Docket: 2012-1806(IT)G

BETWEEN:

ALLAN WARDLAW,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on January 21, 2019, at London, Ontario.

Before: The Honourable Justice Gaston Jorré, Deputy Judge

Appearances:

For the Appellant:	The Appellant himself
Counsel for the Respondent:	Sonia Bellerive

JUDGMENT

The appeal with respect to the 2009 taxation year is dismissed in accordance with the attached reasons for judgment. If the parties are unable to agree on costs within 60 days of the date of this judgment, they may make submissions in writing to the Court on the matter of costs.

Signed at Ottawa, Canada, this 24th day of September 2019.

« Gaston Jorré »

Jorré D.J.

Citation: 2019 TCC 199
Date: 20190924
Docket: 2012-1806(IT)G

BETWEEN:

ALLAN WARDLAW,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

AMENDED REASONS FOR JUDGMENT

[These amended reasons are issued in substitution
for the reasons for judgment signed on 24 September 2019.
They correct a slip in paragraph 13; the word "not" has been removed.]

Jorré D.J.

[1] One feature of the appeal is that it illustrates that there are circumstances where a penalty that appears to be a 50 % penalty can in fact be significantly higher, in this case around 70 %.

[2] When the Appellant filed his 2009 taxation return he claimed a nonexistent business loss of over $357,000. He also requested that the portion of the loss in excess of what he could use in 2009 be carried back over the prior three taxation years.

[3] This loss, had it been accepted by the Minister of National Revenue (the "Minister"), would have resulted in expected refunds of almost $104,000 in tax withheld for 2009 and in tax paid for the prior three years; he would have paid no federal or provincial income tax in 2009 and, while the evidence with respect to the three prior years does not allow me to make an exact determination, it looks like he would not have paid any federal or provincial income tax in the prior three years.

[4] As it turned out, the Appellant never saw any refunds because the Minister did a substantive examination of the claimed loss prior to doing an initial assessment. The Minister denied the loss.

[5] The Minister also applied what is often referred to as the gross negligence penalty. This penalty is set out in subsection 163(2) of the *Income Tax Act* (the "*Act*").

[6] The Appellant no longer claims the loss but is appealing against the gross negligence penalty.[1]

[7] The key portions of subsection 163(2) read as follows at the relevant times:

> (2) Every person who, knowingly, or under circumstances amounting to gross negligence, has made or has participated in, assented to or acquiesced in the making of, a false statement or omission in a return, form, certificate, statement or answer (in this section referred to as a "return") filed or made in respect of a taxation year for the purposes of this Act, is liable to a penalty of the greater of $100 and 50% of the total of
>
> …

[8] The provision becomes even clearer if one focuses on the key words:

> (2) Every person who, knowingly, or under circumstances amounting to gross negligence, has made…a false statement…in a return, form, … filed… in respect of a taxation year…, is liable to a penalty of the greater of $100 and 50% of the total of
>
> …

[9] There are two key elements required for the penalty: first, the making of a false statement and, second, that it is made either knowingly or in circumstances amounting to gross negligence. There can be no doubt that a false statement was made, the claim of a nonexistent loss. The key question here is whether that statement was made knowingly or in circumstances amounting to gross negligence.

[10] No issue was raised with respect to the quantum of the penalty. The calculation of the penalty is set out in subsection 2 and later in the section.

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[1] The original notice of appeal filed 4 May 2012 asked that the court…"restore the assessment to reflect the return as originally file, with prejudice…" In his amended Notice of Appeal filed on 12 August 2012 the Appellant limited his appeal to the penalties.

[11] Broadly, the penalty is 50% of the difference between the amount of tax that should be paid under the provisions of the Act given the actual facts and the amount of tax that would have been paid if the false statement had been accepted.

[12] However, there is a particularity in the mode of computation where the false statement, if accepted, would result in a loss carry back. As a result of this peculiarity the penalty is in fact higher than 50%. As was pointed out by Justice Woods, as she then was: "Under the formula, which is based on the tax that is sought to be avoided, the tax is computed at a relatively high tax rate which does not take into account that the actual tax savings would be spread over four taxation years and computed at lower tax rates (s.s. 163(2.1))."[2]

[13] In this particular case the federal and provincial penalties levied are of slightly less than $74,000. This appears to be a harsh result given that it produces a penalty of around 70% of the amount that would have been paid if the loss claimed had been unchallenged.

[14] This penalty appears particularly high when one considers that the claim on the Statement of Business or Professional Activities (Form T 2125) appears to be nonsensical on its face and that no refund was made on initial assessment.

[15] The Appellant completed grade 12 and has further training as a licensed mechanic. He obtained the designation of red seal automotive service technician he also has a certificate in adult education obtained from St. Francis Xavier University.

[16] The Appellant was referred to the Mortgage Centre in Harriston, Ontario, by someone he knew who said to him that the people at the Centre were great and that they had prepared her taxes and she was going to get a large refund.

[17] In early 2009 he went to the Mortgage Centre to inquire about a mortgage. It was the Centre that approached him about the possibility of doing his taxes. They said they were specialists in doing taxes and introduced him to Fiscal Arbitrators.

[18] To persuade him they showed him tax returns of other persons that they had prepared where the other persons' name was whited out. They did not do a very good job of whiting out the names and he recognized one of the names and saw that this individual was getting a large tax return.

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[2] *McLeod v. R* 2013 TCC 228, para.30.

[19] He spoke with his girlfriend at the time about this and she had heard that the individual he recognized had gotten a large tax refund.

[20] The person he dealt with at the Mortgage Centre was Kim Herd. His understanding was that the Mortgage Centre would work with Fiscal Arbitrators to prepare his return.

[21] The Mortgage Centre suggested to him that he could use his refund as a down payment on a house. He was excited at the prospect of being able to do this because he did not have at that time the funds necessary for a down payment. His financial situation was difficult because of a divorce in 2006.

[22] The Appellant had no business in 2009 and not surprisingly he did not provide Kim or Fiscal Arbitrators with any receipts for business expenses or any information about the business.

[23] He asked Kim if this tax arrangement was legal as well as what would happen if the claim was disallowed. Kim told him that it was all aboveboard and legal; that the CRA would not disallow his claim but, if they did, they would just disallow it.

[24] With one exception, the Appellant did not make inquiries about this tax arrangement with anyone else. For example, he did not ask a company called Craig Financial what they thought or what is ex-wife thought of this; in one past year he had had his return prepared by Craig Financial, where his ex-wife had worked part-time. He did discuss the matter with his current girlfriend at that time, who he is now married to.

[25] In terms of paying for the preparation of the tax return, the arrangement was as follows. First, the Appellant was to pay a flat amount of $500. This he did by writing a check for $500 made out to Lawrence Watts dated 12 March 2010.[3] Secondly, once he received the refund he was supposed to pay immediately a 20% fee of $20,769.[4]

[26] The return signed by the Appellant[5] shows a net business loss of $357,873.54 at line 135. When one turns to the Statement of Business or

[3] See Tab 19 at Exhibit R-1.
[4] See the second page of Tab 20 of Exhibit R-1.
[5] See Tab 1 of Exhibit R-1.

Professional Activities[6] on form T 2125 E in the return one sees the following: the main product or service is described as "AGENT". At line 8230 gross income of $130,800.29 is shown and is described as "RECEIPTS AS AGENT". At line 9270 on the second page, a line for other expenses, expenses of some $488,673.83 are shown and are described as "AMT TO PRINCIPLE FR AGENT". At the bottom of the page the expenses are deducted from the gross receipts and show a net loss of $357,873.54.

[27] Before signing the return the Appellant did wonder where the $357,000 loss came from and he circled the number on the return. He asked Kim about it and does not really remember what she answered other than it had something to do with definitions in the Act and the difference between a person and a business.

[28] Later in the return there is a request for loss carry back form, T1A E[7]. On this form the Appellant asks that all of the loss that has not been applied to 2009 be carried back and applied against his income in 2008, 2007 and 2006. This form is dated 7 April 2010 and "per:" has been written by hand immediately prior to the Appellant's signature.

[29] On the last page of the return, just below the statement "I certify that the information given on this return and in any documents attached is correct, complete and fully discloses all my income" there is, immediately prior to the Appellant's signature, the word "per" written by hand.

[30] He wrote the word "per" because Kim told him to. He did not know what it meant and did not ask anyone else about what it meant.

[31] There is a great deal of case law about the penalty under subsection 163(2) and about what constitutes making a false statement "knowingly" or "under circumstances amounting to gross negligence".

[32] In the case of *Peck v. The Queen*[8] Justice Owen provides the following summary of the law:

> B. The "Knowingly" and "Under Circumstances Amounting to Gross Negligence" Standards

[6] See pages 13 and 14 of the T1 Return.
[7] See pages 15 and 16 of the T1 Return.
[8] 2018 TCC 52. See also paragraphs 4 to 45 of the decision of Justice D'Auray in *Bradshaw v. Queen*, 2019 TCC 1.

[43] In *Wynter v. The Queen*, 2017 FCA 1985 (CanLII) the Federal Court of Appeal stated the following about the two standards in subsection 163(2):

> [11] When Parliament uses alternative terms, it is assumed that it intended them to have different meanings. Put otherwise, Parliament does not repeat itself: see Ruth Sullivan, Statutory Interpretation, 3rd ed. (Toronto: Irwin Law Inc., 2016) at 43. Section 163 allows the imposition of penalties **where the taxpayer has knowledge or in circumstances amounting to gross negligence**. The section is not conjunctive, and presumptively, these two terms differ in their meaning and content.
>
> [12] The distinction between gross negligence — determined by an objective assessment of the comportment of the taxpayer — and wilful blindness — determined by reference to the taxpayer's subjective state of mind — has a long history. Admittedly, it is, on occasion, a fine distinction and one that is not always clearly drawn. Nonetheless, Parliament is taken to have been cognizant of the distinction.

[44] As suggested in *Wynter*, the word "knowingly" requires a determination of whether the Appellant had subjective knowledge that he was making a false statement in the Return or the Request when he signed those documents. The burden is on the Respondent to present evidence that establishes on a balance of probabilities that the Appellant knew he was making a false statement when he signed the Return and the Request.

[45] As also suggested in *Wynter*, the subjective knowledge of the Appellant may be proven by evidence establishing on a balance of probabilities that the Appellant was wilfully blind as to whether the statements in the Return and the Request were false. This is a helpful clarification of the point that wilful blindness is used to attribute subjective knowledge to the Appellant and that wilful blindness and gross negligence are different legal concepts.

[46] To establish wilful blindness, the evidence must prove on a balance of probabilities that the Appellant subjectively knew that the false statements in the Return and the Request were probably false but deliberately chose not to make further inquiries because he subjectively knew or strongly suspected that the inquiries would provide him with the knowledge that the statements were indeed false (see *Sansregret v. The Queen*, 1985 CanLII 79 (SCC), [1985] 1 S.C.R. 570 at 584, *R. v. Jorgensen*, 1995 CanLII 85 (SCC), [1995] 4 S.C.R. 55 at paragraphs 102 and 103 and *Briscoe v. The Queen*, 2010 SCC 13 (CanLII), [2010] 1 S.C.R. 411 at paragraphs 21 to 23). The wilful blindness test is summarized in *Wynter* as follows:

> [13] A taxpayer is wilfully blind in circumstances where the taxpayer becomes aware of the need for inquiry but declines to make the inquiry because the taxpayer does not want to know, or studiously avoids, the truth. The concept is one of deliberate ignorance: *R. v. Briscoe*, 2010 SCC 13 (CanLII) at paras. 23-24, [2010] 1 S.C.R. 411 (*Briscoe*); *Sansregret* at para. 24. In these circumstances, the doctrine of wilful blindness imputes knowledge to a taxpayer: *Briscoe* at para. 21. . . .

[47] The subjective knowledge required for a finding of actual knowledge or wilful blindness refers to the actual or subjective knowledge of the person committing the prohibited act and not the objective or constructive knowledge of a reasonable person in the same circumstances (see, generally, *Shand v. The Queen*, 2011 ONCA 5 (CanLII) at paragraph 188 and *Roks v. The Queen*, 2011 ONCA 526 (CanLII) at paragraph 132).

[48] Actual subjective knowledge and wilful blindness may be proven by direct evidence, by circumstantial evidence or by a combination of the two. The determination of whether there is actual subjective knowledge or wilful blindness must be made in light of all the circumstances.

[49] The subjective nature of the wilful blindness standard versus the objective nature of the gross negligence standard means that conduct that contributes to a finding of wilful blindness may support a finding of gross negligence, but the converse is not necessarily true. For example, the fact that a reasonable person in the same circumstances would have made inquiries does not support a finding of wilful blindness but can support a finding of gross negligence. In *Briscoe*, the Supreme Court of Canada explains this distinction as follows:

> [24] Professor Don Stuart makes the useful observation that the expression "deliberate ignorance" seems more descriptive than "wilful blindness", as it connotes "an actual process of suppressing a suspicion". Properly understood in this way, "the concept of wilful blindness is of narrow scope and involves no departure from the subjective focus on the workings of the accused's mind" (*Canadian Criminal Law: A Treatise* (5th ed. 2007), at p. 241). While a failure to inquire may be evidence of recklessness or criminal negligence, as for example, where a failure to inquire is a marked departure from the conduct expected of a reasonable person, wilful blindness is not simply a failure to inquire but, to repeat Professor Stuart's words, "deliberate ignorance".

[50] The subjective nature of the wilful blindness standard also means that the personal attributes of the individual may be considered in determining whether the individual is wilfully blind.

[51] In contrast, the objective nature of the gross negligence standard means that the personal attributes of the individual are not relevant unless the individual establishes that he or she is incapable of understanding the risk the individual has failed to avoid (see *R. v. Beatty*, 2008 SCC 5 (CanLII), [2008] 1 S.C.R. 49 at paragraph 40). In *R. v. Roy*, 2012 SCC 26 (CanLII), [2012] 2 S.C.R. 60 at paragraph 38 the Court refers to this as the modified objective standard:

> . . . The modified objective standard means that, while the reasonable person is placed in the accused's circumstances, evidence of the accused's personal attributes (such as age, experience and education) is irrelevant unless it goes to the accused's incapacity to appreciate or to avoid the risk . . . .

[52] Although *Roy* addresses the criminal law standard of negligence, I see no reason to approach "gross negligence" under subsection 163(2) differently since the test under any negligence standard is whether the conduct in question departs from the objective standard of the reasonable person. *Roy* simply emphasizes that the relevant objective standard is that of the reasonable person in the same circumstances as the person whose conduct is in issue.

[53] The risk that the Appellant must be capable of understanding in order for gross negligence to be established is the risk of failing to meet the obligation imposed on all taxpayers under Canada's self-assessment system to prepare their income tax returns with honesty and integrity; in short, the risk of failing to meet the obligation not to commit a prohibited act. In *R. v. Jarvis*, 2002 SCC 73 (CanLII), [2002] 3 S.C. R. 757 the Supreme Court of Canada stated at paragraph 49:

> Every person resident in Canada during a given taxation year is obligated to pay tax on his or her taxable income, as computed under rules prescribed by the Act . . . . The process of tax collection relies primarily upon taxpayer self-assessment and self-reporting: taxpayers are obliged to estimate their annual income tax payable . . . and to disclose this estimate to the CCRA in the income return that they are required to file . . . .

[See also: *(Canada) National Revenue v. Thompson*, 2016 SCC 21 (CanLII) at paragraph 31, [2016] 1 S.C.R. 381]

[54] Accordingly, short of evidence establishing that the Appellant could not understand the obligation placed on him by Canada's self-assessment income tax system not to commit a prohibited act, the words "under circumstances amounting to gross negligence" require a determination of whether the conduct of the Appellant represented a marked and substantial departure from the expected conduct of a reasonable person in the same circumstances as the Appellant. For

there to be a finding of gross negligence, the conduct of the Appellant must reflect a high degree of negligence (*Venne v. The Queen*, 84 DTC 6247).

[55] Importantly, the objective standard against which the conduct of the Appellant is measured does not vary according to the personal attributes of the Appellant or the actual knowledge of the Appellant. In all cases, the standard is the expected conduct of a reasonable person in the same circumstances as the Appellant. The question that must be addressed is this: To what degree, if any, has the conduct of the Appellant deviated from that objective standard?

[56] A helpful albeit brief summary of the necessary departure from the objective standard of the reasonable person required for a finding of gross negligence is found in the recent judgment of the Supreme Court of Canada in *Guindon v. Canada*, 2015 SCC 41 (CanLII), [2015] 3 S.C.R. 3 where, at paragraph 60, the Court, in discussing the gross negligence standard described in *Venne*, adopts the following statement of the Tax Court of Canada from paragraph 23 of *Sidhu v. The Queen*, 2004 TCC 174 (CanLII):

> The burden here is not to prove, beyond a reasonable doubt, *mens rea* to evade taxes. The burden is to prove on a balance of probability such an indifference to appropriate and reasonable diligence in a self-assessing system as belies or offends common sense

[33] There is no fixed set of criteria for determining whether or not there is wilful blindness or gross negligence. Any relevant factor may be considered and there is a fair amount of overlap in what is relevant to either standard.

[34] Justice Miller of this Court enumerated a useful list of matters to be considered in determining whether there is wilful blindness or not in the case of *Torres v. The Queen*[9].

…

c) In determining wilful blindness, consideration must be given to the education and experience of the taxpayer.
d) To find wilful blindness there must be a need or a suspicion for an inquiry.
e) Circumstances that would indicate a need for an inquiry prior to filing, or flashing red lights as I called it in the *Bhatti* decision, include the following:
   i) the magnitude of the advantage or omission;
   ii) the blatantness of the false statement and how readily detectable it is;

[9] 2013 TCC 380 at paragraph 65; the decision was confirmed by the Federal Court of Appeal in *Strachan v The Queen*, 2015 FCA 60.

iii) the lack of acknowledgment by the tax preparer who prepared the return in the return itself;
iv) unusual requests made by the tax preparer;
v) the tax preparer being previously unknown to the taxpayer;
vi) incomprehensible explanations by the tax preparer;
vii) whether others engaged the tax preparer or warned against doing so, or the taxpayer himself or herself expresses concern about telling others.

f) The final requirement for wilful blindness is that the taxpayer makes no inquiry of the tax preparer to understand the return, nor makes any inquiry of a third party, nor the CRA itself.

[35] In this case there are all kinds of factors calling for the appellant to be very suspicious and make inquiries, for example:

i) Showing very substantial gross business income of some $130,000 and expenses of some $480,000 when the appellant does not engage in any kind of business or activity and when he had no revenues or expenses of any kind.

ii) While living in a society with significant levels of taxation and government services, paying no income tax for the 2009 year and claiming large refunds for prior years based on a very large business loss when there was nothing happening to the Appellant that would suggest a financial disaster of the magnitude of a loss of some $350,000.

iii) The nonsensical annotation “AMT TO PRINCIPAL FR AGENT” as well as being asked to write “per” before his signature and the fact that he was receiving explanations that he did not understand.

iv) The fact that, in addition to the $500 upfront payment the Appellant made for the preparation of the return, he was also supposed to also pay 20% of the expected refund, an amount of over $20,000.

[36] There is nothing in the Appellant’s evidence that would suggest that he was unable to recognise these very visible flashing red lights.

[37] Although the circumstances called for great caution, the only inquiries the Appellant made were of Kim Herd, who was promoting this arrangement, and a discussion with his girlfriend at the time. He did not seek out anyone who was independent of the scheme and who would be knowledgeable.

[38] In the circumstances I am unable to see how there could not be wilful blindness with the consequence that the second requirement is met[10]. As a result, there is no reason to vary the assessment.

[39] I previously mentioned the quantum of the penalty seemed very high to me in the circumstances. Given that Parliament has set a fixed formula in the *Income Tax Act*, I have no power to alter the penalty.

[40] However, perhaps Parliament, the Department of Finance and The Minister of National Revenue may wish to consider whether the legislation ought to be adjusted. Not only does the penalty seem high in the circumstances but, in addition, it does seem odd that what is apparently meant to be a 50% penalty can, where a loss carry back is involved, become a significantly higher percentage.

[41] The Appellant may wish to consider making an application for a reduction of the penalty and interest under the taxpayer relief provisions contained in subsection 220(3.1) of the *Income Tax Act*. This Court has no role to play in relation to those provisions[11].

[42] In conclusion, the appeal is dismissed.

[43] Costs are generally awarded to the successful party and, accordingly, unless there is some special factor I am not aware of, the result in this case would normally be for me to award costs in accordance with the tariff to the Respondent. However, just in case there are special factors I should be aware of, the parties are directed to attempt to agree on costs and, if they are unable to agree within 60 days of this judgement, they may make submissions in writing to the Court on the matter of costs.

Signed at Ottawa, Canada, this 26th day of September 2019.

« Gaston Jorré »

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[10] Given this finding I do not need to consider whether the circumstances here amount to gross negligence.

[11] The Appellant may wish to obtain from the Canada Revenue Agency publication IC07-1R1 entitled *Taxpayer Relief Provisions*. The publication discusses the CRA's policy with respect to such applications and when it may consider granting relief. The appellant may also wish to obtain form RC 4228, *Request for Taxpayer Relief*.

CITATION:	2019 TCC 199
COURT FILE NO.:	2012-1806(IT)G
STYLE OF CAUSE:	ALLAN WARDLAW AND HER MAJESTY THE QUEEN
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DATE OF AMENDED REASONS FOR JUDGMENT:	September 26, 2019

APPEARANCES:

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