Docket: 2009-3334(GST)G

BETWEEN:

LESLIE MCKENZIE,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on October 17 and 18, 2011
and March 15, 2012 at London, Ontario.

Before: The Honourable Justice J.E. Hershfield

Appearances:

Counsel for the Appellant:	Scott Smith
Counsel for the Respondent:	André LeBlanc

JUDGMENT

The appeal from the assessment made under the *Excise Tax Act*, notice of which is numbered 00000000077 and dated August 20, 1997, for the period March 1, 1995 to July 31, 1996, is allowed, with costs, and the assessment is referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with and for the reasons set out in the attached Reasons for Judgment.

Signed at Ottawa, Canada this 26th day of July 2013.

"J.E. Hershfield"

Hershfield J.

Citation: 2013 TCC 239
Date: 20130726
Docket: 2009-3334(GST)G

BETWEEN:

LESLIE MCKENZIE,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Hershfield J.

[1] The Appellant was the sole director, officer, employee and shareholder of 731771 Ontario Limited, a company carrying on business as Associated Car Company ("Associated Cars"). She was actively engaged in its business relying to a considerable extent on the employees of a related company: Associated Auctioneers Inc. ("AAI") to assist in the operation of Associated Cars.

[2] Associated Cars failed to collect and remit GST alleged by the Respondent to have been a failure contrary to the provisions of the *Excise Tax Act* (the "*Act*"). An assessment was issued (the "underlying assessment"), an appeal was filed and abandoned and Associated Cars failed to pay the amount assessed. The Appellant was assessed as being liable for the unpaid underlying assessment amount under the director's liability section of the *Act*, namely section 323. Her defence, commonly known as the "due diligence defence", is based on her submission that she acted with the required due diligence in coming to the belief that no GST was collectible in respect of the supplies at issue by virtue of section 87 of the *Indian Act*.

General Background and the Relevant Provisions of the *Act*

[3] Associated Cars was a registered motor vehicle dealer engaged in the business of buying and selling vehicles in London, Ontario. It was assessed, pursuant to the provisions of the *Act* for failing to collect and remit GST on the

sale of 572 used cars between March 1, 1995 and July 31, 1996, (the "relevant period"). The assessment also denied input tax credits (ITCs) in respect of the GST paid by it on its purchase of those vehicles. The assessment was in the amount of $1,692,941.10 which included tax, interest and penalties.

[4] A rather unusual assessment process resulted in the Reply to the Notice of Appeal (the "Reply") stating that the Respondent reserved the right to challenge, in effect, whether the particular underlying assessment that the Appellant was challenging was the correct underlying assessment since there had been two such assessments. The second assessment was in respect of a longer period of time that overlapped the relevant period and was for a larger dollar amount. The Respondent, subsequent to filing the Reply, determined that the first assessment was the correct underlying assessment. Although the Reply was never amended, the Appellant proceeded with the hearing without raising issues over this unusual assessment process.[1]

[5] In any event, Associated Cars withdrew its appeal of the relevant assessment and the resultant liability for tax, penalties and interest was left unpaid.

[6] The Appellant appeals the assessment against her, *qua* director, on the basis that subsection 323(3) of the *Act* applies to relieve her of any liability under subsection 323(1). Those provisions read as follows:

> Liability of directors
> 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

[1] Counsel for the Respondent advised that the second assessment was "protective". The Respondent was unsure whether Associated Cars or its related company conducted the transactions at issue so the second assessment was issued against both companies. Justice O'Connor of this Court vacated the second assessment on the basis, at least in part, that it was statute-barred. I was advised that this Judgment was discussed in chambers with Justice O'Connor and consented to by the parties on the basis that it would allow the issue of the applicability of the *Indian Act* exemption to be determined in respect of the subject transactions by moving ahead with the first assessment against Associated Cars. It was effectively conceded by the parties that the second assessment against Associated Cars was thereby void leaving the first assessment undisturbed. At the same time, as the second assessment was vacated, Associated Cars withdrew its appeal of the first assessment. It is the tax debt arising from the first underlying corporate assessment for which the Appellant can be, and was, assessed under the director's liability section of the *Act*. See *Lornport Investments Ltd. v. Canada*, [1991] 1 C.T.C 57 (F.C.T.D.), (aff'd [1992] 2 F.C. 293 (F.C.A.)) and *Coleman C. Abrahams (No.1) v. M.N.R.*, [1966] C.T.C. 690.

> 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.
>
> […]
>
> Diligence
>
> (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.

The Issues

The Denial of ITCs

[7] The issue of the denial of ITCs was not pursued at the hearing or in the submissions of the Respondent. Accordingly, I will not hold the Appellant liable for that portion of the underlying assessment for which she has been assessed.

GST and Preliminary Comments on "Notional" ITCs

[8] It is not in dispute that Associated Cars did not, in fact, collect and remit GST in respect of the subject sales. Associated Cars took the position, at the time these sales were completed, that the purchasers were exempt purchasers pursuant to section 87 of the *Indian Act* and as such no GST could be imposed. On the same grounds, the Appellant asserts that she can not be held liable for the collection and remittance failure.

[9] As well, recognizing that a director's liability is more forgiving, the Appellant in this case relies on the competence of Associated Cars' agent, AAI, the related company that carried out, as an unpaid contractor, essentially all of Associated Cars' business that was not directly handled by the Appellant.

[10] While the due diligence issue surrounding the application of section 87 of the *Indian Act* might seem pointed enough, the heart of the issue, from the Respondent's perspective, is, in fact, coloured by the role Associated Cars played in a scheme that the Respondent views as misrepresenting the real terms of the vehicle purchase and sale transactions pursuant to which vehicles were only purportedly to be delivered by Associated Cars to a First Nation reserve ("Reserve"). The Respondent, in accordance with published practices, which were set out in Technical Information Bulletin B-039R dated November 25, 1993) focuses on the place of delivery of the subject vehicles in respect of the application

of section 87 of the *Indian Act* without concern over other connecting factors used in income tax cases to determine the application of that section.

[11] The scheme was to take advantage of what might be called an unintended gap in the *Act* whereby it was possible, using First Nations as intermediaries, for vehicle dealers to receive unintentional multiple "notional" ITCs. Section 176 of the *Act*, as it read in the relevant period, gave vehicle dealers that acquired used cars ITCs on such vehicles purchased as if GST had been collected by it from the used car vendor. This was a notional ITC if, in fact, no such GST collections were neither made nor required to be made. This would be the case where the vendor of the used cars had acquired them *qua* consumer and paid GST without receiving an ITC on the sale of that vehicle to the used car dealer.[2]

[12] In brief, notional ITCs were intended by Parliament to ensure that GST paid on supplies along the chain of sales could still be recovered when it came back into the commercial stream by a consumer selling the property to a commercial buyer.

[13] What was not contemplated by Parliament, it seems, was that flipping vehicles through a First Nation would give rise to multiple notional ITCs; i.e. multiple tax benefits. As a result of the proliferation of this abuse, the notional ITC was eliminated in 1996 and replaced with a more limited "trade-in" rule in subsection 153(4).

[14] However, car-flipping schemes completed prior to that amendment, were still attacked by the Canada Revenue Agency ("CRA") on various grounds.[3] As my analysis will demonstrate, one of the points of attack is to not allow the application of section 87 of the *Indian Act* unless the used property was delivered to a Reserve. As my analysis will also demonstrate, however, published CRA administrative policies were not always followed.

[15] Before moving on to set out my factual findings in this case, I wish to note a fact that could otherwise get lost in the detail. Associated Cars, as a used car dealer, did not purchase the subject vehicles from consumers and never received the benefit of notional ITCs. Associated Cars was in a chain of other dealers that

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[2] A vendor who acquired *qua* consumer would not be a registrant selling the used car in the course of a commercial activity.

[3] I note, here, that Bulletin B-039R referred to above was issued by Revenue, Customs, Excise and Taxation. As will be noted later, in these Reasons, administrative practices set out in later Bulletins did not vary materially from Bulletin B-039R.

benefited, but was itself, in effect, only a facilitating intermediary. It paid GST to dealer vendors in all cases and remitted same in respect of each of the 572 used car transactions examined in this appeal. The ITCs it collected were not notional ITCs - they were ITCs claimed for actual GST paid in the normal course of its commercial activities of buying and selling used cars from other dealers.

Background to the Formation of Associated Cars and Associated Cars' Role in the Scheme

[16] The Appellant testified at the hearing. She has a high school education and six months of nursing studies. After leaving school she worked at various administrative jobs including being an administrative assistant at a bank. She began working for AAI in an administrative capacity in 1985 after her husband, a licensed auctioneer, incorporated AAI. It carried on business as a public auction house in London, Ontario.

[17] At all relevant times, the Appellant's husband was the sole shareholder of AAI. He also testified at the hearing.

[18] AAI historically would take personal property on consignment from a variety of customers such as financial institutions that may have seized various personal property items or from trustees in bankruptcy who were liquidating the assets of a bankrupt. These consignments included vehicles. Indeed, although AAI was a general auction enterprise, vehicles became its primary source of business even though it was not a licensed motor vehicle dealer and did not employ a registered motor vehicle sales person.

[19] The growth in the vehicle auction business was fuelled by licensed dealers who had vehicles in their inventory to shed and by licensed dealers looking for inventory, so many of AAI's auction transactions involved vehicle dealer consignment vendors and dealer purchasers. The auction was the means by which these sales were facilitated. AAI would, in the normal course of its business, act as the intermediary in the case of a successful auction sale by acquiring the vehicle from the consignor and transferring it to the successful buyer. In the normal course of its business it took care of all the administrative details of, and paperwork for, these transactions such as transferring ownership from the consignor vendor to

itself and then from itself to the auction purchaser.[4] It collected a fee from the purchaser and a commission from the vendor.

[20] However, in its first few years of business, the Ontario government was threatening to shut down AAI's vehicle consignment business because it was not a licensed motor vehicle dealer. This would cripple a major source of its income. An application by AAI to be licensed as a motor vehicle dealer was denied; hence the formation of Associated Cars by the Appellant. Unlike AAI, it was able to obtain the necessary license. The Appellant also became a registered motor vehicle salesperson in compliance with a requirement imposed on licensed dealers that they have at least one such person engaged in dealer sales. At that point, the Appellant ceased to be an employee of AAI and became the sole employee of Associated Cars.

[21] While the business format and structure changed, practically speaking it seems that not much else changed when Associated Cars first started its business in 1987. The administrative work continued to be done by AAI personnel and the Appellant much as it had always been done. The Respondent did not take issue with this structure between these related, technically unassociated, entities. It was the company's operating format for years before it started to engage in the subject transactions.

[22] In any event, this business format and structure was in place then when the GST came into force in 1991. Associated Cars was a registrant under the *Act* and relied on AAI employees to assist in dealing with GST collection and remittance requirements, and making ITC claims in respect of Associated Cars' transactions, including its large volume of dealer-to-dealer auction sales.
[23] The subject 572 transactions came about as a result of what was described as an expansion of Associated Cars' business in 1995.

[24] That expansion came about as a result of the Appellant's husband having been approached by a representative of Canada Auctions with the idea to sell used

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[4] While ownership transfers to and from Associated Cars was the normal practice, Mr. McKenzie testified that in dealer-to-dealer transactions that was not always the case. There was no evidence at the hearing as to whether this meant that Associated Cars registered such vehicles directly from the vendor to the First Nation purchaser. This would still make Associated Cars a registry agent, an intermediary role for which it earned a fee. The evidence I do have indicates that ownership was transferred along the line to different buyers. A missing registration might only be the result of a person entitled to be registered as owner instructing a registry agent to make the transfer to another party.

vehicles directly to First Nations. The sales were to be pre-ordained, at fixed prices between fixed buyers and sellers, with Associated Cars acting solely as an intermediary. Nonetheless, the proposal would enhance sales volume and income and thereby business value, which were important factors to both AAI and Associated Cars in the event of a possible sale of their businesses, a possibility also purportedly raised by this representative of Canada Auctions.

[25] Still, this business proposal must have raised questions in the mind of the Appellant's husband. He sought advice from AAI's accountant who then met with the CRA to discuss any issues that would arise with selling used cars to First Nations and not collecting GST.

[26] The accountant met with a CRA officer, Mr. Arner, who testified at the hearing. There is little dispute as to the cautionary comments made by Mr. Arner which were passed on to the Appellant's husband by the accountant and emphasized again to the Appellant's husband at another meeting. This second meeting was between the Appellant's husband and Mr. Arner where the caution was repeated. The caution was that there must be GST charged on sales to First Nations unless the vehicles were delivered to a Reserve and proof of such delivery could be established by appropriate "almost perfect" records.

[27] Mr. Arner testified that he tried to discourage the Appellant's husband from entering into these transactions. However, his testimony did not suggest that he explained the abuse associated with car-flipping schemes using First Nation buyers, a scheme about which the CRA was then already concerned. Nor did his testimony suggest that he warned of the likelihood of an audit as the reason for suggesting that their records be "almost perfect". He did testify that he offered to review their documentation to help ensure that there would be no issues in respect to relying on section 87 of the *Indian Act*.

[28] The Appellant testified that she was not aware of Mr. Arner's discouraging comments or offer to assist, but she acknowledged meeting with her husband and AAI's bookkeeper to determine how to proceed. On the other hand, her testimony made it clear that she knew that the subject vehicles were required to be delivered to a Reserve both contractually and for GST purposes. Her testimony did not speak of a discussion at this meeting with her husband and AAI's bookkeeper, as to how AAI was to proceed and to ensure that this requirement was met. She said that she was knowledgeable about documentation procedures but she did not express any particular knowledge of delivery procedures.

[29] Indeed, the evidence suggests that deliveries were normally the responsibility of the buyer since the inception of the business and before the introduction of the subject transactions. Even after the introduction of such transactions, they only constituted about 20% of Associated Cars' total vehicle business during the relevant period. That is, during the relevant period, some 80% of Associated Cars' total vehicle sales were auction sales. Most of the latter business was likely dealer-to-dealer transactions given that this was the primary source of the vehicle business conducted by Associated Cars and AAI. In that context, deliveries were the responsibility of the buyer. If Associated Cars or AAI arranged a delivery to Toronto, an additional fee of $75 was charged.[5] This was not charged in the case of the subject transactions. This led the Respondent to suggest that there were, in fact, no deliveries of the subject vehicles to Reserves.

[30] On the other hand, R.W.A. Inc. ("RWA"), a transport enterprise that delivered 166 of the 572 subject vehicles, charged a delivery fee on a COD basis. RWA delivery documents showed point of origin as Associated Cars (or AAI) and point of delivery at addresses within the Six Nations of the Grand River Reserve ("Six Nations Reserve").

[31] In any event, the business expansion involving First Nation sales went forward and, as noted, 572 used cars were acquired from dealers and resold by Associated Cars during the relevant period. There were ten used car sellers and five First Nation purchasers.

[32] The vehicle sellers in this case are as follows:

a. Hometown Motors, located in Gananoque, Ontario.

b. Code Ford Mercury Sales Ltd., located in Gananoque, Ontario.

c. Autocrat Motor Cars Inc., located in Oakville, Ontario.

d. Humberview Motors, located in Toronto, Ontario.

e. Gus Zeidler Auto & Boat Sales, located in Orillia, Ontario.

f. Oakville Motors Sales & Leasing, located in Oakville, Ontario.

g. Adnil Holdings, located in Milton, Ontario.

[5] The Appellant testified that deliveries of the subject vehicles were done by AAI personnel.

h. Rexe Automotive Wmls, located in Napanee, Ontario.

i. 1159223 Ontario Ltd., located in Ganonoque, Ontario.

j. Bennett Auto Sales, located in London, Ontario.

[33] The purchasers of the vehicles were:

a. CTM Wholesale & Leasing, located in Shannonville, Ontario.

b. Ojibway Car Sales, located in Ohsweken, Ontario.

c. William Wood, located in Ohsweken, Ontario.

d. F. Nettagog Sales, located in Ohsweken, Ontario.

e. Katharine Hopkins, located in Thamesville, Ontario.

[34] While I have noted that Associated Cars acted as purchaser and vendor of all vehicles, and as the registry agent, for both the auction and First Nation sales, there were notable differences.

[35] In respect of auctions, if a bid was successful the vehicle was first transferred and registered as being acquired by Associated Cars and then Associated Cars transferred and registered it to the successful bidder.[6] As I said, delivery was the responsibility of the purchaser. Each vehicle had its own transaction paperwork. Documentation would be routine and complete, although not always accurate. If there was a representation problem as to the vehicle, it could be returned or the price could be adjusted. There would be more reliance on vendor representations on dealer-to-dealer sales.

[36] In the case of the subject vehicles all the sales were dealer-to-dealer sales, so the normal practice of Associated Cars acting as the intermediary registered owner was not always followed. In some cases, Associated Cars would transfer pre-arranged sales directly from the seller to the pre-arranged buyer although delivery remained the responsibility of Associated Cars. Each vehicle still had its own transaction paperwork. Documentation was to be routine and complete although that was not always the case. Inaccuracies were not unexpected or abnormal.

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[6] *Ibid*; in dealer-to-dealer vehicle sales Associated Cars was not always registered as the intermediary owner.

[37] The Appellant testified that some 4,000 automobile auctions were processed during the subject period in addition to the subject transactions. An Agreed Book of Documents consisting of 12 volumes and 572 transactions was submitted at the hearing. Each of those transactions during the relevant period was the subject of the reassessment. That is, they pertained to vehicles that Associated Cars bought for pre-arranged sales and delivery to either the Mississaugas of the New Credit First Nation Reserve ("New Credit Reserve") or the Six Nations Reserve. Both destinations were in the order of 100 kilometres from London, Ontario.

[38] It is relevant to note the pre-arranged sales of all the subject vehicles included naming the particular buyer, place of delivery and fixing a pre-determined price. Associated Cars essentially only acted as a registry agent and purportedly performed a delivery service.

Further Particulars of the Appellant's Testimony

[39] The documents included in respect of each of the subject sales were transaction records showing who the vendor and purchaser were. Each record showed the purchase price including GST on the purchase by Associated Cars and the sale price without GST for the sale to the named buyer. Serial numbers of the particular vehicle acquired and received by Associated Cars were noted on each transaction sheet. For every such transaction sheet there was a delivery document which identified, by matching serial numbers, the vehicle acquired by Associated Cars as the vehicle resold by it and purportedly delivered by Associated Cars to the pre-arranged buyer at a particular location.

[40] In the case of deliveries by AAI drivers, delivery locations were not identified by address but rather were identified more generally. For example, some 380 vehicles said to be delivered by AAI drivers to Hagersville were acquired from two dealers in Gananoque and sold to different buyers and had shipping documents that showed the delivery address as "New Credit Reserve". These shipping documents showed AAI as the point of origin.

[41] Other shipping documents showed a carrier as having delivered the vehicles. That is, there are two distinct types of delivery documents that the Appellant used as evidence: 1) shipping documents when AAI drivers were purportedly used, and 2)

shipping documents when a carrier was used. The only carrier identified on the shipping documents was RWA.[7]

[42] The 406 shipping documents that do not have a carrier have, for the most part, a signature by a Walter Sault who appears to have signed as the agent of AAI. Those shipping documents, for the most part, are also stamped by a Randy Walter Sault or a Margaret Sault. The stamps of Randy Walter Sault are initialled whereas the stamps of Margaret Sault bear her signature.

[43] The stamp has the following description if signed by Randy Walter Sault:

> Randy Walter Sault, a Commissioner, etc,. County of Brant and the Regional Municipality of Haldimand-Norfolk, while Band Administrator of the Mississaugas of the New Credit First Nation. Expire March 15, 1997.

[44] If the stamp was signed by Margaret Sault it had the following description:

> Margaret Sault, a Commissioner, etc,. County of Brant and the Regional Municipality of Haldimand-Norfolk, while Membership/Lands Officer of the Mississaugas of the New Credit First Nation. Expire March 15, 1997.

[45] Also, the shipping documents usually had a second stamp that appeared in one of two forms:

> MISSISSAUGAS OF THE NEW CREDIT FIRST NATION R.R. #6 HAGERSVILLE, ONTARIO N0A 1H0

or

> AUTOMOBILE **RECEIVED** AT NEW CREDIT RESERVE CON. 1 LOT 2 & 3 R.R. 1, HAGERSVILLE N0A 1H0 OFFICIAL NEW CREDIT COUNCIL [Emphasis added.]

[46] No signatures appeared with these latter stamps. The shipping documents without a stamp signed by either Randy Walter Sault or Margaret Sault all had the *received* at the New Credit Reserve stamp, again without signatures. For the purposes of these Reasons, I will refer to the shipping documents having the *received* stamp as those having "Receipt Stamps". The other stamps do not speak expressly to the issue of delivery at a Reserve.

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[7] There are 166 shipping contracts that show RWA as the carrier.

[47] At this point, I should note that Associated Cars was paid at the lowest end $56 and at the highest end $432 as a commission fee from the vendor and the buyer paid a fee of between $100 and $300 in respect of the subject sales. I also note that while no allegation was expressly made that the purchases and sales did not take place in a legal sense, the Respondent, having done a partial search, found a number of instances where no registration transfers were found. The Appellant's husband testified that not all transfers were registered.[8] Documentary proof of registered transfers was provided for 195 of the subject vehicles. The registrations being referred to are registered transfers from the initial vendors to Associated Cars and then from Associated Cars to the buyer.

[48] It does not seem to be in dispute that the buyer paid by cheque payable to Associated Cars and such amount was deposited in Associated Cars' account. From that account Associated Cars would pay the initial vendor. Based on such evidence, the Appellant relies on her testimony that all legal formalities were observed.

[49] I note here, as well, that Respondent's counsel undertook to provide a complete cross-reference of relevant facts pertaining to each of the subject sales. This resulted in a spreadsheet exhibit that Appellant's counsel viewed and approved. The spreadsheet allowed the Court to more readily see the course that each transaction followed as well as assisting the Respondent in highlighting some of the discrepancies on which reliance was placed.

[50] Indeed there are questionable aspects, if not discrepancies, on the face of many of the shipping documents. For example, in the case of AAI driver deliveries many delivery documents do not have the date of shipping and virtually none have the name of the driver or a specific address for delivery.

[51] As well, in the case of AAI driver deliveries there are many shipping documents that show the purported delivery of vehicles to have occurred days prior to the sale of or payment for the vehicles. There are also shipping documents that showed the purported delivery of the vehicles to have occurred days before Associated Cars was registered as the owner of vehicles. At the hearing, the Appellant testified that the discrepancies in dates were due to the fact that AAI conducts auctions on Tuesdays and Thursdays and auction sales were dated

[8] The Appellant testified that she thought all transfers were registered. However, her husband's evidence, noted in earlier footnotes, provides a reasonable explanation of the absence of registration in many dealer-to-dealer transactions.

accordingly. Since Associated Cars relied on AAI staff for both its auction sales business and the subject vehicle sales, the documentation for the subject vehicle sales was dated on a Tuesday or Thursday even if that was not the actual sale date.

[52] The shipping documentation also raises odometer reading questions which the Appellant acknowledged in written submissions. On 99 of AAI's sale forms,[9] the reading of the odometer on the vehicles exceeds the mileage of what was reported by the purported driver on the shipping documents. On 74 of the vehicles, the mileage of what was reported by the purported driver on the shipping documents exceeds the reading of the odometer on AAI's sale forms. Mr. McKenzie's testimony provided an explanation for such discrepancies at least in relation to the auction business. AAI's staff was not required to personally observe the odometer reading upon the receipt of a vehicle from a seller as any discrepancy pertaining to mileage of the vehicle would be raised by the ultimate buyer.

[53] The Respondent submits that the number of mistakes on the odometer readings are highly improbable and that the information may well have been provided by a third party because there was in fact no physical inspection of the vehicle by AAI on behalf of Associated Cars. The Respondent infers that the lack of physical inspection is a result of the vehicles not ever being physically located at AAI's premises.

[54] To the contrary, Mr. McKenzie testified that Associated Cars would rely on dealer vendors to supply relevant vehicle information such as model and year and odometer readings. If there was a mistake of any significance, the buyer could return the vehicle or negotiate a new price. The inference of the testimony was that Associated Cars was the intermediary in these transactions putting the responsibility on the initial vendor. In effect, it was suggested that it was common in the industry in dealer transactions for the initial vendor to warrant the vehicle specs relieving the intermediary, such as Associated Cars, from having to maintain meticulous and careful inspection records. Discrepancies, he said, were the norm in the industry of auction sales. Indeed, he testified: "I would say that 99 percent of the odometer readings are incorrect at every auction throughout the country." He also said that things are "far more accurate today than it was back then".

[55] Other testimony confirmed or asserted the following additional particulars:

[9] Sales documents are all on AAI sales forms even though the vendor in all cases was Associated Cars.

- AAI received no compensation for any of the services that it provided to Associated Cars;

- Such services included, for example, an AAI yard employee accepting delivery of a vehicle acquired by Associated Cars. An AAI employee would record vehicle particulars and attend to the delivery of the vehicles, in respect of the pre-arranged sales, to the purchaser once the paperwork was completed. Such paperwork, including the vehicle transfer registrations, was done either by the Appellant personally or by AAI's employees including its bookkeeper. The only difference in documentation amongst types of transactions was dependent on whether sales were dealer-to-dealer. If they were, one less sales document needed to be completed;

- The Appellant attended at the premises of AAI on a full-time basis as an employee of Associated Cars. When she did not personally attend to the preparation of documents relating to the purchases and sales undertaken by Associated Cars, she said she personally reviewed all of the documentation prepared by AAI staff;

- The Appellant said she frequently observed the vehicles that were involved in the subject sales being delivered to the yard and then being taken away for delivery once the documentation was complete;

- The Appellant said she did not know there was an issue that the subject vehicles had never been delivered to the reserves. Associated Cars ceased doing that business as soon as the Appellant learned that the CRA had a problem with deliveries;

- The Appellant admitted that she had never been to the Reserves and that she relied on AAI's drivers and RWA to make the deliveries and, as well, that she relied on the Receipt Stamps returned to her by the drivers after deliveries were made;

- The Appellant testified that the bookkeeper for AAI did most of the work relating to GST and that there had never been a GST issue or problem with any of AAI's compliance with the *Act* since the introduction of GST until late in 1996 or early 1997 when a CRA auditor indicated that there was a problem;

- The Appellant said that she relied on the fact that her husband had met with the CRA, as had AAI's accountant, to enquire about the *Indian Act* exemption and the GST and input tax credit regime that needed to be complied with in the context of that exemption. She said she also relied on her understanding of the way in which Associated Cars conducted its business in respect of the subject sales complied with CRA requirements. Her understanding that the exemption applied to property delivered to the Reserves led her to believe that the shipping documents and Receipt Stamps were sufficient.

Appellant's Position

[56] The Appellant submits that she exercised the degree of care, diligence and skill necessary to prevent the failure to collect and remit tax and that she had no reason to believe that the subject vehicles were not delivered to a Reserve and thereby exempt from taxation:

a. She was aware that for GST to be exempt for a sale of a vehicle, it would have to be sold to a First Nation and then delivered to a Reserve.

b. She took all the reasonable steps to ensure that the purchaser was a First Nation by requiring the purchaser to produce an Indian status card which was copied and filed with Associated Cars as proof of status.

c. Associated Cars relied upon common practice and forms to evidence delivery to a Reserve.

d. The Appellant had no reason not to rely on the documents relating to proof of delivery presented to her by AAI and the representations of Mr. McKenzie.

e. The sale of vehicles to First Nations was not special except that each transaction required proof of delivery, and in respect of the subject transactions, they were not through a public auction house.

f. The Appellant would match the shipping document to the corresponding sale document to ensure that sales to First Nations had proof of delivery to a Reserve.

g. The Appellant submits that from the particulars of the shipping documents, despite the deficiencies, a reasonable person would conclude that delivery to a Reserve had taken place.

Respondent's Position

[57] The Respondent submits that the Appellant did not exercise the degree of care, diligence and skill to prevent the failure to remit tax that a reasonably prudent person would have in the circumstances:

a. With respect to the subject sales, the Appellant reduced her handling of the transactions below her normal practice compared to the documentation for Associated Cars' day-to-day operation.

b. The Appellant provided no evidence of delivery fees charged to the buyer.

c. There were too many problems with the shipping documents to support the required delivery, i.e., in the case of AAI driver deliveries - missing driver or carrier name, shipping address, and so on.

d. The Appellant should not have simply relied on shipping documents from unknown individuals purporting to be First Nations.

e. The Appellant should have taken additional precautions with these "special" transactions.

[58] The Respondent submits that an adverse inference should be drawn from the fact that no key witnesses were called to clarify their role in the transactions.

[59] The Respondent also submits that on a balance of probability the delivery of vehicles did not occur at all.

Analysis

[60] My analysis will proceed under the following headings:

1. The Notional ITC – Legislative Policy and Abuses

2. The Application of Section 87 of the *Indian Act* to GST

Authorities and Administrative Practices

3. The Due Diligence Defence

(a) Onus of Proof and Underlying Corporate Liability

(b) The Context for Analyzing the Appellant's Due Diligence Defence: (i) The Appellant's Reliance
(ii) A Prudent Person's Reliance

4. Conclusions

1. The Notional ITC – Legislative Policy and Abuses

[61] When the GST came into force in 1991, subsection 176(1) provided as follows:

> 176. (1) **Acquisition of used goods** -- Subject to this Division, where
>
> (a) used tangible personal property is supplied in Canada by way of sale after 1993 to a registrant, tax is not payable by the registrant in respect of the supply, and the property is acquired for the purpose of consumption, use or supply in the course of commercial activities of the registrant, or
>
> (b) used tangible personal property is supplied in Canada by way of sale before 1994 to a registrant, tax is not payable by the registrant in respect of the supply, and the property is acquired for the purpose of supply in the course of commercial activities of the registrant,
>
> for the purposes of this Part, the registrant shall be deemed (except where the supply is a zero-rated supply or where section 167 applies to the supply) to have paid, at the time any amount is paid as consideration for the supply, tax in respect of the supply equal to the tax fraction [7/107ths] of that amount.

[62] As noted at the outset of these Reasons, this subsection as it read in the relevant period gave used car dealers ITCs on used cars purchased as if GST had been collected from the dealer by the vendor and remitted out of the total price paid, where, in fact, no collections, payments or remittances were required to be made. Such grant of a notional ITC to a purchaser of used goods, who was in the business of reselling such goods, was conceptually pure. It was intended to ensure that GST originally paid on supplies of new property was recovered from the government when a consumption purchaser resold the property into the commercial stream and the commercial buyer was then required to collect and

remit GST again. That resale would not generate the ITC for the consumption purchaser that a normal, uninterrupted, commercial stream of transactions would have allowed. Section 176 gave the lost ITC to the buyer who brings the used property back into the commercial stream. This was an outright tax benefit given to the buyer that Parliament might have believed would be passed onto the purchaser by decreasing the sale price. This is reflected in the July 1997 explanatory notes published by the Minister of Finance. There it is stated that the notional ITC was a mechanism "intended to notionally remove the portion of the current fair market value of the used goods representing tax that was originally paid on the goods and not recovered".

[63] At the Standing Senate Committee on Banking, Trade and Commerce, to which Bill C-70 (1997) was to amend the *Excise Tax Act*, Mr. Paré speaking for the Recreational Dealers Association of Canada, addressed his concerns over the elimination of the notional ITC. He noted that the notional ITC was implemented to establish equity in that it seeks to remove an element of double taxation that would otherwise exist. He further stated that it acts as a counterbalance in allowing dealers to better compete with private sellers of vehicles that do not charge GST on the sale. That again reflects the belief that the notional ITCs would be passed onto the purchaser who acquired a vehicle from a dealer.

[64] Still, the notional ITC was repealed due to the abuse. The illustration cited in the course of removing the notional ITC was of the scheme using First Nations as temporary buyers. The illustration was, simply, as follows:

New car dealer → First Nation = NO GST
First Nation → same dealer = NO GST; Dealer gets Notional ITC

[65] In this illustration, the fisc never received any GST but gave the notional ITC to the dealer regardless. This result does not reflect the government's policy behind the notional ITC. Hence, it was recognized as an abuse that needed to be corrected. The express target was sales to First Nations at a time when the application of the GST to them was uncertain but for CRA administrative practices. Still, illustrating an abuse that needed to be corrected, going forward, should not distract from the analysis in this case.

[66] For example, the CRA traced the vehicles that were involved in the subject transactions and found some at least were flipped more than once ostensibly through a Reserve creating multiple notional ITCs thus each creating a loss to the fisc.

[67] Consider the following somewhat modified illustration of an exhibit tendered at the hearing:

> Status Indian A acquires a new vehicle - no GST
>
> A sells to used car dealer X - no GST - Notional ITC
>
> X sells to Associated Cars - GST collected from Associated Cars
> - X Gets ITC
>
> Associated Cars sells to Status Indian B - No GST
> - Associated Cars Gets ITC
>
> B sells to used car dealer Y – no GST - Notional ITC

[68] The result here is that GST is collected once and ITCs are given three times. The process can still be repeated over and over so that the same vehicle will give rise to multiple transactions and multiple ITCs to recover taxes never paid. Using such examples, the Respondent suggested that such car-flipping schemes have led to criminal prosecutions.

[69] However, the car-flipping schemes that led to criminal prosecutions were alleged and found to be fraudulent, leading to convictions for conspiracy to defraud the government through the GST system. See *R. v. Prokofiew*.[10] No such allegations were made here. Indeed, to say that GST should have been paid and collected in this case requires the Respondent to insist that the transactions were legally effective and not a sham. As I said, the insinuations of criminality are nothing but a distraction in my view.

[70] Still, it is worth noting some of the factual findings of the trial court judge in *Prokofiew*. There was a finding in *Prokofiew* of false invoices and forged

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[10] [2004] G.S.T.C. 103. Templeton J. found three of seven accused guilty of conspiracy to defraud the government through the GST system. This case was appealed to the Ontario Court of Appeal, 2008 ONCA 585, and was overturned as the judge's lack of reasons did not allow for a meaningful appellate review of the fraud conviction. A new trial was ordered even though the Court of Appeal accepted the correctness of the trial judge's finding with respect to the existence of the conspiracy. Nonetheless, there is nothing in the Court of Appeal's ruling that would suggest that Templeton J.'s factual findings of particulars with respect to the wholesale used car industry can not still be used as evidence in the case at hand subject to the jurisprudence governing my being able to take judicial notice of it which will be discussed below.

documents. While the Respondent seems to have also played on the reliability of the shipping documents and the like, if not their genuineness, I can not find anything other than the documentation in this case is less than perfect.

[71] It is also worth noting that the evidence accepted by the trial judge in *Prokofiew* in large measure supports the testimony of the Appellant and her husband. In wholesale used car deals it is not uncommon that the dealers never see the vehicles and that they are often pre-sold and never reach the vendor's lot. Also, in large volume wholesale used car deals, it is not uncommon that dealers take each other's word as to vehicle specs without actually inspecting the vehicles.[11] As well, vehicle registration dates or even the absence of vehicle registrations is not determinative of actual dealer-to-dealer sales.[12] While this is not evidence in the case at bar, in fairness to the Appellant, such findings of another court, in my view, can not be ignored in terms of assessing the credibility of the Appellant, or more particularly that of her husband, given the need here to credibly identify comparable circumstances.[13]

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[11] *Prokofiew*, *supra* note 10 at para 86.

[12] *Ibid* at para 60-96.

[13] There is an issue of whether these specific facts relating to the wholesale used cars industry from *Prokofiew* can be judicially noted. In *R. v. Williams*, [1998] 1 S.C.R. 1128, the Supreme Court of Canada at paragraph 54 permitted judges to take judicial notice of facts found on evidence in previous cases:

> The fact that a certain fact or matter has been noted by a judge of the same court in a previous matter has precedential value and it is, therefore, useful for counsel and the court to examine the case law when attempting to determine whether any particular fact can be noted.

I have not afforded counsel this opportunity. My own review of the law dictates that I must be respectful of what has been referred to as the Morgan Criteria when determining whether a fact can be judicially noted. The Supreme Court of Canada in *R. v. Spence*, 2005 SCC 71, suggests that the analysis should start with the Morgan Criteria, regardless of the type of fact, and if the test is met, the matter can be judicially noted. If the fact is "adjudicative" and the Morgan Criteria are not met, the fact will not be judicially recognized. If the facts are "social" or "legislative", the Morgan Criteria are not necessarily conclusive. However, even if the facts are social or legislative, the Morgan Criteria will carry more weight if they are dispositive of the issue. That said, it is my view that judicial findings of normative business practices are "social". Further, while the credibility of the Appellant's husband's evidence as to industry practices is relevant in the case at bar, the corroborating findings in *Prokofiew*, are by no means dispositive. In words closer to those employed in *Spence*, the findings of industry practices in *Prokofiew* are not specific to the circumstances of a particular case and are properly linked to the adjudicative facts in the case at bar by helping to explain aspects of the evidence.

[72] All this is to say that the inferences here, and the examples of abuse and discrepancies, have been given little weight. As to the discrepancies, the Appellant's husband's un-coached testimony in this area was, in my view, credible.

2. The Application of Section 87 of the *Indian Act* to GST Authorities and Administrative Practices

[73] In *Union of New Brunswick Indians v. New Brunswick (Minister of Finance)*,[14] the issue before the Supreme Court of Canada was whether Indians in New Brunswick were required to pay Provincial Sales Tax on goods purchased off the reserve for consumption on the reserve. The court had to decide whether paragraph 87(1)(*b*) of the *Indian Act* applied to the tax levied under the former *New Brunswick Social Services and Education Tax Act*.

[74] While the court stated that the purpose of section 87 was to "preserve the entitlements of Indians to their reserve lands and to ensure that the use of their property on their reserve lands was not eroded by the ability of government to tax, or creditors to seize",[15] it concluded that section 87 does not exempt Indians from all sales taxes on property used on reserves just because of such use.

[75] In drawing its conclusion, the court stated that the tax levied by the province on a retail sale is not a consumption tax but a sales tax that is imposed at the time of sale (a point of sale test) on property off-reserve. Using a point of sale test obviates the need to be concerned about where the property is used. This approach allows Indians living off-reserve to purchase goods tax-free on reserve regardless of where the goods are to be used. The court does note that delivery of goods to a reserve may partially offset this problem.[16]

[76] Regardless of this decision of the Supreme Court of Canada, in the *Prokofiew* decision referred to earlier in these Reasons (which was heard some six years after *Union of New Brunswick Indians*) Templeton J. appears to have relied on CRA testimony as to CRA's policy on the application of section 87 of the *Indian*

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[14] [1998] 1 S.C.R. 1161.

[15] *Ibid* at para 8.

[16] *Ibid* at para 42.

Act with respect to sales to Indians.[17] That policy was said to be that the CRA had to be comfortable that the goods or services were *consumed* on reserve and that documentation that showed delivery to the reserve was *usually* sufficient. There was also testimony that the sale had to be to an individual *residing on reserve* but that *different auditors had different views as to whether goods – vehicles – had to be used on the reserves or had to stay on the reserve*.[18]

[77] Such evidence of the practices of different auditors does not coincide with the CRA's published practices at that time. The relevant Bulletin on its administrative practices regarding the application of GST to Indians is the one issued in 1993.[19] That was years before *Union of New Brunswick Indians*, but, in one aspect, was reflective of the decision by the Supreme Court of Canada in that case. The stated administrative policy was that Indians do not pay GST on property "acquired on reserve". Presumably, "acquired on a reserve", means "the point of sale was on a reserve". Neither residence nor place of use were, or are today, criteria for the application of this policy exemption under section 87.

[78] The Bulletin, however, acknowledged that further relief would be given under section 87 for off-reserve purchases by Status Indians if the property was delivered to a reserve. This policy might be said to have anticipated the statement in *Union of New Brunswick Indians* that a place of delivery test might resolve some issues.[20]

[79] Yet, regardless of one real similarity between policy and the finding in *Union of New Brunswick Indians*, regarding the point of sale test for on Reserve purchasers, the evidence heard by Templeton J, in *Prokofiew*, heard years later demonstrates that the law in this area was totally confused. CRA's own administrative practices,

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[17] *Supra* note 10 at para 68.

[18] *Ibid* at para 69.

[19] GST Administrative Policy B-039R dated November 25, 1993.

[20] It should be noted that the abuse of quick flips is not resolved by deliveries to reserves. Delivery failures are just a hook to catch some of the abuse of car-flips via a Reserve. Even if the *Act* had expressly included a delivery requirement, and if delivery was proven, the same abuse could have prevailed. In fact, in spite of the Respondent's theories, that may have been the case here.

which never changed,[21] do not seem to have been known to all auditors or applied by its auditors on a uniform basis.

[80] Forgive me if I say this sounds alarming, but it is. Evidence of CRA audit practices heard in *Prokofiew* bore no resemblance to its published policy at the time. For example, as I said, the stated administrative policy made it clear that neither residence nor place of use are criterion for the application of the policy exemption under section 87. Templeton J. in *Prokofiew* heard evidence to the contrary.

[81] One might conclude then that a clear understanding of, and the relevance of, administrative practices is difficult to assess even though in the case at bar it may have been all that a reasonably prudent person would have had to rely on in the circumstances. A further difficulty arises for me given that this case was argued by both parties on the basis the sole issue was whether there was delivery to a reserve or not. Limiting the issue, even to one that is potentially irrelevant, based on agreement of the parties who have accepted a stated administrative practice, strikes me as unacceptable. However, a highly respected judge of this Court has accepted such a limitation in the past.

[82] In *3258688 Canada Inc. v. R.*,[22] Justice Dussault at paragraph 43 states that: "at first glance at least, the decision of the Supreme Court of Canada in *Union of New Brunswick Indians v. New Brunswick (Minister of Finance)* seems to me to apply with respect to GST". However, having said that, he goes on in the same paragraph to say that he would refrain from any final determination as to whether the point of sale test was the only test where there is a sale of personal property to persons with Indian status, because the issue presented to him was based on the delivery test then set out in Bulletin B-039R.

[83] In effect, I am in that same boat except I am dealing with a director's liability.

[84] However, Justice Dussault's comment is a warning that if the CRA's administrative practices are challenged, the application of section 87 to GST may

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[21] I note that later revisions of B-039R, including the current version (B-039 GST/HST Technical Information Bulletin Administrative Policy – Application to Indians) dated June 2013, essentially contain no substantive differences in relation to the facts of this case.

[22] 2006 TCC 262 [*Informal*].

require further judicial consideration.[23] Indeed, as early as 2001 the delivery test seems to have been put in doubt by Justice Archambault of this Court.

[85] In *9000-6560 Québec Inc. v. Canada*,[24] the issue was whether the appellant was liable to collect tax on vehicles sold to native persons. No tax had been collected or remitted in respect of such sales. While delivery to a reserve appears to have been relevant to the decision in that case, there were no assumptions set out in the reply to the notice of appeal relating to delivery. Further, there was testimony of the CRA auditor that the assessment was not based on delivery and that he had assumed that all the sales took place on reserve and the vehicles where delivered there.

[86] The Crown's main submission in *9000-6560* was that the appellant was aware that the native persons were not acting on their own behalf but acted as "mandataries" or "prête-noms". The transactions were initiated by non-native third-party purchasers to be delivered to the native mandataries or prête-noms. As in the case at bar, it was shown that even before the purchase of the vehicle by the native person, payments by and the locations of further buyers were pre-arranged. As well, Justice Archambault found that in the majority of transactions, the intention of the native persons was to resell them quickly to such other buyers.

[87] Ultimately, Justice Archambault held in *9000-6560* that the appellant was not required to collect GST because he interpreted section 87 to say that "a native person is entitled to the tax exemption if the vehicle is situated on a reserve at the time of

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[23] David Sherman's editorial comment on *3258688 Canada Inc.* reported in [2006] G.S.T.C. 81 (TCC) notes that in that case Crown counsel argued that, since the contracts had been concluded off-reserve, the *Indian Act* exemption did not apply, and that it was only by administrative policy (Bulletin B-039R) that tax might not apply. Mr. Sherman suggested that Dussault J. was quite prepared to rule that Bulletin B-039R was too lenient, and that the sales were taxable simply because the contracts were concluded in Montréal, based on the 1998 Supreme Court of Canada decision in *Union of New Brunswick Indians*. While I find that Justice Dussault refrained from considering that case in respect of the application of the GST, I agree with Mr. Sherman's suggestion that the Court served notice that taxpayers can not necessarily rely on the Bulletin that replaced B-039R2. If the CRA chooses to assess, the test in *Union of New Brunswick Indians* may be the one to apply except possibly where there is finding that the tax on the transaction at issue is a consumption tax. However, in *3258688* Justice Dussault did not have to make such a ruling. He accepted the parameters of the case as presented to him. The evidence of delivery on the reserve was simply not credible, in his view, and he found as a fact that the vehicles had not been delivered to the reserve. Thus, the sales were taxable under the administrative policy in Bulletin B-039R.

[24] [2001] T.C.J. No. 47.

sale".[25] In the same paragraph Justice Archambault states that his interpretation was the same as that of the Deputy Minister of National Revenue as expressed in a letter. However, the translated portion of the letter quoted by Justice Archambault said no GST was payable on "purchases made on a reserve *or* purchases made off reserve that are delivered to the reserve." [Emphasis added.] The emphasized part of this quote has a footnote that states that this interpretation did not strike Justice Archambault as consistent with that adopted by the Supreme Court of Canada in *Union of New Brunswick Indians*. That is to say, Justice Archambault does not appear to necessarily accept place of delivery as the determinative test.[26]

[88] Indeed, he goes on to quote passages from *Union of New Brunswick Indians*. The passages quoted emphasize the "point of sale" test embraced by the Supreme Court of Canada in that case. Given the auditor's concession that he assumed the sales had been made on reserve, Justice Archambault allowed the appeal.

[89] Another point that I wish to note about Justice Archambault's decision in *9000-6560* is that in applying the point of sale test in *Union of New Brunswick Indians*, he found that the use of the purchased goods by the Status Indian on reserve was irrelevant to the question of the application of section 87. Whether the use was personal or business – including a business of quick flips financed by third parties to pre-arranged buyers on pre-arranged terms - section 87 applied. However, if it was a business, the Status Indian could be subject to the *Act*'s collection and remittance obligations on the sale to a person not entitled to the exemption.

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[25] *Ibid* at para 66.

[26] The Crown's concessions in *9000-6560* only make the water murkier in respect of the application of section 87 to the GST. Aside from moving against its own administrative practices in that case (as it did in *Phillips v. R.*, 2006 TCC 24), the uncertainty rests in the meaning of "point of sale". The *Act* imposes liability for GST *at the time of sale*. *Union of New Brunswick Indians* speaks of the *point of sale*. When a contract of purchase and sale is concluded at a particular place, the two concepts may be compatible. Otherwise, there may be a conflict between them in terms of determining the application of the GST in the context of section 87 of the *Indian Act*. Further, there is the issue as to whether the GST is a consumption tax. *Union of New Brunswick Indians* may have no application if it is. Is a value-added tax, levied before a consumer purchase (and refunded as an ITC), a consumption tax? Is the tax levied on the end user a consumption tax? In my view, the latter tax is clearly a consumption tax. It strikes me then that the point of sale test in *Union of New Brunswick Indians* might well apply in the context of the case at bar since the subject transactions were in the commercial stream and not a consumption purchase. Having said that, it must also be said that this Court has, to date, has not received adequate submissions to make such a finding at law.

[90] A similar point can be found in the case of *Tusket Sales & Service Ltd. v. Canada*.[27] In that case Mr. Pictou, a Status Indian, acquired vehicles from the Tusket Sales & Service Ltd. (Tusket) by using trade-in vehicles as consideration. Mr. Pictou did not charge Tusket GST on the trade-ins. The issue was whether Tusket could claim a notional input tax credit pursuant to former subsection 176(1) of the *Act* on sales to Mr Pictou. Pursuant to subsection 240(1) of the *Act*, Mr. Pictou would have to charge GST if he made a taxable supply to Tusket (the trade-ins) in the course of a commercial activity and consequently Tusket would not be entitled to claim the notional input tax credit. Ultimately, the court held that Tusket was entitled to claim the notional ITC because Mr. Pictou was found to have used all the vehicles as personal-use vehicles.

[91] All this is to say that the uncertainty in this area has been fuelled by CRA's inconsistent administrative views that have been met by this Court with hints of potential resistance to the CRA's published guidelines and to the application of *Union of New Brunswick Indians* to the GST.

[92] My view is that while delivery can be a practical test to administer (although proof of compliance can raise difficulties as seen in the case at bar), it is wholly outside the inherent principles that have guided the application of section 87 of the *Indian Act* in income tax cases. Further, as I have ventured to suggest in footnote 26, the GST is, in my view, a consumption tax to the end-user, so, if the sale is to a consumer *Union of New Brunswick Indians* may be of no application. The test might be to resort to a connecting factors test in relation to the application of section 87 of the *Indian Act* in GST cases as used in income tax cases. That is, if the sale of property is to a Status Indian for personal use, and that person and that use warrants a tax exemption under the connecting factors test, then no GST would be applicable.[28]

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[27] [2000] G.S.T.C. 60 [*Informal*].

[28] Admittedly this may not be a practical test and would be one that would not be well received. Agents of the Crown suffer enough to be responsible to know when, under the *Act*, GST applies. To be responsible to police the application of the *Indian Act* on top of that lacks sensitivity to the limitations of these agents that Parliament has appointed to act on the Crown's behalf. Suppliers in such circumstances, as agents of the Crown, should be given a role that will not discourage or complicate sales to First Nations or that would put them, suppliers, in the position of assuming that a Status Indian buyer's personal delivery to a reserve can not be relied upon: a position inherent in the CRA's long standing administrative policy. Perhaps a simple form of declaration that sets out the identifying information required by the CRA and a certification of its correctness, for a First Nations to complete, could be designed. Failing completion of the form and meeting its simple requirements, GST would have to be collected. Perhaps Ontario's resolution to this problem should

[93] On the other hand, I have suggested in footnote 26 that a sale by a value adding supplier is not a consumption tax so, in the case at bar, the point of sale test in *Union of New Brunswick Indians* would apply.[29] On that basis, it strikes me then that there is not a lot to be said for a delivery test in the context of the case at bar. Indeed, while there is yet no consensus as to the application of section 87 of the *Indian Act* to the GST, the delivery test has been seemingly questioned, if not rejected, by both Justice Archambault and Justice Dussault. In any event, this Court has not received adequate submissions to venture definitive answers.

3. The Due Diligence Defence

(a) Onus of Proof and Underlying Corporate Liability

[94] It is commonly accepted, as re-iterated in *Canada v. Buckingham*,[30] that directors have the onus to prove that the conditions required to successfully plead a due diligence defence have been met. [31]

[95] On the other hand, it strikes me that the onus could shift if the underlying corporate assessment can be attacked by the Appellant. Indeed, in my view, the Appellant can pursue such an attack.[32] In any event, in spite of the failure of

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be given some thought. Ontario HST Sales Tax Guide 80 published in September 2010, allows vendors to credit 8% of the HST for qualifying off-reserve supplies on a point of sale basis on sales of property acquired by a Status Indian for personal consumption. There is no delivery requirement or even residence on a reserve requirement that I can see in my review of this administrative policy. If the registered vendor does not charge GST in such cases an 8% credit is allowed in HST return.

[29] That is, the sale by Associated Cars to a Status Indian would be taxable. Then, on a quick flip by that Status Indian to a non-Status Indian, the Status Indian as vendor, if registered, will get an ITC and must collect and remit GST on the sale, as suggested by Justice Archambault in *9000-6560*. The result is the same as if Associated Cars never collected the GST in the first place. There would be no abuse there unless the Status Indian did the flip without collecting GST.

[30] 2011 FCA 142.

[31] *Ibid* at para 33.

[32] Regardless of decisions like *Zaborniak v. Canada*, 2004 TCC 560, the current approach taken by the Federal Court of Appeal appears to me to clearly favour its decision in *Gaucher v. Canada*, 2000 DTC 6678. In that decision the Federal Court of Appeal opined that the appellant was entitled to challenge the underlying primary assessment related to a section 160 (of the *Income Tax Act*) transfer of property. The court reasoned that it was the "basic rule of natural justice, barring a statutory provision to the contrary, a person who is not a party to litigation can not be bound by a

Associated Cars to appeal the underlying assessment, we have no admitted underlying failure. Indeed, by putting the delivery of the vehicles at issue, the Respondent has reintroduced the issue that likely faced Associated Cars. If I accept that delivery of the subject vehicles to a Reserve is sufficient to establish an entitlement to rely on section 87 of the *Indian Act*, as it appears I must,[33] then that broadens the Appellant's line of defence to include, in effect, fighting Associated Car's appeal. However, for the onus to be on Associated Cars in respect of the underlying assessment, there would have to have been an assumption by the CRA that there was no delivery. If that assumption was not made by the CRA, the onus shifts to the Crown. Similarly, if an assumption was not made that sales were not to non-Status Indians, the onus would shift to the Crown on that point.

[96] In fact, I might be inclined, subject to submissions that I do not have, to suggest that, in cases like the one at bar, the assumptions of the CRA made in the underlying corporate assessment that are material to the assessment under subsection 323(1) of the *Act* ***must*** be set out in the Respondent's reply to an appeal of an assessment against a director. How else can a person be assessed under subsection 323(1) direct their attention to a material fact at issue?

[97] It should go without saying that assumptions of critical importance to any appellant in any appeal should be clearly set out as a matter of natural justice. A director's liability case should not be an exception unless the underlying assessing assumptions have been mutually acknowledged or that the findings of the court in the adjudication of the underlying assessment reveal and deal with them. The due diligence defence of a director would then be limited to a more traditional analysis without allowing a re-trial of a factual issue. This is not a question of ignoring a

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judgment between other parties." The court further states that when the Minister issued a derivative assessment under subsection 160(1), the second person must have a full right of defence to challenge the assessment, including that of the primary assessment. In *Doncaster v. Canada*, 2012 FCA 38, the Federal Court of Appeal allowed the appeal on the grounds that the appellant was unfairly deprived of a chance to produce evidence to prove that the assessment might have been wrong. In *Abrametz v. Canada*, 2009 FCA 70, although the court reversed the trial judge's decision based on the insufficiency of the evidence relied on in respect of the correctness of an underlying assessment, that ruling inherently accepted the trial judge's finding that it was both "just and sensible" and that it be open for the appellant to challenge the underlying corporate assessment. Further, Justice Campbell in *Vrsic v. R.*, 2010 TCC 127, reviewed cases with opposing views and concluded that the principle of natural justice prevails.

[33] Recall that earlier, in these Reasons, I noted that I was in the same boat as Justice Dussault in *3258688*.

failure of the underlying company to pursue an appeal. It is a question of knowing what assumptions the Respondent can rely on as being proven.

[98] In this case, as in other subsection 323(1) cases that have come before this Court, no assumptions relating to the underlying assessments have been set out in the Reply to the Appellant's Notice of Appeal. However, there can be no doubt, based on Mr. Arner's testimony and that of the Appellant's husband, that the underlying assessment and that against the Appellant have always been based on the issue of delivery. There has been no complaint as to the lack of an expressly stated assumption in the Respondent's Reply, nor has there been a submission by the Appellant suggesting that the onus here has shifted to the Crown. Indeed, the Appellant agreed at the commencement of the hearing that the underlying assessment would not be put in issue. These factors, taken together, suggest that it is not open for me to find that the onus has shifted in this case. I will proceed then on the basis that the Appellant has the onus of proof.

[99] Still, I can not help but point out that the Respondent having put delivery to a Reserve at issue in this appeal, regardless that it was almost certainly the issue in the underlying corporate appeal, permits the Appellant to bring evidence to satisfy me that on a balance of probability, the subject vehicles were so delivered to a Reserve. That is, I can not find that the Appellant was not diligent to prevent a failure that never occurred.

[100] The evidence before me does raise questions as to whether or not the subject vehicles were delivered to a Reserve. However, the Respondent's view of the answer to this question is inevitably slanted. It is slanted by virtue of the Respondent's disapproval of the facilitator role played by Associated Cars in this car-flipping scheme designed to abuse a loophole in the *Act*. I will deal with my decision on the delivery issue, as and if necessary, since, while a decision that on a balance of probability the vehicles *were* delivered to a Reserve would absolve the Appellant of liability, a contrary finding is by no means fatal to the Appellant's reliance on the due diligence defence.

[101] The Appellant stands in a better position than Associated Cars even though she is clearly an inside sole director. Indeed, Associated Cars is her *alter ego* in every sense of that concept except to permit a piercing of the corporate veil in the context of section 323 of the *Act*.[34] Still, the due diligence defence allows her more

[34] While I am not aware of a case where the *alter ego* concept between individuals and a corporation has been considered in the context of a director's liability, the case of a sole shareholder, officer,

room. She does not have to prove delivery. She only has to prove that she acted reasonably. More specifically, she can rely on her belief that the subject vehicles were delivered to Reserves and that this was sufficient to relieve her of liability *if* a reasonably prudent person, exercising the skill and diligence required of a director in comparable circumstances, would also have formed a similar belief and, relying on that belief, would have done nothing more.

[102] Put this way, the due diligence test is not at odds with the purely objective test set out in *Buckingham*. In *Buckingham*, Mainville J.A. opines that the objective standard in *Peoples Department Stores Inc.(Trustee of) v. Wise*[35] is to be used for subsection 323(3) of the *Act*. In *Peoples*, the focus of the inquiry is subsection 122(2) of the *Canadian Business Corporations Act*, RSC 1985, c C-44 ("CBCA") which also addresses the "exercise of due care, diligence, and skill that a reasonably prudent person would exercise in comparable circumstances". While the court acknowledges the different focus of the CBCA, it still comes to the conclusion that the objective test applied in subsection 122(2) of the CBCA should also govern the application of subsection 323(3) of the *Act* under the principle of presumption of coherence between statutes.[36]

[103] Relying on *Peoples*, Mainville J.A distinguished, if not rejected, the test in *Soper v. Canada*.[37] In *Soper* dealing with an identical due diligence defence provision in the *Income Tax Act*, the court held that the proper test was an objective-subjective one.

[104] Mainville J.A emphasizes that the objective standard encompasses the factual aspects of the circumstances of the director whereas the former test considered subjective motivations. The court at paragraph 39 states the proper test to be employed is:

> 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.

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director and employee does raise questions of whether the actions of one are the actions of the other. Still, it strikes me that the intent of the due diligence defence to the director's liability provisions in the *Act* is to permit recognition of the corporate veil, not the piercing of it.

[35] [2004] 3 S.C.R. 461.

[36] *Supra* note 30 at para 34.

[37] [1997] 3 C.T.C. 242 (F.C.A.).

[105] Such an objective test is said to impose a stricter more stringent standard on inactive or outside directors. That is, reliance on one's own inaction will not assist a director if a reasonably prudent person appointed in that position would, in the circumstances faced by the assessed director, have acted differently to prevent a failure that resulted in a liability to the corporation.

[106] It strikes me then that, most authorities preceding *Buckingham* will no longer assist directors who plead reliance on others due to their own personal lack of experience or knowledge.[38] That is, a lack of experience or knowledge, in itself, would not qualify as part of a relevant context. On the other hand, reliance on the historical competence of staff and systemic compliance can be seen as a relevant context that needs to be assessed in the objective light of what a reasonably prudent person would do.

[107] Similarly, the ability to rely on one's own highly qualified skill set, one's own personal experience and substantial direct involvement, is also a relevant context that needs to be assessed in the objective light of what a reasonably prudent person would do.

[108] That is, while under *Buckingham* inactive, outside directors who only have superficial knowledge of, and involvement in, the affairs of the corporation can no longer rely on passive participation to relieve them of liability whereas a highly qualified and experienced active, inside director will not likely avoid a higher standard of care. Their liability will no doubt be assessed in the light of what a highly qualified reasonably prudent and active inside person, with similar knowledge of the circumstances, would do. This should not be seen as adding a subjective element to the test. Rather, it should be seen as a relevant circumstance. As well, assessing the credibility of a director may turn on the improbability of asserted reliance on asserted events which could bring a subjective element into the analysis.

[109] In any event, aside from labelling the nature of the analysis of the due diligence defence, it remains of prime importance to identify the context in which to apply the relevant test. That context includes the Respondent's not so subtle inferences here, that the Appellant knew or ought to have known that there was a CRA perception that Associated Cars was facilitating a scheme to misuse the *Act*, and that to avoid being assessed for the GST care had to be taken to see that the

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[38] See *Constantin v. R.*, 2012 TCC 425 [*Informal*].

subject vehicles were in fact delivered to a Reserve. I agree. What the Appellant knew or ought to have known in this regard, is a very relevant and necessary contextual finding to make. That is, while I have discounted the Respondent's insinuations of the Appellant's role in a car-flipping scheme as a reason to discredit her, determining the environment facing the Appellant is a relevant part of the context required to apply an objective test.

(b) The Context for Analyzing the Appellant's Due Diligence Defence

[110] The context of the due diligence defence analysis requires an examination of the following issues:

1. Did the Appellant rely on a CRA officer's assurance that, or have other knowledge of CRA's policy that, delivery to a Reserve *per se*, with supporting evidence, would ensure the application of section 87 of the *Indian Act*, and was such reliance relevant to determining the application of the due diligence defence?

2. If so, would a reasonably prudent person, exercising the skill and diligence required of a director in comparable circumstances, have relied on delivery to a Reserve as the sole requirement to ensure the application of section 87 of the *Indian Act*, and if so would such person have done more to verify or satisfy oneself that there was no failure to deliver the subject vehicles to a Reserve?

(i) The Appellant's Reliance

[111] Under this heading, I will address the Appellant's understanding that delivery to a Reserve would be sufficient to ensure the application of section 87.

[112] Putting aside the *Indian Act* for the moment, it should be noted that assessing the requirements of the *Act*, itself, have led to considerable litigation. That is to say: considering the *Act* as whole, liability for GST is not always an easy question. Yet, Parliament has seen fit to require vendors of goods and services to make such determination at their peril.

[113] Regrettably, this has, in my view, led to some injustices. For example, consider where a supplier has followed guidance from the CRA as to whether a supply was a taxable supply, perhaps by telephone with a CRA officer, or even from a CRA publication. The supplier might rightfully believe an injustice has

been done when an assessment is issued that contradicts the guidance given and followed, and the supplier is then told by this Court that such guidance was not binding (even though it was likely well intended).[39]

[114] I make this point to distinguish it from the case of a *director's* reliance on guidance from the CRA. While a corporate supplier can not rely on guidance from the CRA as a safe harbour, that is not the case in respect of the operation of the due diligence defence afforded to directors.

[115] As well, I make this point to draw an analogy between a director's reliance on guidance from the CRA in respect of the *Act* and such guidance in respect of the application of section 87 of the *Indian Act*. While a taxpayer can not necessarily rely on guidance from the CRA in respect of section 87 of the *Indian Act*, indeed it did not suffice in *9000-6560*, a director must be able to rely on such guidance in respect of the operation of the due diligence defence afforded to directors. An independent legal opinion might be preferable and safer in some cases; however, such recourse should not, in my view, be imposed as a necessary precaution on businesses. On the other hand, directors have a fiduciary duty and there will be circumstances where directors might well be liable for the imprudence of not getting legal counsel.

[116] Returning then to the question of whether the Appellant had knowledge of CRA's practices, that delivery to a Reserve, with supporting evidence, would be sufficient to ensure the application of section 87 of the *Indian Act*, I find that she did.

[117] She testified that, among other things, she relied on RWA's shipping documents and the Receipt Stamps on AAI driver documents as being sufficient to warrant not collecting and remitting GST on the sale of the subject vehicles. That is, she was clearly aware of and understood CRA's position as to the need for deliveries to a Reserve and to have documentary evidence of such deliveries in order to ensure the application of section 87 of the *Indian Act*. I accept that she relied on such understanding and that she believed that her actions and responses to such understanding were consistent with her duties as a director and a sufficient exercise of those duties. Applying the objective test, this finding leads to the

[39] The injustices here are that well-intended vendors, trying to be compliant, are assessed years back without any practical ability to recover the GST from the recipient of their supplies. As well, the injustice, financially, will include interest and often penalties.

question of whether a reasonably prudent person would have relied on such an understanding and have believed that the Appellant's actions and responses to such understanding were consistent with the duties of a director and a sufficient exercise of those duties to prevent a failure to collect and remit GST.

[118] Importantly, I note here that while I have concluded that the Appellant knew of the CRA's delivery requirement, I have doubts as to whether her husband revealed all the details of his talks with Mr. Arner to his wife. I question what, if anything, she knew of the CRA's reasons for its warning to be cautious or its view of the need for "almost perfect" records or what would constitute "almost perfect" records. She would not have knowledge of the uncertainties that haunt the issue of when section 87 of the *Indian Act* operates to exempt native persons from paying GST. Further, I do not find as a fact that the Appellant knew of CRA's offer to assist in the documentation. Indeed, I have concerns about suggesting that she or a reasonably prudent director would go along with that offer.[40] It did nothing but add to the problems of the appellant in *9000-6560*. On the other hand, she had to be aware that the subject transactions were going to be watched over closely.

[119] With those exceptions, I accept that the Appellant knew as much as her husband about the cautions warned of by the CRA and AAI's accountant. While this should not be an automatic assumption considering that it is not contested that she was not at meetings where such cautions were discussed, in this case it is apparent to me that the Appellant is intimately familiar with the operations of both the businesses that Associated Cars took over and the business of AAI as well. She

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[40] It strikes me that the auditor in this case might be seen as a wolf in sheep's clothing. He is clearly aware by advance notice from Mr. McKenzie and his accountant that a car-flipping scheme was about to be implemented. He offers to help by reviewing the documentation in advance? Perhaps I am being a bit cynical, but is there not another agenda here - to learn in advance the players involved in this car-flipping scheme - perhaps with criminal conspiracy charges in mind? While I might suggest that a reasonably prudent person would "walk away" from the subject transactions knowing that the CRA was closely watching over them, I can not accept that position. I can not accept "walking away" as relevant course of action where doing so would be the result of CRA intimidation brought on by a policing role being engaged in, without specific policing authority, at a time when car-flipping schemes were being viewed by the CRA as a criminal activity. Where a government body has regulatory or administrative functions, as well as the function of investigating penal offences, a shift from one, to the other, affects the applicable *Canadian Charter of Rights and Freedoms* ("Charter") standards. In particular, where the predominant purpose of an enquiry is to determine penal liability, regulatory and administrative powers cease and officials are restricted to investigative powers appropriate in the penal context. See *R. v. Jarvis*, [2002] 3 S.C.R. 757 and *R. v. Ling*, [2002] 3 S.C.R. 814.

knew and understood the business structure imposed by her formation of Associated Cars. She knew why it was formed and how it was to be operated. She knew the delivery procedures differed for each of Associated Cars' two distinct businesses. Delivery of vehicles acquired by auction was the responsibility of the buyer. Delivery of the subject vehicles acquired for pre-arranged sales to Status Indians were Associated Cars' responsibility. She may not have been at the meetings where GST cautions were discussed in respect of vehicles acquired for pre-arranged sales to Status Indians, but she knew of the GST collection and remittance requirements that went hand-in-hand with Associated Cars' other business. Almost certainly she would have enquired why the subject vehicles would be exempted from that regime and would have been alerted to being cautious.

[120] This fills out the context in which the actions of a reasonably prudent director are to be compared to those of the Appellant. The issue then is to determine what a reasonably prudent person's actions and responses would have been in these circumstances.

(ii) A Prudent Person's Reliance

[121] First, I find that our hypothetical director in comparable circumstances, would also have relied on an understanding of CRA policies that delivery to a Reserve with supporting documentation would be sufficient to ensure the application of section 87 of the *Indian Act*.

[122] As well, I find that our hypothetical director would proceed with some caution in dealing with First Nations claiming protection from taxation pursuant to the *Indian Act*. The issue of liability under the *Act* has all but been eclipsed in this case by the question of the application of the *Indian Act*. Indeed, the law on the application of section 87 of the *Indian Act* is very complex and ever evolving.[41] Even an expert in this area might be hard pressed to give an unqualified opinion. As such, would our hypothetical director, even with working knowledge of the business practices of the underlying corporation, including GST compliance, and who had access to professional accounting advice, done more than familiarize themselves with CRA guidelines? In my view, the answer is a qualified "no". While the circumstances of this case seem to beg for further enquiry, a reasonably prudent person should not presume or even be suspicious of fraud or forgeries just because the CRA is concerned with the reliability of imperfect shipping documents

[41] For example see: *Bastien Estate v. Canada*, 2011 SCC 38.

reflecting deliveries to a Reserve. The thought of that is disturbing. However, some enquiry is appropriate and the question remains as to whether a reasonably prudent director would have acted differently.

[123] Any enquiry by a director, short of getting a legal opinion, would have, at the least, resulted in being more informed about CRA practices as to the requirements for the application of section 87 of the *Indian Act*. That enquiry, most practically made though AAI's accountant, would have led to the discovery of publicly available information such as Technical Information Bulletin B-039R, dated November 25 1993, dealing with the "Application of the GST to Indians" (the "Bulletin"). It sets out the administrative practices of the CRA on the application of GST to Indians as they were during the relevant period.

[124] Relevant portions of the Bulletin are attached to these Reasons as Appendix 1.

[125] The Bulletin highlights the following two administrative requirements: that the vendor must maintain proof of Indian status; and, the delivery must be to a Reserve. There is no indication as to the need for the vendor who delivers the property to document a specific address. On the other hand, where delivery is made by a vendor's agent, a Reserve address appears in the Bulletin as an example of proof of delivery although other evidence could suffice. Such distinction can only bear to the reliability of a delivery by an agent. Regardless, I prefer to accept that the CRA can not insist on an administrative policy that requires proof of delivery to a particular on-reserve address.[42] In any event, I note that the Bulletin is not precise as to what constitutes delivery and even the evidence said to be required to satisfy compliance with the delivery directive, can not be said to be all encompassing.

[126] Having said this, I emphasize I am not embracing administrative practices without qualification. It is well established that CRA polices "are not determinative but are entitled to weight and can be an important factor in cases of doubt about the

[42] The AAI driver shipping documents appear to have an agent's signature. The signed documents do not show a delivery address - just the name of the Reserve where delivery was said to have been made. I have no reason to believe that AAI drivers would not know where to deliver the vehicles to obtain Receipt Stamps or the more general Reserve stamps. Although the Respondent's argument puts considerable focus on the reliability of the shipping documents, the latest Bulletin B-039 (June 2013) ironically states a freight bill is adequate evidence of delivery to a reserve. In some cases, it appears that some auditors will require unambiguous or near perfect freight bills.

meaning of legislation".[43] That is, while administrative practices are certainly not binding,[44] this Court has been reluctant to ignore an administrative practice that assists a taxpayer in cases where the legislation is ambiguous.

[127] My approach then is to compare the Appellant's and the hypothetical director's approach to resolving the questions of what constitutes delivery and what constitutes sufficient evidence to prove delivery. The circumstances facing the Appellant set the context for this approach.

[128] At the risk of repeating myself somewhat, I would list the circumstances facing the Appellant as follows:

- The Appellant is a sole director of Associated Cars responsible for the day-to-day management of its affairs. Further, she was knowledgeable in respect of Associated Cars' business, and experienced and involved in the day-to-day management of its affairs. The extent of day-to-day involvement might be sufficiently relevant to warrant more discussion;

- There were warning signs that there may be an issue in not charging GST to First Nations. As stated above, the Appellant's testimony satisfies me she recognized such warning signs. This circumstance requires a fuller discussion as it is at the heart of the Bulletin compliance issue raised above;

- There were warning signs that an audit might follow. I must find that she knew or ought to have known that there was a high probability of this;

- There were cautions and insinuations known to the Appellant that should have caused her to impose a more meticulous documentation regime on Associated Cars so as to avoid the discrepancies and arguably suspicious circumstances of acting as facilitator on pre-arranged sales to a Reserve. I am reluctant to give such circumstance much weight in light of my comments on *Prokofiew*;

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[43] *R. v. Nowegijick*, [1983] S.C.J. No. 5 (S.C.C.) at page 5044.

[44] *General Electric Canada Company v. Canada*, 2011 TCC 564 at para 101.

- There was reliance on driver shipping documents with Receipt Stamps, and on RWA shipping documents. Such reliance requires a fuller discussion as they are not free of potentially relevant issues;

- There was reliance on the Appellant having seen a number of the subject vehicles arriving at and being moved about and from the lot. This testimony was weak at best, if not dubious, and I have given it no weight;

- There was reliance on AAI's staff and experience in attending to much of the documentation and deliveries. This warrants further discussion;

- While the only proof of the Indian status of vehicle purchasers was the sworn testimony of the Appellant, I take it that the assumptions in the underlying assessment did not take issue with the registered Indian status of the purchasers;

- There is no evidence that Associated Cars, responsible for deliveries, had any responsibility to bear the cost of deliveries. This too warrants further discussion.

[129] I will address the circumstances listed above that warrant further discussion as follows:

1. The extent of day-to-day involvement in the affairs of Associated Cars;
2. Warning signs of section 87 issues and Bulletin compliance;

3. Reliance on AAI's staff and experience in attending to much of the documentation and deliveries;

4. Reliance on driver documents, Receipt Stamps and RWA shipping documents;

5. The Cost of Deliveries.

1. <u>The extent of day-to-day involvement in the affairs of Associated Cars</u>

[130] As I said, the Appellant was very involved in the day-to-day management of Associated Cars. She knew GST must be collected and remitted on the sale of vehicles. She knew failure to collect and remit would cause Associated Cars to be liable to pay GST unless there was an exception in the law to its normal obligation to collect and remit. She would have known, or ought to have known, that a liability to remit where there had been no collection would result in a large indebtedness with little opportunity to get reimbursed from even five purchasers who would have relied on section 87 protection.

[131] Not collecting GST on any transaction would alert a reasonably prudent director to get a good understanding as to why GST need not be collected. I do not find that the Appellant did enough in this case to alert herself as to how to act to prevent a failure. That does not in itself mean what she ended up doing, and relying on, were not sufficient due diligence to save her from liability, but it is a factor that weighs against her.

2. Warning signs of section 87 issues and Bulletin compliance

[132] The Appellant's testimony satisfies me that she understood the need not only that the delivery of the subject vehicles be to a Reserve but that the sale be to a Status Indian.

[133] While the Appellant produced no evidence that the five purchasers were Status Indians, I accept that they were. Neither the pleading nor submissions make an issue of this. I noted earlier, in these Reasons, that I do not know the assumptions made in respect of the underlying assessment. While I was ready to accept an assumption of no delivery to a Reserve, I am not inclined to accept an assumption was made that the purchasers were not Status Indians. Further, the Respondent, knowing the particulars of the five purchasers, could readily have brought evidence questioning their status if that had been an issue in the underlying assessment. Again, I make the point that it is necessary for the Respondent to set out the assumptions made in respect of the underlying assessment when it proceeds against a director under section 323 of the *Act*.

[134] As to the delivery requirement, I am of the view that while the Bulletin sets out a practical and somewhat lenient administrative regime, it does not present a narrow picture of what constitutes "delivery" to a Reserve in the context of section 87 of the *Indian Act*. As I read the Bulletin, any credible indication of the subject vehicles being taken to a Reserve would suffice.

[135] I ask then, what evidence was put before the Court to support the Appellant's testimony that she believed the vehicles were all delivered to a Reserve?

[136] She suggested that she could see many of the subject vehicles arriving and departing from AAI's yard, which added confidence to her belief that they were being delivered as required. As well, she trusted AAI's experience and good business history to comply with both the contractual and section 87 requirements respecting delivery of the subject vehicles to Reserves. These factors would contribute to her reliance on Receipt Stamps and on RWA shipping documents as proof that the vehicles were delivered as required.

[137] As to her seeing the subject vehicles on the lot, portions of her testimony revealed that there were so many vehicles going through the lot, that she was not sure she could identify the subject vehicles or the drivers that would have delivered them to a Reserve.

[138] Even though I accept that the Appellant believed that the subject vehicles were delivered to a Reserve, that is not to say that a hypothetical reasonably prudent person, who recognized the warning signs respecting the need to deliver the subject vehicles to a Reserve, would not have done more to corroborate and demonstrate that such belief was warranted. AAI does not have a history of vehicle deliveries. Ordinarily, to rely on AAI's shipping documentation would be neither prudent nor reasonable in the circumstances. However, considering that the circumstances include her not knowing of the need for nearly perfect records and given that industry standards in the dealer-to-dealer used car business are lax, I am less certain that a reasonably prudent person would have provided more input and direction over the delivery process, even given the Bulletin's emphasis on documentation.

[139] Still, this factor weighs against the Appellant.

3. Reliance on AAI's staff and experience in attending to much of the documentation and deliveries

[140] It is necessary that I make a finding on the extent that the Appellant relied on AAI's staff. The first reliance is in respect of the deliveries themselves and the second is in respect of the documentation. While the documentation is far from

perfect, perfection is not a requirement.[45] The documentation is somewhat sloppy but in my view the Receipt Stamps and RWA shipping documents are reasonable evidence of the deliveries.

[141] On the other hand, as I noted earlier in these Reasons, the experience and knowledge of the Appellant form part of the objective context here. She knew that AAI's staff would not typically arrange for deliveries and therefore would not have had routine systems and documents for use in such cases, and any such routines and forms of documentation would not likely have paid special attention in their use for section 87 and GST purposes. Even if she knew that there was no need for near perfect documentation, a reasonably prudent person might have done more in the circumstances to set up verifiable delivery procedures and record maintenance. A reasonably prudent person in the circumstances might have reviewed, if not monitored the shipping documentation, more frequently. Had that been done, changes might have appeared necessary with the result that the documentation would have not been as sloppily and carelessly filled out as it was. The very existence of sloppy documentation just reinforces a finding that the Appellant's conduct was sub par.

[142] However, to the extent that it was sub par, it was so in the context of GST record keeping requirements, not in the context of dealer-to-dealer wholesale used car industry. As such, I am not inclined to give this factor as much weight as a factor that would otherwise weigh more heavily against the Appellant. A reasonably prudent person in the used car business would not likely have seen the need to change the systemic and documentary approach normally taken in respect of dealer-to-dealer transactions believing, as did the Appellant, that industry norms would be acceptable even in the context of sales to First Nations. In coming to this view, I have, admittedly, de-emphasized the question of whether an auditor's warnings would have been better heeded by a reasonably prudent person. I have considerable discomfort with this aspect of the case given my view that the warnings were likely made in the context of the CRA's looking into the criminality of car-flipping schemes.[46]

4. Reliance on driver documents, Receipt Stamps and RWA shipping documents

[45] See *Smith v. R.*, 2001 FCA 84, Justice Sharlow stated at para 14 "the standard is reasonableness not perfection".
[46] *Supra* note 40.

[143] I find these to be helpful to the Appellant. Even being cautious, I do not believe I can suggest that our hypothetical director would have believed that the Receipt Stamps were fraudulent. As an isolated factor, I would lean toward a finding that a reasonably prudent person would in the circumstances accept a reserve Receipt Stamp as supporting the delivery to a Reserve requirement.

[144] In this case, there are some 166 deliveries by RWA and some 406 were purported to be delivered by AAI drivers. The RWA shipping documents, although not perfect, are adequate proof of delivery to a Reserve.[47] Of the 406 AAI driver delivered vehicles, 333 have Receipt Stamps. That is a high enough percentage to encourage me to find that reliance on the Receipt Stamps would meet the bar set by a reasonably prudent person in the circumstances of this case.

[145] This factor weighs heavily in favour of the Appellant.

5. The Cost of Deliveries

[146] It is unclear whether Associated Cars was being paid the same amount to handle the registration aspect of its business for both the auctioned vehicles and the subject Reserve destined vehicles. What the evidence shows is that Associated Cars made from $100 to $300 on each of the subject vehicles that was AAI driver delivered. The RWA deliveries were all at $100 and the delivery charges were virtually all COD.

[147] Arguably, one might speculate that the $100 fee was the handling and registration fee. Any more might have related to delivery where RWA was not involved. However, the Appellant's testimony in this area consisted mostly of "I do not remember". When she attempted to recall, she confirmed only that Associated Cars was responsible for deliveries. She did recall that buyer pick-ups were the norm for AAI's auction business but when AAI did a delivery on that side of the business, a delivery fee of $75 to Toronto was charged to the buyer.

[148] The problem here is that so many years have passed. It is hard to take an adverse inference from a failure to remember. Still, while considerable time has elapsed, the issues here and the assessments occurred not too long after the relevant period ended. One might have hoped that memories and records at that time would have been preserved for as long as it took to dispose of these matters.

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[47] *Supra* note 45.

[149] In spite of these memory issues, I do not find that they are the result of the Appellant trying to be less than forthright with the Court. She could have said what seemed apparent, namely that Associated Cars did charge a delivery charge when AAI drivers did the deliveries as evidenced by the volume of higher charges for AAI driver deliveries compared to the fixed COD charges shown on the RWA shipping documents. She made no such self-serving statement.

[150] I find this factor to be of little over-all influence

4. Conclusions

[151] At the end of the day, the due diligence issue, in my view, comes down to consideration of whether the Appellant can be seen as being wilfully blind to her duties as an inside sole director by relying too much on the experience and business practices of AAI as well as relying too heavily on the shipping documents as imperfect as they were. However, as noted earlier, the application of the objective test in *Buckingham* may not lower the diligence bar for a director with a high skill set. The greater the director's skill set, personal experience and direct involvement in the business of a corporation, the harder it will be to avoid a finding of wilful blindness or careless, or imprudent, reliance. If the Appellant was to lose her appeal, it would have been on the basis that given her skill set and experience, she could not avoid a finding of wilful blindness. However, after serious thought and some reservations, that was not a finding I could make in the circumstances of this case.

[152] The Appellant's presence and involvement in the business and the documentation she relied on, as imperfect as it was, ultimately have saved her from losing her appeal. While a director could have done more to better evidence delivery to a Reserve, as I said, perfection is not required.

[153] Still, my comparisons with the actions of a reasonably prudent person, exercising the degree of diligence and skill expected of such a person in comparable circumstances, have been less than clearly conclusive either way. On balance however, I still find in favour of the Appellant; although, there was a temptation here, given the closeness of the call, to split hairs and assess a more reasonable penalty for the Appellant having allowed Associated Cars (that I have called her *alter ego*) to be engaged as an intermediary in a business about which serious cautions had been expressed. I could find that the evidence was sufficient to find that all the RWA deliveries were to a Reserve and the evidence of deliveries

to a Reserve by an AAI driver was only supported by Receipt Stamps in respect of 333 such deliveries. Indeed, that may have been a good settlement position.

[154] However, it would be unreasonable to find that our hypothetical director could not rely on the adequacy of some 80% of the documentation showing delivery to a Reserve as sufficient to confirm the probability that *all* deliveries were to a Reserve. To impose a higher level of due diligence would, in my view, be unacceptable. Even a more skeptical inside director is not going to follow 572 vehicles to a destination. Nor is an inside director going to do a daily detailed audit of the documentation of 572 transactions. The Appellant was involved and was satisfied with the documentation as being within industry standards. I can not and do not find that a reasonably prudent director in comparable circumstances would have necessarily done something different to enhance the documentation. This goes right to the heart of the objective test.

[155] I acknowledge that I made my decision without giving equal weight to all the factors I have considered to be relevant. For example, a finding that a reasonably prudent person would, but for industry standards, have done more systemically to ensure deliveries to a Reserve, was ultimately given less weight than the Appellant's reliance on the shipping documents.

[156] While not a factor in my decision, I question the propriety of a CRA auditor being too closely involved in a taxpayer's business affairs where it could be seen as taking a policing role looking into a suspected criminal activity.[48] It would trouble me too much, in these circumstances, to say that a director's record keeping duties move from industry standards to nearly perfect. As well, it underlines the imprudence of *insisting* on something (evidence of delivery) where compliance seems dependent on an unreliable CRA administrative practice as preached by a particular auditor.

[157] As I said earlier in these Reasons, the applicability of the *Act* to Status Indians is far from decided. While I said that I was in the same boat as Justice Dussault who found it necessary to direct his judgment to the delivery issue posed by the parties, I make the distinction here that the depth of the analysis, in a director's liability case, must be broadened. In doing so, I find in favour of the Appellant.

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[48] *Supra* note 41.

[158] Accordingly, the appeal is allowed in its entirety, with costs. There is no reason to deal with the underlying assessment issue as to whether the subject vehicles were delivered to a Reserve.

Signed at Ottawa, Canada this 26th day of July 2013.

"J.E. Hershfield"

Hershfield J.

APPENDIX 1

Individual Indians

When the purchaser is an individual Indian, vendors must maintain adequate evidence that a sale was made to an Indian, as registered under the *Indian Act*. Revenue Canada will accept as adequate evidence, notation on the invoice or other sales document which is retained by the vendor, of the nine or ten digit registry number or the band name and family number (commonly referred to as the band number/treaty number).

Indian bands and Band-Empowered Entities

When the purchaser is an Indian band or band-empowered entity, a certificate must be provided and retained by the vendor that the property is being acquired for band management activities.

Please [see above] regarding the entitlement for tax relief on acquisitions by incorporated and unincorporated band-empowered entities.

The certification should be similar in wording to the following:

This is to certify that the *Name of band or band-empowered entity* is acquiring property on the reserve or is acquiring services for band management activities. This supply will not be subject to the Goods and Services Tax.

……. ……..
Signature of Authorized Officer Date

…….
Title of Signing Officer

Off-Reserve Purchases of Property Delivered to a Reserve

Along with the individual's Certificate of Indian status card number or the certification by the Indian band or band-empowered entity, the vendor is required to maintain proof of delivery (e.g., waybill, postal receipt, freight bill, etc.), indicating the destination of the property to a reserve.

DELIVERY

If the store from which property has been acquired is not located on a reserve, then the property must be delivered to a reserve for the purchase to be relieved from the GST.

The property must be delivered by either the vendor or an agent of the vendor.

If these conditions or the provisions for remote stores described on page B228 are not met, the normal GST rules apply.

Vendor

Where property is delivered to a reserve in the vendor's own vehicle, the vendor must maintain proof that delivery was made to a reserve. This will be indicated on the invoice of the vendor and the vendor's internal records, e.g., mileage log, dispatch records.

Such proof must be maintained in addition to the proof of Indian status or certification by an Indian band or band-empowered entity.

Normal GST rules will apply where an Indian, Indian band or band-empowered entity that is the purchaser takes possession of the property off a reserve and delivers the property to a reserve in his or her own vehicle.

Vendor's Agent

Where the property is delivered by the vendor's agent to a reserve, the vendor must maintain:

- proof of Indian status or certification by the Indian band or band-empowered entity; and

- proof of delivery being made to the reserve (e.g., a waybill, postal receipt showing a reserve address, etc.).

An agent of the vendor includes an individual or company under contract to the vendor for making deliveries (e.g., postal services, trains, boats, couriers, etc.). The vendor would normally bear all the risks of the agent during the course of the delivery as if these risks were the vendor's own, unless specifically covered in the agency agreement.

A carrier who is under contract with the recipient is not regarded as the agent of the vendor. In addition, undertakings by purchasers of property to deliver the property to themselves as agents of the vendor are not acceptable to the Department.

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