Tax Court Round-Up: Reassessment and Appeal Limits

Suppose your client has a large tax loss in a year and the CRA allows only part of it, reducing income for the year to nil. Can your client appeal? What should the client do? Or what if your client has appealed an assessment to the Tax Court of Canada and the CRA issues a reassessment of that taxation year. Must your client start over and object to the new reassessment? Suppose you were negligent in preparing your client's tax return several years ago. Can the CRA now reassess that year even if it's statute-barred, based on your error?

Since the practice of tax accounting relies on laws that are always being revised or challenged (and their corresponding precedents), keeping abreast of the latest significant decisions coming out of the Tax Court of Canada is vital to keeping informed as a tax practitioner. As such, this edition of the Tax Newsletter summarizes some recent decisions of the Tax Court of Canada dealing with reassessments and appeal limits, to give you insight into the above questions.

Bérubé c. La Reine, 2014 CCI 304 **(Tardif) — You can't appeal an assessment that says you don't owe tax, but you can claim the loss in later years**

This case deals with an issue that comes up occasionally: you can't appeal a nil assessment.

In 2012, the appellant sought to use an allowable business investment loss generated in the 2001 and 2004 tax years. The CRA allowed the allowable business investment loss (ABIL) to reduce 2002, 2003, 2004, 2005, and 2007 taxable income to nil, but that had not used up the full amount of the loss. (2001 was not included because in 2012 the 2001 tax year was too old for adjustment using the taxpayer-relief rule in *ITA* s. 152(4.2).) In 2013, the taxpayer applied to the Court to reopen 2002 on the basis that the loss really arose then, not in 2001, so that he could apply the remaining $500,000 of loss to 2001, 2000, and 1999.

The main obstacle facing the taxpayer was the fact that the CRA's reassessment of 2002, based on the taxpayer's initial 2012 adjustment request, had reduced 2002 tax to nil. As a result, he could not challenge the 2002 nil assessment to show that the loss occurred in that year and not in the 2001 year.

> [50] It is thus clearly established in the jurisprudence that a taxpayer can not file an appeal against a nil assessment for the simple reason that an assessment according to which no tax is payable is not an "assessment" within the meaning of the *ITA*.
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> [50] Il est donc clairement établi dans la jurisprudence qu'un contribuable ne peut interjeter appel d'une cotisation néant pour la simple raison qu'une cotisation selon laquelle aucun impôt n'est payable n'est pas une « cotisation » au sens de la LIR.

A taxpayer is not without a remedy in cases like this where a tax year is statute-barred or there is a nil assessment. As the court said, the taxpayer still had the right to claim the loss against future year capital gains. (The ABIL was lost, though, because after 10 years an ABIL can be used only against capital gains. See *ITA* 111(8)"non-capital loss"E(c).

> [78] Nevertheless, he can, faced with subsequent real assessments (which are not reduced to zero), appeal from those … with the goal of being able to deduct his losses incurred in 2002 against those later tax years, and this, subject obviously to statutory limitation periods. [Author's translation from the French.]
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> [78] Toutefois, il pourra, à l'encontre de véritables cotisations ultérieures (qui ne sont pas réduites à zéro), appeler de celles-ci … afin de pouvoir déduire ses pertes subies en 2002 sur ces années d'imposition ultérieures, et ce, sous réserve évidemment des délais de prescription.

Another option open to a taxpayer faced with a nil assessment is to ask for a loss determination under *ITA* s. 152(1.1). Depending on the circumstances, the CRA may or may not have a legal obligation to issue one. There is a right to appeal a loss determination: *ITA* s. 152(1.2). It may not help you remedy tax payable for statute-barred years, though.

Ford v. Canada, 2014 FCA 257 — A later reassessment invalidates an earlier one

Ian and Norma Ford took part in an art donation scheme. They were reassessed in 2002 and 2003 and filed objections. As often happens with these donation schemes, the appeal process took a long time. About 10 years later, in 2012, the CRA reassessed the participants in the program to remove the gross negligence penalty and to eliminate a related capital gain, but restricted the donation credit to the amount the Fords had actually paid into the program. The Fords appealed on the basis that the CRA's 2012 reassessment was void because it hadn't been made "with all due dispatch" as required by the objection rule in *ITA* subsection 165(3).

As Justice Webb pointed out, if the Fords won their court appeal, the result would be that the 2003 reassessments, which were *worse* than the 2012 reassessments, would be reinstated:

> [16] Each time that Ian Ford and Norma Ford were reassessed in relation to a particular taxation year, such reassessment nullified the previous assessment or reassessment that had been issued in relation to that year … If a reassessment is vacated, then the previous assessment or reassessment for that same taxpayer for that same year is no longer nullified and such immediately preceding assessment or reassessment is reinstated. For example, if the reassessment issued on April 27, 2012 for the 2001 taxation year of Norma Ford were to be vacated, the reassessment issued on September 29, 2003 for the 2001 taxation year of Norma Ford would be restored.
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> [17] …, these reassessments reduced the tax liability of Norma Ford and Ian Ford by deleting the gross negligence penalties and the taxable capital gain that they had reported in relation to the donation of art. If these reassessments were to be vacated, then the immediately preceding reassessment issued for each year would be restored and their tax liability would be increased, as the charitable donation tax credit would still be reduced from the amount as originally claimed in their tax returns, but the gross negligence penalties and taxable capital gains related to the donated art would be restored. …

For a large corporation (more than $10,000,000 of taxable capital), the rule that a prior reassessment is invalidated by later reassessment can raise other trouble. Large corporations must specify the issues for appeal, the amounts in dispute and the facts and reasons relied on. (See *ITA* ss. 165(1.11) and 169(2.1).) So, if the reassessment changes, the taxpayer may need to file a new objection rather than appeal directly to the Tax Court. The mining company Rio Tinto faced this problem recently, but the court allowed it to amend its notice of appeal. (See *Rio Tinto Alcan inc. c. La Reine, 2014 CCI 288* (Favreau).)

Note that when (as here) the CRA issues a reassessment while an objection is outstanding for the taxation year, then the taxpayer has the option to appeal directly to the Tax Court rather than file a new objection to the reassessment: *ITA* s. 165(7).

Vachon c. Canada, 2014 CAF 224 (FCA) **— For reopening statute-barred tax years, negligence of the taxpayer, not his accountant, is critical**

Despite the normal three-year reassessment period, the CRA can reassess at any time if it can show that your client or the person filing the return "made any misrepresentation that is attributable to neglect, carelessness or wilful default": *ITA* s. 152(4)(a)(i). In *Vachon*, the taxpayer had entrusted his accountant with amounts to be used to pay taxes. The accountant stole the money. The Tax Court judge blamed the taxpayer for trusting his "con artist" accountant and not taking greater care to monitor him.

On appeal, the Federal Court of Appeal confirmed that "negligence of an accountant is not the factor that allows one to by-pass the time limit under 152(4)(a)(i) of the *ITA*. It is the negligence of the taxpayer at the time of filing that must be analyzed." Because "the judge [did] not specify which facts were wrongly declared in the tax return, nor what the appellant knew or should have known on this subject at the moment of their declaration," the case was sent back to the Tax Court to be re-tried (paragraphs 4 and 7). [Author's translation from the French.]

> [4] Dans *Aridi c. La* Reine, 2013 CCI 74 (CanLII), 2013 D.T.C. 1123 (Fr.), la CCI précise au paragraphe 34 que « la négligence du comptable n'est pas le facteur qui permet de passer outre au délai de prescription au sous-alinéa 152(4)a)(i) de la LIR. C'est la négligence du contribuable au moment de la présentation qui doit être analysée ».
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> [7] L'intimée reconnaît que le juge ne précise pas quels faits auraient été présentés erronément dans les déclarations de revenus, ni ce que l'appelant savait ou aurait dû savoir à ce sujet au moment de leur production. Elle souligne toutefois que les éléments de preuve au dossier permettent à cette Cour de faire cet exercice et de tirer de telles conclusions.

Although this might inspire you to try to help your client by asserting that the fault was all yours, your admission may not spare your client if, having "reviewed the draft return as a prudent individual, he would have seen questions within the return which would have prompted him to ask the appropriate questions of his accountant." See *Vine Estate v. The Queen, 2014 TCC 64* (Campbell; under appeal to FCA) at paragraph 40. In

Vine Estate, despite having very skilled accountants prepare the estate's return, the executors were faulted for the error so that the Court allowed the late reassessment.

As is always the case, decisions in this kind of appeal depend very much on the facts, and on whether the Court has enough sympathy for the taxpayer to allow the limitation period to apply.