating to five years. Check out this new chart as well as the personal and corporate tax rates Smart Charts that are available.

RECENT CASES

Capital gains exemption could be applied only against aggregate value of farm property, not property by property

The deceased owned three farm properties at the time of his death. In his will, he bequeathed one of the farms to his niece, with the capital gains tax to be paid from the residue of the estate. He bequeathed another to the applicants, with the capital gains tax to be paid by them. The third farm fell into the residue of the estate. The respondent, AS, the deceased's nephew, was the beneficiary of the residue of the estate. The will directed that all taxes, including capital gains tax, be paid from residue unless otherwise directed by the will. The applicants applied to the Ontario Superior Court of Justice for an order determining the extent of their obligation to pay the capital gains tax owing by the estate. The applicants' position was that they should calculate the percentage gain on their property from the total gain on the three properties, and that they should then receive credit for a proportional share of the deceased's capital gains exemption for qualifying farm property. AS's position was that the measure of taxes attributable to the property bequeathed to the applicants was the difference between the taxes that were payable with that property included in the calculation and those that would have been payable but for that property.

The Court found that the applicants' position was correct. AS's suggestion that there was a capital gains tax attributable or caused by the gain on a certain property without the farm property exemption deduction was impossible under the capital gains tax scheme or return. The deduction could only be applied against an aggregate value, and not piecemeal, property by property. It was unfortunate that the residue was cash poor, but to accept a modified or hybrid capital gains calculation would be an "unreasonable forcing of the language" of the will.

¶47,959, *Fournie*, 2012 DTC 5011

Application for certification as class action statute-barred

The taxpayer and about 900 others participated in a tax scheme in which they purchased time-shares in a resort and then donated both cash and time-shares to Canadian athletic associations in anticipation of receiving charitable tax credits for their charitable donations. Included in the promotional material for the time-share program was a tax opinion prepared by the defendant law firm, which stated that it was unlikely that the Canada Revenue Agency (the "CRA") could successfully deny the tax credits. In 2004, the CRA disallowed the anticipated tax credits in their entirety. After seeking legal advice, a test case was settled, and the CRA allowed the participants to receive a tax credit for the cash portion of the donation, but denied the greater part based on the value of the donated time-shares. The taxpayer commenced an action in the Ontario Superior Court of Justice in 2009, based on negligence and negligent misrepresentation, and then applied for certification of his action as a class action.

The taxpayer's action was dismissed. The Court found that the five criteria for a class action were satisfied: (a) the pleadings disclosed a cause of action; (b) there was an identifiable class; (c) the claims of the class members raised common issues of fact or law; (d) a class proceeding would be the preferable procedure; and (e) there was a representative plaintiff who would adequately represent the interests of the class without conflict of interest, and who had produced a workable litigation plan. However, the Court found that the action was statute barred, as it was commenced more than two years after the claim was discovered. The taxpayer and other class members knew or ought to have known in 2004, when their tax credits were denied, that they had a claim against the defendant. At that time, and not later than 2006, when counsel was retained to appeal the tax assessments, the class members knew or ought to have known the material facts on which the negligence or negligent misrepresentation claims against the defendant were based.

¶47,960, *Lipson*, 2012 DTC 5013

CRA unreasonably denied relief to estate — Executors denied key information by third parties

The executors for the taxpayer's estate (the "Estate") brought an application for judicial review of a Canada Revenue Agency ("CRA") decision, where they had requested relief from interest and penalties that were applied against the deceased taxpayer's 2003 final tax return, for a late-filed tax return that included previously unreported income. The return included $45,361 payable to the Estate as sole beneficiary of the estate of her predeceased spouse, G. The executors for the Estate argued that litigation between themselves and the executors of G's estate impeded them from accessing two T4RSP slips payable to the Estate, and that the CRA was uncooperative when contacted about the affairs of the Estate. There was also confusion over the names and details provided in the slips when they were finally provided to the executors of the Estate.

The taxpayer's application was allowed. The CRA made an unreasonable decision to deny relief to the Estate, as the executors were denied key information by third parties that necessitated a delay in filing the Estate's returns in a timely fashion.

¶47,962, *Kelley*, 2012 DTC 5015

Minister's refusal to waive tax, penalties, and interest on excess RRSP contributions reasonable

In 2008, the taxpayer moved to Montreal from the United States for employment reasons. The taxpayer sought and received conflicting advice from both the Canada Revenue Agency (the "CRA") and his own financial advisers about whether he was entitled to make an RRSP contribution for 2008. Notwithstanding the conflicting advice, the taxpayer made an RRSP contribution of $18,000 in March 2008, and a further contribution of $4,500 in January 2009. By letter dated September 29, 2009, the CRA advised the taxpayer that he had to file a T1-OVP tax return for 2008, and that failure to do so within 90 days of the 2008 year end would result in late-filing penalties, as well as arrears of interest. The taxpayer was also advised in that letter that a tax on excess RRSP contributions would be levied for each month that the excess contributions remained in the RRSP. Finally, he was advised that a tax would continue to be levied on the excess contributions. On January 19, 2010, the applicant filed a T1-OVP tax return for 2008. The Minister assessed the taxpayer for the 1% per month tax on excess RRSP contributions and imposed penalties and interest. The Minister subsequently refused to waive the tax, penalties, or interest. The taxpayer applied to the Federal Court for judicial review.

The taxpayer's application was dismissed. The Court found that the Minister's decision was reasonable. The onus was on the taxpayer to know the law. Furthermore, there was no reasonable explanation as to why he chose to follow the advice that was favourable to his tax position instead of the advice that was unfavourable. The Minister's determination that the taxpayer did not take reasonable steps to eliminate the excess contributions was also reasonable. The taxpayer did not take any steps until some nine months after year end, despite the CRA's warnings. The Court also found that there were no grounds to interfere with the Minister's decision not to waive the penalties and interest.

¶47,964, *Kapil*, 2012 DTC 5017

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