Docket: 2011-1543(GST)I

BETWEEN:

CHANTAL CONSTANTIN,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on September 24, 2012, at Montréal, Quebec.

Before: The Honourable Rommel G. Masse, Deputy Judge

Appearances:

Counsel for the appellant:	Martin Delisle
Counsel for the respondent:	Philippe Morin

JUDGMENT

The appeal from the assessment made under subsection 323(1) of the *Excise Tax Act*, notice of which is dated August 28, 2008, and bears number PL2008-363, is dismissed, in accordance with the attached Reasons for Judgment.

Signed at Kingston, Ontario, this 6th day of December 2012.

"R. G. Masse"

Masse D.J.

Translation certified true
on this 23rd day of January 2013
Margarita Gorbounova, Translator

Citation: 2012 TCC 425
Date: 20121206
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REASONS FOR JUDGMENT

Masse D.J.

[1] This is an appeal from a reassessment dated August 28, 2008, and bearing the number PL2008-363, made under subsection 323(3) of the *Excise Tax Act* (ETA) in respect of the appellant, Chantal Constantin, in her capacity as a director of a corporation. The corporation in question is 9121-1482 Québec inc., which operated a business specializing in sign installation and lighting services under the name of EFN Installation et Service (the corporation or the company). The assessment was for a total of $136,028.65 made up of Goods and Services Tax (GST) that the corporation should have remitted under subsection 228(2) of the ETA for the period in question, from November 30, 2003, to August 31, 2007, and related interest and penalties. The assessment was confirmed by a decision on the objection dated February 21, 2011. Hence this appeal.

[2] During the period at issue, the appellant was the sole director and sole shareholder of the corporation. It is undisputed that the corporation is a legal person duly incorporated and registered for the purposes of Part IX of the ETA. It failed to

remit the tax amounts that it should have remitted, and the appellant does not dispute the assessment made in respect of the corporation.

[3] The only issue in this case is whether the appellant exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances.

Factual background

[4] The appellant, Chantal Constantin, and Denis Dubois are a couple and have lived together for over 25 years as common-law partners. They have two children and they are still living together. The appellant is a professional who works at the Centre de santé et de services sociaux de Laval. Mr. Dubois is a businessman who has operated various companies in the lighting field over the years.

[5] In 2003, Mr. Dubois purchased a business, EFN Installation et Service, which operated under the name 9121-1482 Québec inc. He did this with the aim of operating a sign installation and lighting services business. Mr. Dubois asked his spouse, the appellant, to be the sole shareholder and director of the company in order to share the risks inherent in business and to protect the couple's assets. Mr. Dubois took care of all aspects of managing the company. He made all decisions. The accounting was done internally as was everything relating to tax obligations. Ms. Constantin never worked in the business. She never solicited clients; she never did any administration; she never even signed one cheque. According to Mr. Dubois, she did nothing for the business. Mr. Dubois took care of everything and Ms. Constantin was only the director [TRANSLATION] "in the books".

[6] Mr. Dubois showed a great lack of judgment regarding finances. For reasons that need not be listed here, in the course of several years, Mr. Dubois became indebted to crooks for $125,000. The crooks were charging him a very high usurious interest rate of 10% per month (that is $12,500 per month), and, if he did not pay, reprisals would be taken against him. Mr. Dubois eventually found it impossible to continue paying these excessive amounts. He therefore began receiving unsubtle threats. Mr. Dubois was threatened and harassed almost daily, even at home. He testified that the only way out of it was to participate in a scheme hatched by one of the crooks, a Mr. Robert Beaudry, which consisted in providing accommodation invoices to Mr. Beaudry's clients. The scheme involved a cheque-cashing centre called Arylo. There is no need to describe the minute details of how the scheme worked; suffice it to say that it was a fraudulent scheme. The scheme lasted from 2004 to 2007. During that period, Mr. Dubois told the appellant nothing; he kept her

completely in the dark. She was never informed of anything regarding the fraudulent scheme.

[7] The appellant became the director and shareholder of the corporation in March 2003, and the corporation failed to make GST payments shortly after since the period in question starts on November 30, 2003. Around June 2007, Ms. Longpré, auditor at Revenu Québec, audited the corporation. During the audit, it was Mr. Dubois who communicated with Ms. Longpré. Ms. Longpré allegedly wanted to ask Ms. Constantin some questions, but Mr. Dubois told her that Ms. Constantin knew nothing about the company. Ms. Constantin did not know about the audit; however, she signed a power of attorney authorizing Mr. Dubois to communicate with Revenu Québec on her behalf. Mr. Dubois presented the power of attorney to Ms. Constantin, telling her that he must speak with the government, but not giving her any more explanations than that. She signed it.

[8] Finally, in September 2008, Mr. Dubois confessed to Ms. Constantin. She suspected that there was something wrong and asked him what it was. Mr. Dubois told her everything. Ms. Constantin demanded that he not register any other businesses under her name and wanted him to [TRANSLATION] "get her out of there". Then, Mr. Dubois denounced Mr. Beaudry and his crooked associates to the police. Legal proceedings were instituted, and as a result Mr. Beaudry was sentenced to imprisonment.

[9] Of course, Mr. Dubois had financial difficulties with the business, and therefore the bank sometimes delayed the payment of cheques he deposited, which created a cash-flow problem. This interfered with the sound operation of the business. Therefore, he needed "cash flow", and he stated that he had brought Ms. Constantin to Rapide Chèque and Arylo, two cheque-cashing centres, to sign documents authorizing the opening of accounts at these centres. He explained that the bank [TRANSLATION] "froze" his clients' cheques and that he needed [TRANSLATION] "cash quickly" in order to continue operating the business.

[10] From time to time, Ms. Constantin asked him about the company; she asked him [TRANSLATION] "how it was going". He always told her that it was going well, but that there were sometimes bad debts. He never told her the real situation. He stated that he and Ms. Constantin had the authority to sign the corporation's cheques, but that she had not signed any. Ms. Constantin was not involved in any way in the banking; all she did was sign some documents from time to time. When the assessments were made in respect of the company, Mr. Dubois did not dispute them. The company ceased operations in 2007. He explained to the appellant:

[TRANSLATION] "The company is no longer operating; we're going to get rid of it. There is no point keeping it."

[11] He said that he had had a visit to his home that he described as a threat when his daughter aged 14 or 15 at the time was home. Ms. Constantin was not there. One must wonder why the daughter said nothing to the appellant. Mr. Dubois was very upset by the threats, which he continued to receive, but he did not tell Ms. Constantin about them before 2008. He said that his spouse never spoke to him about her role as director of the company. She knew that she was the sole director of the company, but she never asked him any questions about her responsibilities as director. She did not worry about the risks related to the company. She did not ask him questions regarding the payment of taxes by the company because she knew that it was the accountant who prepared the financial statements. According to Mr. Dubois, she never worried about anything else because she knew that he was working with professionals. However, she always saw the financial statements. In September 2004, when Mr. Dubois brought the appellant to the cheque-cashing centre Rapide Chèque, he told her that the company was having some [TRANSLATION] "minor" financial difficulties and that it was [TRANSLATION] "temporary". In November 2005, when he brought her to the cheque-cashing centre Arylo, he explained to her that it was more secure than Rapide Chèque.

[12] The appellant testified. She has been a social worker and has worked full time at the Laval CFFF for 26 years. She has no training in accounting or management and has no experience in business management. Mr. Dubois and she have lived together for 25 years, and they have two children aged 19 and 17. She told the Court that she had signed the documents that made her director at Mr. Dubois' request in order to protect his assets against another person with whom he did business. She said that her spouse is a businessman and that she had trusted him completely. She testified that she had done almost nothing for the EFN company. She was not involved at all in the corporation's internal decisions. It was her spouse who took care of everything. However, she said that she had signed financial statements or other documents when Mr. Dubois brought them to her to be signed. She invested nothing in the business and she had never received any remuneration whatsoever. She was never on the business's premises. She said that she had asked Mr. Dubois questions to see how things were going as much regarding EFN as the other companies. These questions were general: for example, [TRANSLATION] "how was his day" and [TRANSLATION] "is everything going well?" Her spouse did not tell her very much, other than from time to time mentioning that he had gone to see the accountant, that he had the financial statements or that he had bad debts. She did not ask him for more details. Between 2003 and 2007, she did not suspect anything and had not the

slightest suspicion about Mr. Beaudry and other people's threats and harassment of her spouse. She knew nothing about the false invoice scheme. She found out only at the end of August 2008 when her spouse confessed to her and told her about everything.

[13] She admitted that, on September 27, 2004, she had signed Exhibit P-6 at her spouse's request. Exhibit P-6 is the document authorizing the opening of an account at Rapide Chèque, a cheque-cashing centre. By signing, the appellant, as a surety, personally undertook to cover any cheques given to Rapide Chèque by the company. She authorized Denis Dubois to cash the company's cheques. She said that her spouse had explained to her that the company had been having [TRANSLATION] "minor", "temporary" difficulties, that the bank was late – this could take a week or two – paying the company's cheques and the company needed cash right away, which would enable it to continue operating. She asked him about the financial difficulties experienced by the company, but Mr. Dubois' explanations satisfied her. She also admitted that, on November 2, 2005, she signed Exhibit P-7, which is the document authorizing the opening of an account at Arylo, another cheque-cashing centre. This was again done at her spouse's request and for the same reasons he previously gave. But this time he added another one, namely, that Arylo was more secure than Rapide Chèque.

[14] The appellant stated that she had signed the annual declarations for the Registraire des entreprises du Québec for 2003 and 2005 and that her spouse signed the one for 2004. When she signed these documents, she asked him [TRANSLATION] "what the papers were" and he simply told her that they were for the company. In 2008, when she found out about the false invoices and the threats, she told him: [TRANSLATION] "You're going to get me out of there. I don't want anything to be in my name anymore". She insisted that he go to the police.

[15] In cross-examination, she said that, although she was the sole director and shareholder, she had no knowledge of the risks she was facing as a director even though she knew that there were risks. She did not seek out information about this. She admitted that, on February 4, 2003, she signed as president and secretary of the company the paperwork for opening a business account for the company at the National Bank (see Exhibit I-3). She signed a power of attorney/registration for GST/QST and source deductions dated January 10, 2003, authorizing five employees to take the steps needed to register the company for the purposes of GST and Quebec Sales Tax (QST) and for the purposes of tax deductions at source (see Exhibit I-4). As president, she signed a power of attorney dated February 3, 2003, authorizing Mr. Dubois to sign for her all cheques she made on behalf of the company (see

Exhibit I-5). She signed a letter dated November 3, 2003, informing Revenu Québec of a change of address for the payments of GST, QST, source deductions and income tax (see Exhibit I-6). She signed a resolution of signature (undated) that stated that Denis Dubois was the company's representative and that he exercised management powers consisting in issuing, accepting, endorsing, receiving payment for, negotiating and discounting any cheques, promissory notes, bills of exchange or other negotiable instruments (see Exhibit I-7). She admitted that she had signed a power of attorney dated November 18, 2005, authorizing a client to issue cheques payable to Denis Dubois following supplies made by the company (see Exhibit I-8). She also signed a document dated September 5, 2007, authorizing Revenu Québec to communicate confidential information regarding the company to Denis Dubois and naming Mr. Dubois as her representative and agent with the Ministère du Revenu du Québec (see Exhibit I-9). She was not aware of the fact that Revenu Québec was conducting an audit in June 2007. Her spouse did not tell her anything about an audit when she signed Exhibit I-9. She told the Court that she had looked at the financial statements but that she had asked her husband very few questions about the documents despite the fact that the sales for 2005 had dropped a great deal compared to the previous year. She told the Court that, although she had seen the financial statements, she had not read them line by line.

The appellant's position

[16] The appellant maintains that she was only an outside director and that she had exercised the diligence that a reasonably prudent person would have exercised in comparable circumstances. The appellant trusted her spouse, who is an experienced businessman. She also trusted the company's accountants to tell her if something was wrong with the business. The appellant asked her spouse general questions in order to find out what was going on with the business. Unfortunately, in the circumstances, her spouse misled her; he straight out lied to her and kept her in the dark about the real situation. She could do nothing to prevent the corporation's failure as she had not the slightest inkling of anything that would make her suspect that the company failed to meet its tax obligations. The appellant stated that, in this factual context, she had exercised the diligence that a reasonably prudent person would have exercised in comparable circumstances. In addition, she argues that there is nothing in the factual background of this case that could lead to the conclusion that she was wilfully blind to the company's real circumstances. In sum, her spouse lied to her, misled her and deliberately kept things from her. Therefore, the appellant argues that she should not be liable as a director following the company's failure.

The respondent's position

[17] The respondent claims that the appellant did not show that she had exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances. The respondent maintains that the appellant did not carry out her duties as a director on an active basis and in a positive manner and that, indeed, she did nothing at all. According to the respondent, she cannot use her inaction as a defence against a claim for malfeasance. In addition, the appellant could have known and should have known that the company was having tax problems because she knew that the company had financial problems. She did not worry about the company's tax remittances despite the fact that she had a positive duty to do so. She left everything up to her spouse even though she, in her capacity as director, had the obligation to do what was needed. She signed all documents that needed to be signed, which were given to her by her spouse; she signed them voluntarily, without being constrained or threatened, but refused to learn about their importance. She had enough doubts to wonder, but she refused to ask questions or to go further to find out the real state of things. The respondent maintains that the appellant practiced the ostrich's philosophy and hid her head in the sand so as to know nothing. She was wilfully blind, and, moreover, she completely abdicated her responsibilities, transferring them to her spouse. It was not a delegation of responsibilities but rather a total abdication of all her powers and all her responsibilities. This cannot constitute due diligence.

Statutory provisions

[18] The relevant provisions of the ETA are as follows:

> **323. (1)** If a corporation fails to remit an amount of net tax as required under subsection 228(2) or (2.3) or to pay an amount as required under section 230.1 that was paid to, or was applied to the liability of, the corporation as a net tax refund, the directors of the corporation at the time the corporation was required to remit or pay, as the case may be, the amount are jointly and severally, or solidarily, liable, together with the corporation, to pay the amount and any interest on, or penalties relating to, the amount.
>
> . . .
>
> **(3)** A director of a corporation is not liable for a failure under subsection (1) where the director exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances.

[19] The only issue is whether the appellant, in her capacity as director, "exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances", as required by subsection 323(3) of the ETA, thereby avoiding liability under subsection 323(1) of the ETA.

Analysis

[20] In *Soper v. Canada*, [1998] 1 F.C. 124, 149 D.L.R. (4th) 297, 97 DTC 5407, [1997] 3 C.T.C. 242, 1997 CanLII 6352, the Federal Court of Appeal summarized the principles governing the liability of directors of corporations. In carrying out the duties of his or her position, a director must act with integrity but also show a degree of skill and diligence. A director need not exhibit in the performance of his or her duties a greater degree of skill than may reasonably be expected from a person of his or her knowledge and experience. It is an "objective subjective standard". That is to say, the standard is partly the standard of the reasonable person, but it is defined based on the knowledge and experience of the particular individual. A director is not bound to give continuous attention to the affairs of his or her company, but the common law would not permit directors to adhere to a standard of passivity and irresponsibility. A director who acts irresponsibly – for example, by not attending all board meetings – does so at his or her own risk. Having regard to the needs of the business itself and the requirements of the articles of association, powers and responsibilities may properly be left to some other official, a director is, in the absence of grounds for suspicion, justified in trusting that official to perform such duties honestly. The larger the business, the greater will be the need to delegate. It is incumbent upon an outside director to take positive steps if he or she knew, or ought to have known, that the corporation could be experiencing a remittance problem. The typical situation in which a director is, or ought to have been, apprised of such a problem is where the company is having financial difficulties.

[21] The "objective subjective" standard gave some flexibility towards directors described in tax provisions such as subsection 323(3) of the ETA. But the Supreme Court of Canada rejected the "subjective" standard in *Peoples Department Stores Inc. (Trustee of) v. Wise*, [2004] 3 S.C.R. 461, 2004 SCC 68. Justices Major and Deschamps wrote the following at paragraphs 62 to 64 of their Reasons for Judgment:

> 62 The statutory duty of care in s. 122(1)(*b*) of the CBCA emulates but does not replicate the language proposed by the Dickerson Report. The main difference is that the enacted version includes the words "in comparable circumstances", which

> modifies the statutory standard by requiring the context in which a given decision was made to be taken into account. **This is not the introduction of a subjective element relating to the competence of the director, but rather the introduction of a contextual element into the statutory standard of care**. It is clear that s. 122(1)(*b*) **requires more of directors and officers than the traditional common law duty of care** outlined in, for example, *Re City Equitable Fire Insurance*, *supra*.
>
> 63 The standard of care embodied in s. 122(1)(*b*) of the CBCA was described by Robertson J.A. of the Federal Court of Appeal in *Soper v. Canada*, [1998] 1 F.C. 124, at para. 41, as being "objective subjective". Although that case concerned the interpretation of a provision of the *Income Tax Act*, it is relevant here because the language of the provision establishing the standard of care was identical to that of s. 122(1)(*b*) of the CBCA. With respect, we feel that Robertson J.A.'s **characterization of the standard as an "objective subjective" one could lead to confusion. We prefer to describe it as an objective standard.** To say that the standard is objective makes it clear that **the factual aspects of the circumstances surrounding the actions of the director or officer are important** in the case of the s. 122(1)(*b*) duty of care, **as opposed to the subjective motivation of the director or officer**, which is the central focus of the statutory fiduciary duty of s. 122(1)(*a*) of the CBCA.
>
> 64 The contextual approach dictated by s.122(1)(*b*) of the CBCA not only emphasizes the primary facts but also permits prevailing socio-economic conditions to be taken into consideration. The emergence of stricter standards puts pressure on corporations to improve the quality of board decisions. . . .
>
> [Emphasis added.]

[22] The Federal Court of Appeal reached the same conclusion regarding subsection 323(3) of the ETA in *The Queen v. Buckingham*, 2011 FCA 142. In *Buckingham*, the taxpayer was a sole director and the principle shareholder of a corporation. He managed the business's daily activities day to day and therefore played an important role in its operations. He acknowledged that he had financed the business with GST/HST amounts because it was having financial difficulties. Therefore, he was assessed under section 323 of the ETA for the GST/HST amounts that the business had not remitted and related penalties and interest. Justice Mainville of the Federal Court of Appeal dealt with the standard of care, diligence and skill. Justice Mainville indicated that subsection 323(3) of the ETA does not set out a general duty of care, but rather establishes a ground of defence against the specific liability set out in subsection 323(1) of the ETA. Directors must show that the conditions required to successfully use such a defence are met. The due diligence duty in subsection 323(3) of the ETA is expressly intended to prevent the failure of corporations to remit the amounts due. Directors must establish that they exercised

the degree of care, diligence and skill required "to prevent the failure". The purpose of this subsection is clearly to prevent failures to remit. Justice Mainville ruled that the due diligence standard is an objective standard, not an "objective subjective" standard. The reference to the concept of the reasonably prudent person clearly indicates that the test is objective rather than subjective. Justice Mainville discards any notion of a subjective standard and states the following at paragraph 37:

> Consequently, I conclude that the standard of care, skill and diligence required under . . . subsection 323(3) of the *Excise Tax Act* is an objective standard as set out by the Supreme Court of Canada in *Peoples Department Stores*.

[23] He explains this objective standard as follows at paragraphs 38 to 40:

> [38] This objective standard has set aside the common law principle that a director's management of a corporation is to be judged according to his own personal skills, knowledge, abilities and capacities: *Peoples Department Stores* at paras. 59 to 62. To say that the standard is objective makes it clear that the factual aspects of the circumstances surrounding the actions of the director are important as opposed to the subjective motivations of the directors: *Peoples Department Stores* at para. 63. The emergence of stricter standards puts pressure on corporations to improve the quality of board decisions through the establishment of good corporate governance rules: *Peoples Department Stores* at para. 64. **Stricter standards also discourage the appointment of inactive directors chosen for show or who fail to discharge their duties as director by leaving decisions to the active directors. Consequently, a person who is appointed as a director must carry out the duties of that function on an active basis and will not be allowed to defend a claim for malfeasance in the discharge of his or her duties by relying on his or her own inaction**: Kevin P. McGuinness, *Canadian Business Corporations Law*, 2nd ed. (Markham, Ontario: LexisNexis Canada, 2007) at 11.9.
>
> [39] An objective standard does not however entail that the particular circumstances of a director are to be ignored. These circumstances must be taken into account, but must be considered against an objective "reasonably prudent person" standard. . . .
>
> [40] The focus of the inquiry under subsections 227.1(3) of the *Income Tax Act* and 323(3) of the *Excise Tax Act* will however be different than that under 122(1)(*b*) of the CBCA, since the former require that the director's duty of care, diligence and skill be exercised to prevent failures to remit. In order to rely on these defences, a director must thus establish that he turned his attention to the required remittances and that he exercised his duty of care, diligence and skill with a view to preventing a failure by the corporation to remit the concerned amounts.
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> [Emphasis added.]

[24] What triggers this positive obligation? It should be noted in this regard that the conduct to be examined is that of the director starting from the time when it became clear to him or her that the company entered a period of financial difficulties. Justice Mainville stated the following at paragraph 46:

> [46] . . . The assessment of the director's conduct rather begins when it becomes apparent to the director, acting reasonably and with due care, diligence and skill, that **the corporation is entering a period of financial difficulties**: *Soper* at para. 50.
>
> [Emphasis added.]

[25] In conclusion, Justice Mainville provides the following summary at paragraph 52:

> [52] Parliament did not require that directors be subject to an absolute liability for the remittances of their corporations. Consequently, Parliament has accepted that a corporation may, in certain circumstances, fail to effect remittances without its directors incurring liability. **What is required is that the directors establish that they were specifically concerned with the tax remittances and that they exercised their duty of care, diligence and skill with a view to preventing a failure by the corporation to remit the concerned amounts**.
>
> [Emphasis added.]

[26] Justice Mainville reiterated these principles in the Federal Court of Appeal decision in *Balthazard v. The Queen*, 2011 FCA 331, at paragraph 32:

> [32] In *Buckingham*, this Court recently summarized the legal framework applicable to the care, diligence and skill defence under subsection 323(3), as follows:
>
> a. The standard of care, skill and diligence required under subsection 323(3) of the *Excise Tax Act* is an objective standard as set out by the Supreme Court of Canada in *Peoples Department Stores Inc.(Trustee of) v. Wise*, 2004 SCC 68, [2004] 3 S.C.R. 461. This objective standard has set aside the common law principle that a director's management of a corporation is to be judged according to his or her own personal skills, knowledge, abilities and capacities. However, an objective standard does not mean that a director's particular circumstances are to be ignored. These circumstances must be taken into account, but must be considered against an objective "reasonably prudent person" standard.

b. The assessment of the director's conduct, for the purposes of this objective standard, begins when it becomes apparent to the director, acting reasonably and with due care, diligence and skill, that the corporation is entering a period of financial difficulties.

c. In circumstances where a corporation is facing financial difficulties, it may be tempting to divert these Crown remittances in order to pay other creditors and thus ensure the continuity of the operations of the corporation. That is precisely the situation which section 323 of the *Excise Tax Act* seeks to avoid. The defence under subsection 323(3) of the *Excise Tax Act* must not be used to encourage such failures by allowing a care, diligence and skill defence for directors who finance the activities of their corporation with Crown monies, whether or not they expect to make good on these failures to remit at a later date.

d. Since the liability of directors in these respects is not absolute, it is possible for a corporation to fail to make remissions to the Crown without the joint and several, or solidary, liability of its directors being engaged.

e. What is required is that the directors establish that they were specifically concerned with the tax remittances and that they exercised their duty of care, diligence and skill with a view to preventing a failure by the corporation to remit the amounts at issue.

[27] Much has been written about *Buckingham*: see, for example, *Boles v. The Queen*, 2011 TCC 288, rendered on June 9, 2011, by Justice Boyle (appeal from the assessment dismissed); *Latulippe v. The Queen*, 2011 TCC 388, rendered by Justice Angers on October 11, 2011 (appeal dismissed); *Gougeon v. The Queen*, 2011 TCC 420, rendered by Justice Angers on October 11, 2011 (appeal from the assessment dismissed); *Heaney v. The Queen*, 2011 TCC 429, rendered by Justice Campbell (appeal from the assessment allowed); *Lagacé v. The Queen*, 2012 TCC 117, rendered by Justice Hogan on April 5, 2012 (appeal dismissed); *Martin v. The Queen*, 2012 TCC 239, rendered by Justice Angers on August 27, 2012 (appeals allowed in part); *Roux v. The Queen*, 2012 TCC 249, dated August 15, 2012, where Justice Angers dismissed the appeal from the assessment; *Cappador v. The Queen*, 2012 TCC 267, rendered by Justice Lamarre on July 25, 2012 (appeal dismissed); *Deakin v. The Queen*, 2012 TCC 270, rendered by Justice Boyle on July 26, 2012 (appeals dismissed); *Anderson v. The Queen*, 2012 TCC 333, rendered by Justice D'Arcy, who rejected the due diligence defence but referred the matter back to the Minister for reconsideration and reassessment; and *Boudreau v. The Queen*, 2012 TCC 342, rendered by Justice Bédard on September 28, 2012 (appeal dismissed).

[28] Mr. Delisle, counsel for the appellant, referred to several examples where a director was able to avoid his or her company's tax liabilities because he or she had been kept in the dark about the true tax situation of the business. *Baker v. The Queen*, 2010 TCC 268, is the case of a 64-year-old appellant who was not well educated and was the sole director and shareholder of a corporation. His spouse took care of all the administrative tasks related to operating the business. The appellant never knew about the financial problems or the debts resulting from operating the business, and, although he knew he was the sole director and shareholder of the corporation, he relied solely on his spouse and was completely unfamiliar with the responsibilities that fall to a director. The appellant believed that his spouse was honest and competent and that she took all measures necessary to fulfill the corporation's legal, commercial and tax obligations. In addition to admitting that he knew nothing about his responsibilities as a director, the appellant said that he had never discussed a director's tasks with anybody including his spouse. He never tried to seek out information about them. Justice Hershfield allowed the appeal from the assessment, basing himself on the principles established by the Federal Court of Appeal in *Soper*. *McIsaac v. The Queen*, 2004 TCC 618, rendered by Justice Campbell on September 29, 2004, *Ouahidi v. The Queen*, 2007 TCC 119, rendered by Justice Favreau on March 22, 2007, and *Pascoal v. The Queen*, 2009 TCC 608, rendered by Justice McArthur on December 2, 2009, all reach the same conclusion.

[29] The respondent relied on *Penney v. Canada*, [1999] T.C.J. No. 803 (QL), rendered by Judge Margeson on November 17, 1999. In that case, at her brother's request, the appellant became the sole director of a corporation and held all of the shares in the corporation for her brother. The brother took care of all aspects of operating the company, which did business in Newfoundland. The appellant lived in Toronto. A stamp with the appellant's signature was made, but the appellant never asked any questions with regard to the use of this stamp, which was placed on various documents without the appellant's being consulted. The appellant was told that she was not facing any risk and that she had no obligations regarding the company. She had turned a blind eye to everything relating to managing the business. She did not operate the business, and she did not receive any money from it. She made no decisions regarding the business and did not participate in any way in its operation. The company was fully controlled by the appellant's brother and she was the sole director, shareholder and officer only in theory. The brother had full powers and the sister, the appellant, had no power. The appellant did not know the definition of a director. The appellant was not interested in the company except to be of service to her brother, whom she trusted completely. Judge Margeson found that the appellant's actions in the circumstances were equivalent to refusing to see the truth.

According to what was stated in *Starkman v. Canada*, [1996] T.C.J. No. 1629 (QL), 97 DTC 220, even a passive or inactive director cannot necessarily avoid all liability, and even in the context of a family business, the circumstances of the case must be taken into account. Judge Margeson found that the appellant had abdicated her responsibilities, transferring them to her brother. The Court dismissed the appeal from the assessment and found the appellant as well as her brother liable for the corporation's failures.

[30] It should be noted that all the case law cited above predates *Buckingham*. Thus, we can see that before *Buckingham* a director who had been kept in the dark by family members who managed the business could rely on the due diligence defence. Certainly, since *Buckingham*, the standard has become stricter given that subjectivity is no longer relevant. Now it is simply an objective standard considered within the entire factual background. Case law subsequent to *Buckingham* clarifies this.

[31] In *Lagacé v. The Queen*, *supra*, Justice Hogan wrote the following at paragraph 21:

> [21] A successful **due diligence defence requires evidence of the directors taking concrete actions to prevent failure. Applying *Buckingham* here, it is not sufficient to say that Ms. Lagacé should not be found liable because she was an outside director. The evidence shows that she was in business with Mr. Eastveld. They lived together and worked together in the business out of a home office. The appellants had the burden of establishing that they took steps to prevent the corporation's failure.** . . .
>
> [Emphasis added.]

[32] In *Boles v. The Queen*, *supra*, the appellant argued that he did not even know that he was a director of the corporation in question before the Canada Revenue Agency began to prosecute him. He stated that he had never been consulted with regard to the business's activities or ever participated in its activities or had any direct knowledge of the business's commercial activities or affairs or, at any moment in time managed its operations or took part in its operations in any way. However, he admitted signing some documents for the corporation. Justice Boyle referred to *Buckingham* at paragraph 2 of his Reasons for Judgment:

> [2] The most recent pronouncement on the scope of director's liability for unremitted GST or income tax withholdings and upon director's possible defences thereto are set out by the Federal Court of Appeal in its recent decision in *Canada v. Buckingham*, 2011 FCA 142, dated April 21, 2011. In *Buckingham* the Federal Court of Appeal confirmed that the scope of the director's liability provisions is potentially broad and far reaching in order to effectively move the risk for a failure

> to remit by a corporation from the fisc and Canadian taxpayers generally to the directors of the corporation, being those persons legally entitled to supervise, control or manage the management of its affairs. The Court also confirmed that a director seeking to be exculpated for having exercised reasonable care, diligence and skill must have taken those steps "to prevent the failure" to remit and not to cure it thereafter. . . .

[33] Justice Boyle also states the following at paragraph 9:

> [9] This leaves the question of whether Mr. Boles did in fact exercise the degree of skill, care, diligence and prudence to prevent the company's failure to remit GST in the circumstances. **There was no evidence whatsoever that Mr. Boles involved himself at all with Begley Associates in the years in question and therefore he cannot say that he did anything actively to prevent the failure to remit the GST.** There was some evidence that in later years he may have helped free up some money for Mr. Clark, prior to his death, to significantly pay down or pay off any tax arrears of Begley Associates. **However, it is clear that the active steps must be to prevent the failure and not merely to remedy it.** . . .
>
> [Emphasis added.]

[34] In *Latulippe, supra*, Justice Angers wrote the following at paragraphs 20, 21 and 24:

> [20] I cannot ignore the recent decision of the Federal Court of Appeal rendered in *Buckingham v. The Queen,* 2011 FCA 142, which sets aside the subjective standard and established that the test should be objective. **The application of this more strict standard is such that the arguments based on personal shortcomings should be aside**. . . .
>
> [21] The particular circumstances of a director may be taken into account, but only against the objective reasonably prudent person standard, as the Federal Court of Appeal explains in paragraph 39 [quotation omitted]:
>
> . . .
>
> [24] However, our Court also rendered decisions in which it was less indulgent with respect to *de jure* directors, who, considering the family ties, did not assume their responsibilities as directors. Suffice it to refer to P*enney v. Canada,* [1999] T.C.J. No. 803 (QL), [1999] G.S.T.C. 102, *Black v. Canada*, [1994] T.C.J. No. 191 (QL), [1994] 1 C.T.C. 2750, *Hanson v. Canada*, [1996] T.C.J. No. 1392 (QL), [1997] 1 C.T.C 2456 and *Western v. Canada*, [1999] T.C.J. No. 155 (QL). All of these decisions emphasize that there is nothing in the wording of the relevant provisions that would suggest that Parliament intended to assist directors who failed to act because they ignored their responsibilities and those of the company of which

they were the directors. Suffice it to cite paragraph 22 of the decision of Sarchuk J. in *Hanson*:

> The mere fact that one becomes a director in a family context is not sufficient to permit such director to turn his or her back on the affairs of the company; to ignore it for all practical purposes; to ignore her responsibilities; indeed, to fail to ask even the most rudimentary question as to what those responsibilities are, and thereby to escape liability under the provisions of the *Income Tax Act*.

[Emphasis added.]

[35] In *Deakin v. The Queen*, *supra*, Justice Boyle states at paragraph 24 that a director's obligations under subsection 323(3) of the ETA are similar to a guarantee:

> . . . The directors' liability provisions of the legislation should be regarded by business persons as somewhat similar to a form of personal guarantee by the directors that can expose them to comparable liability for the amount involved. . . .

[36] In my view, directors' obligations and responsibilities are very significant and may be very onerous, even in the case of a small family company. The position of a *de jure* director should not be assumed lightly. Directors have responsibilities towards the company, towards the shareholders, towards the company's employees and towards the tax authorities. In my opinion, a diligent director must seek out at least general information about what he or she is involved in and take his or her responsibilities seriously.

[37] In this case, did the appellant demonstrate that she had exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances? Was she actually concerned about the tax remittances in order to prevent the company's failure to remit the amounts at issue? Did she take concrete actions in order to prevent the failure?

[38] All of the supporting evidence that was submitted at the hearing clearly shows that the appellant presented herself to the world including the tax authorities as the president and director of the company. Although she was the sole director and shareholder, she had no knowledge of the risks she was facing as director even though she knew that there were risks. She did not, however, seek out information about them; yet, it seems to me that a reasonably prudent person, in comparable circumstances, would inquire about the potential risks related to the position of a director of a company, even if a spouse was its manager.

[39] The factual background shows that the appellant played a role in the company's affairs, even though in that role she followed her spouse's instructions. No one was forcing her to do what her spouse asked her to do. She did it to help him out. It is clear that the appellant knew nothing about the business's operations and had had nothing to do with operating it. She left all of that to Mr. Dubois. It is true that she asked Mr. Dubois questions, such as how things were going or how his day had been or whether everything was going well. But these questions were general questions concerning the EFN business as well as other companies that Mr. Dubois managed. Although Mr. Dubois had told her that sometimes there were bad debts, she had not asked him for more details. I am under the impression that these questions were asked as part of trivial conversations between spouses. A reasonably prudent person, who knew that there were bad debts, would not have asked only general questions.

[40] From the factual background, it is clear that the appellant abdicated almost all of her powers as director and conferred them on her spouse. As director, she signed a power of attorney dated February 3, 2003, authorizing Mr. Dubois to sign all cheques for her on behalf of the company, and it is a fact that she had never signed a single cheque. It was Mr. Dubois who signed all cheques. The appellant signed on behalf of the company powers of attorney authorizing Mr. Dubois and his accountants to communicate with Revenu Québec and designated Mr. Dubois as the contact person. Mr. Dubois signed documents for the appellant and on her behalf, which was clearly done with her approval: see income tax returns for the 2004 and 2006 taxation years. The appellant signed a Signature Resolution (undated) in order to make Denis Dubois the company's representative and to allow him to exercise management powers consisting in issuing, accepting, endorsing, receiving payment for, negotiating and discounting any cheques, promissory notes, bills of exchange or other negotiable instruments. She signed a power of attorney dated November 18, 2005, authorizing a client to issue cheques payable to Denis Dubois following supplies made by the company. She signed a power of attorney dated September 5, 2007, authorizing Revenu Québec to disclose to Denis Dubois confidential information about the company and naming Denis Dubois as her representative and agent with the department. Clearly she would have signed any document that Mr. Dubois gave her with no more explanations than [TRANSLATION] "It's for the company". In this case, it is not a delegation of powers; rather, it is an abdication of decision-making powers in favour of Mr. Dubois. However, a director of a corporation cannot avoid his or her responsibilities and obligations simply by casting off the director's powers.

[41] Did the appellant know or should she have known that the company was having financial difficulties? She knew that the company sometimes had bad debts because her spouse had told her about it. The existence of bad debts in itself is not something out of the ordinary, but it is a sign that indicates potential problems that call for a more rigorous monitoring of active debts. She knew that the company had done business with the National Bank since 2003. But, in September 2004, she signed the document for the opening of an account at the cheque-cashing centre Rapide Chèque. In addition, she had to personally undertake to cover as surety all cheques given to Rapide Chèque by the company. In my opinion, it is unusual for a company to do business with a cheque-cashing centre instead of a bank. The appellant's spouse told her that the bank [TRANSLATION] "froze" cheques and that, as a result, the company was short of cash to the point of needing cash quickly in order to continue its activities. At that point, although Mr. Dubois described the cash-flow problems as [TRANSLATION] "minor" and "temporary", the appellant should have known that the company had serious financial problems that should have been closely monitored, especially since she had had to personally make an undertaking. Clearly, the cash-flow problems were not "minor" or "temporary" since fourteen months later the company continued to do business with the cheque cashing centre, Arylo instead of a bank. The fact that cash-flow problems lasted for fourteen months indicates that the business had serious financial problems, which was a sign that there were probably also tax problems. The appellant looked at the financial statements and she even signed as the director the financial statement dated June 30, 2006, relating to 2005. She did not read the financial statements line by line and asked her spouse very few questions about these documents despite the fact that, in 2005, sales dropped a great deal compared to the year before. She signed a power of attorney dated November 18, 2005, authorizing a client to issue cheques payable to Denis Dubois following supplies made by the company. She did not wonder at that time why a client would pay Mr. Dubois directly instead of having the cheque go through the company. She signed a power of attorney dated September 5, 2007, authorizing Revenu Québec to disclose to Denis Dubois confidential information about the company and naming Denis Dubois as her representative and agent with the department. This should have tipped her off about the existence of a potential problem with respect to remitting taxes. She was definitely aware of the fact that Revenu Québec wanted to obtain information; if she was not, why sign a power of attorney?

Conclusion

[42] Although the appellant's spouse lied to her and misled her, the factual background shows that there were many clues of the financial problems that a

reasonably prudent person should have recognized in comparable circumstances. I have come to the conclusion that the appellant should have known that the business had financial problems and therefore tax problems. In reality, the appellant was not concerned about the tax remittances and took no concrete action in order to prevent the company's failure to remit the amounts at issue.

[43] In conclusion, having considered all of the evidence and taken into account the factual background of this case, I am not satisfied that Ms. Constantin demonstrated that she had exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances.

[44] For these reasons, the appeal is dismissed.

Signed at Kingston, Ontario, this 6th day of December 2012.

"R. G. Masse"

Masse D.J.

Translation certified true

on this 23rd day of January 2013
Margarita Gorbounova, Translator

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