Challenging and Defending Assessments Before the Tax Court of Canada and Appellate Courts: A Postscript to the Continental Bank Case

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PRÉCIS

L'affaire de la *Banque Continentale* fait suite à une controverse, à savoir si une société en nom collectif existe ou non à l'égard de l'impôt sur le revenu et, dans l'affirmative, si le gain matérialisé à la disposition d'une participation dans une société en nom collectif constitue un gain en capital ou un revenu. En répondant par la négative à la première question, la Cour suprême du Canada a soulevé des doutes quant à la seconde question et à un argument subsidiaire concernant le droit de la Couronne de contester une cotisation, en vertu d'un nouveau fondement, après l'expiration du délai prévu pour la nouvelle cotisation. La Cour a néanmoins maintenu que la Couronne ne pouvait avancer un nouveau fondement pour justifier une nouvelle cotisation après l'expiration du délai prévu à cette fin. Selon l'auteur, l'incidence de cette décision comporte deux aspects. D'abord, elle a modifié ce qui était considéré auparavant comme un terrain d'entente entre les contribuables et la Couronne en ce qui concerne la définition de cotisation et le lien qui existe avec tout litige qui s'ensuit. En second lieu, cette décision implique que les contentieux fiscaux feraient l'objet de règles différentes de celles qui régissent habituellement les contentieux des affaires civiles. L'auteur soutient qu'il ne devrait y avoir aucune différence entre ces règles et que la Cour suprême du Canada a commis une erreur en énonçant effectivement les mêmes préoccupations en matière de politique pour une instance judiciaire en vertu de l'article 169 de la *Loi de l'impôt sur le revenu* que pour une cotisation. À ce sujet, il évoque le fait que la nature et l'objectif des cotisations et des instances judiciaires, de même que les préoccupations en matière de politique qui les sous-tendent, sont différents et que le fait de les

* Counsel, Department of Justice (Canada). I am grateful to my colleagues for their comments and suggestions. However, all views expressed in this article are my own and do not necessarily represent the position of the Department of Justice. As well, responsibility for any errors or omissions is mine alone.

traiter autrement nuit au procès. Par conséquent, l'auteur conclut que le Parlement a eu raison de réagir en ayant recours à une législation infirmant la décision de la Cour suprême.

ABSTRACT

The *Continental Bank* case arose out of a dispute concerning whether or not a partnership exists for income tax purposes and, if so, whether or not the gain realized from the disposition of a partnership interest is on capital or income account. By answering the former question in the negative, the Supreme Court of Canada rendered moot the latter issue, as well as a subsidiary question regarding the Crown's entitlement to defend an assessment on an alternative basis following the expiry of the reassessment period. The court nonetheless held that, after the reassessment period, the Crown could not raise alternative bases in support of its assessment. According to the author, the effect of this decision was twofold. First, it changed what previously was regarded as common ground between taxpayers and the Crown about what an assessment is and its relationship to any ensuing litigation. Second, it meant that tax litigation would be subject to different rules from those that govern civil litigation generally. The author argues that there should be no difference in the rules and that the Supreme Court of Canada erred by effectively positing the same policy concerns for a legal proceeding under section 169 of the Income Tax Act as for an assessment. In that regard, he suggests that the nature and objective of assessments and legal proceedings, as well as the policy concerns that underlie each, are different and that to treat them otherwise undermines the litigation process. As a result, he concludes that Parliament was right to respond with legislation reversing the Supreme Court's decision.

INTRODUCTION

As Bauer noted in his case comment on *Continental Bank Leasing Corporation v. The Queen et al.*,[1] the decision of the Supreme Court of Canada dealt with important questions regarding the existence of a partnership for income tax purposes, whether or not the substance-over-form debate encompasses an economic substance test, and the role of the judiciary in reviewing perceived tax-avoidance schemes.[2] *The Queen v. Continental Bank of Canada*[3] arose out of the

1 98 DTC 6505 (SCC).

2 Thomas A. Bauer, "Partnerships: A Matter of Substance," Current Cases feature (1998), vol. 46, no. 5 *Canadian Tax Journal* 1067-75, at 1073-74.

3 98 DTC 6501 (SCC).

foregoing case and dealt with whether or not the gain realized from the disposition of the partnership interest, if such existed, was on income or capital account. The Supreme Court of Canada also considered the Crown's entitlement to defend an assessment on an alternative basis after the limitation period for reassessing has expired and decided the Crown could not do so.[4] While Bauer described the court's decision on the latter issue as a sidelight,[5] it nonetheless reverberated within the tax bar, particularly among Crown counsel, because it apparently changed what were thought to be fundamental principles regarding the conduct of tax litigation. Parliament responded by amending the Income Tax Act[6] to include subsection 152(9), which permits the Crown to amend its pleadings in defined circumstances.[7] The purpose of this article is to examine the change wrought by the *Continental Bank* case and the reasons for it, and to consider whether or not Parliament's decision to overrule the Supreme Court of Canada was warranted by legal and policy considerations.

QUESTIONS RAISED BY THE CONTINENTAL BANK CASE

Facts

In 1986, Continental Bank ("Bank") was in the process of winding up and disposing of its property, which included selling either the shares or assets of a wholly owned subsidiary, Continental Bank Leasing Corporation ("Leasing") to Central Leasing Corporation ("Central"). Because Central was concerned about the creditworthiness of several of Leasing's leases, it did not purchase its shares and instead purchased selected leases through a series of transactions. Leasing formed a partnership with certain subsidiaries of Central to carry on a leasing business, transferred the desired leases to the partnership pursuant to an election under subsection 97(2) of the Act, and distributed its partnership interest to Bank at its cost base as part of its winding up. Bank then sold this interest to Central. The minister of national revenue ("the minister") assessed Leasing on the basis that these transactions did not give rise to a partnership, rendering the election under subsection 97(2) invalid, and that the true nature of the transactions was a disposition by Leasing of its leases, giving rise to recaptured capital cost allowance. As an alternative to reassessing Leasing, and to protect his position, the minister also reassessed Bank on the basis that it had realized an income gain as opposed to a capital gain from the disposition of the alleged partnership interest that it had acquired from Leasing.

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4 Ibid., at 6504-5.

5 Supra footnote 2, at 1075.

6 RSC 1985, c. 1 (5th Supp.), as amended (herein referred to as "the Act"). Unless otherwise stated, statutory references in this article are to the Act.

7 Infra footnote 74.

On appeal to the Tax Court of Canada, Bowman TCJ upheld the validity of the partnership entered into by Leasing and rejected the Crown's argument that Bank's gain on the sale of its interest in the partnership was reportable on income account.[8] The Federal Court of Appeal restored the minister's assessment in respect of Leasing, holding that Leasing had not entered into a partnership with Central since they did not have an intention to carry on business in common with a view to a profit.[9] As a result, the court dismissed the Crown's appeal in respect of Bank, although it agreed with Bowman TCJ that, if Leasing had become a member of the partnership, the resulting gain realized by it on the sale of its partnership interest to Bank would have been on capital account.[10] The Supreme Court of Canada vacated the assessment against Leasing and dismissed the Crown's appeal in respect of Bank.[11]

In anticipation of Leasing's arguing that the actual vendor of the leases was Bank, and that it was therefore not required to include in its income recaptured capital cost allowance arising from the disposition of the leases, the Crown advanced an alternative argument before the Supreme Court of Canada. Counsel argued that, in view of paragraph 88(1)(f), the minister's assessment of Bank was supportable on the basis that this amount was includible in its income pursuant to section 9 and subsection 13(1).[12] Although the court no longer needed to consider this alternative argument, it nonetheless addressed the issue of the Crown's entitlement to raise it. The court held that "even if it was found that Bank was the vendor of those assets and liable for recapture, the appellant could not succeed in upholding its reassessment [of Bank] in this appeal."[13] The reason it gave was that the applicable limitation period for reassessing Bank had expired and that the Crown is not permitted thereafter to advance a new basis for reassessment.[14] According to the court, to decide otherwise "would, in effect, create a situation where the Crown is permitted to raise new arguments simply because other arguments failed in the courts below."[15] Moreover, in the court's view, what the minister was seeking to do was substitute an assessment of Leasing for an assessment of Bank because the first assessment did not succeed.[16] The court concluded by stating that, in any event, it did not have before it

8 *Continental Bank of Canada et al. v. The Queen*, 94 DTC 1858 (TCC).

9 *The Queen v. Continental Bank Leasing Corporation et al.*, 96 DTC 6355 (FCA).

10 Ibid., at 6369.

11 Supra footnotes 1 and 3.

12 Supra footnote 3, at 6504.

13 Ibid.

14 Ibid.

15 Ibid., at 6505.

16 Ibid.

all the facts necessary to consider this argument.[17] In deciding the Crown's entitlement to defend its original assessment of Bank on a different basis, the court relied on the reasoning of the Federal Court—Trial Division in *The Queen v. McLeod*[18] as well as that of the Federal Court of Appeal in *British Columbia Telephone Co. v. Minister of National Revenue*.[19]

The Queen v. McLeod

In the *McLeod* case, the minister had disallowed the deduction of losses incurred by the taxpayer from his farming operation on the grounds that he was not engaged in a business. The taxpayer appealed to the Tax Court of Canada, which held that the farming operation had a reasonable expectation of profit and therefore constituted a business.[20] It also held that the taxpayer was entitled to deduct his full farming losses since "farming may reasonably be expected to provide the bulk of income or the centre of work routine."[21] The Crown appealed the decision by way of trial de novo to the Federal Court—Trial Division.

The Crown alleged in its statement of claim that the minister had assumed that the taxpayer was not engaged in a farming business and in the alternative alleged that, if the farming operation had a reasonable expectation of profit, the taxpayer's chief or combined source of income was not farming. The Crown subsequently sought to amend the statement of claim by replacing the foregoing

17 Ibid. Bastarache J gave the following example of the kind of further evidence that might be needed: "[T]he value of the goodwill associated with the Bank's leasing business, which was transferred to Central in December 1986, could bear on the appellant's new claim for recapture by the Bank. It is not possible to measure the extent to which the Bank might otherwise be liable for recapture, on the Bank's income for tax purposes, without being able to properly allocate the purchase price paid by Central between goodwill and leasing assets. Because the Bank was not assessed on the recapture, the evidence relating to the allocation of the purchase price was not adduced at trial. To allow the appellant to proceed with its new assessment without the benefit of findings made at trial would require this Court to become a court of first instance with regard to the new claim."

18 90 DTC 6281 (FCTD).

19 (1994), 167 NR 112 (FCA). As Bastarache J explained in the *Continental Bank* case, supra footnote 3, at 6504-5, "The proper approach was expressed in *The Queen v. McLeod*, 90 DTC 6281 (F.C.T.D.), at p. 6286. In that case, the court rejected the Crown's motion for leave to amend its pleadings to include a new statutory basis for Revenue Canada's assessment. The court refused leave on the basis that the Crown's attempt to plead a new section of the Act was, in effect, an attempt to change the basis of the assessment appealed from, and 'tantamount to allowing the Minister to appeal his own assessment, a motion that has been specifically rejected by the courts.' Similarly, the Federal Court of Appeal has described such attempts by the Crown as a 'belated attempt to put the appellant's case on a new footing' (*British Columbia Telephone Co. v. Minister of National Revenue* (1994) 167 N.R. 112, at p. 116)."

20 84 DTC 1297 (TCC).

21 Ibid., at 1299; quoting from *Moldowan v. The Queen*, 77 DTC 5213, at 5216 (SCC).

assumption with a new one based on the alternative allegation. When the taxpayer refused to consent to this change, the Crown brought a motion for leave to amend its pleadings. The presiding motions judge, Collier J, disallowed the application on the ground that the proposed amendment would cause an injustice to the taxpayer, since it would be tantamount to allowing the minister to appeal his own assessment.[22] His refusal to permit an amendment to pleadings that involve altering the minister's assumptions was consonant with the view that assumptions should not be pleaded in the alternative.[23] However, the reasons he gave for his decision effectively challenged what until then was common ground for the taxpayer and the Crown about what an assessment is and its relationship to any ensuing litigation.

While the courts have prohibited the minister from appealing his own assessments, that was not what he was seeking to do in the *McLeod* case. Upholding the validity of an assessment on a basis different from that which the minister relied on in making it constitutes an appeal by the minister if the result would be a tax liability greater than the amount originally assessed. As Cattanach J explained in *Vineland Quarries and Crushed Stone Ltd. v. MNR*,

> [a]s I understand the basis of an appeal from an assessment by the Minister, it is an appeal against the amount of the assessment.
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> In *Harris v. M.N.R.*, (1965) 2 Ex. C.R. 653 [64 DTC 5332], my brother Thurlow said at page 662:
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> > . . . On a taxpayer's appeal to the Court the matter for determination is basically whether the assessment is too high. This may depend on what deductions are allowable in computing income and what are not but as I see it the determination of these questions is involved only for the purpose of reaching a conclusion on the basic question. . . .
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> Here the Minister does not seek to increase the amount of the assessment. He seeks to maintain the assessment at the amount he assessed. However by his amendment to his Reply he seeks to ensure that, if the Court should find that the basis of his assessment was wrong, he might then, pursuant to reference back, assess a considerably lesser amount on what he foresees the Court might say is the correct basis of assessment.
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> In *M.N.R. v. Beatrice Minden*, 62 DTC 1044, Thorson P., the former President of this Court, said at page 1050:

22 *The Queen v. McLeod*, 90 DTC 6281, at 6286 (FCTD).

23 *Brewster v. The Queen*, 76 DTC 6046, at 6049 (FCTD). However, as has been pointed out by Innes and Moorthy, infra footnote 50, at 1202, "[i]n subsequent decisions . . . the courts have adopted a less stringent view of pleading in the alternative." In that regard, see *Hillsdale Shopping Centre Ltd. v. MNR*, 81 DTC 5261, at 5266 (FCA); and *Schultz v. The Queen*, [1996] 2 CTC 127, at 136 (FCA).

> . . . In considering an appeal from an income tax assessment the Court is concerned with the validity of the assessment, not the correctness of the reasons assigned by the Minister for making it. An assessment may be valid although the reason assigned by the Minister for making it may be erroneous. This has been abundantly established.
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> In effect the Minister says that for a reason he thinks to be correct he assessed the appellant to income tax at "X" dollars. The appellant says that the reason assigned by the Minister was incorrect. The Minister then says if the Court should hold the basis for his assessment of "X" dollars is erroneous, then for what the Court might find to be correct reasons, he would assess the appellant at "X" minus "Y" dollars.
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> This I think the Minister is entitled to do and accordingly I would allow the motion and permit the Minister to amend his Reply to the Notice of Appeal as requested.[24]

If the minister, for whatever reason, wishes to claim more tax than originally assessed, he must issue a reassessment within the time limits prescribed in section 152.[25]

Collier J acknowledged in the *McLeod* case that the proposed amendment would have reduced the amount of taxes in issue:

> The position taken by the plaintiff in its original statement of claim disallowed the defendant from claiming the full extent of his farming losses. The position now taken by the plaintiff in its amended statement of claim . . . entitles the defendant to claim restricted losses under section 31.[26]
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> The question before me is whether the Minister should be allowed to claim *less* tax than is owing, but on a totally different basis.[27]

While Collier J was careful not to refer to the amendment proposed by the Crown as an appeal from the minister's assessment, that was his effective conclusion when he stated that it would be "tantamount to allowing the Minister to appeal his own assessment."[28] His conclusion is inconsistent with what previously was considered trite law.[29] It is also at odds with the goal of resolving disputes efficiently and expeditiously. As Crown counsel argued,

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24 70 DTC 6043, at 6045-46 (Ex. Ct.).

25 Infra footnote 39.

26 Supra footnote 18, at 6284.

27 Ibid., at 6286.

28 Ibid.

29 Supra footnote 24. See also, for example, *No. 526 v. MNR* (1958), 20 Tax ABC 114; *Shiewitz v. MNR*, 79 DTC 340, at 341 (TRB); *Boyko et al. v. MNR*, 84 DTC 1233, at 1237 (TCC); *Cooper v. MNR*, 87 DTC 194, at 205 (TCC); *Cohen v. MNR*, 88 DTC 1404 (TCC); and *Keys v. MNR*, 89 DTC 91 (TCC).

> [the proposed amendments] assist rather than prejudice the defendant with respect to examinations for discovery and preparation for trial in that they facilitate litigation on the real question in controversy and reduce the proof and argument required at trial.[30]

Collier J acknowledged the argument but did not address its merits.

British Telephone Co. Ltd. v. Minister of National Revenue

At issue in the *British Columbia Telephone Co.* case was the company's entitlement to a refund of taxes paid pursuant to the Excise Tax Act.[31] The minister had determined that the value of British Columbia Telephone Co.'s directories was subject to excise tax. The Federal Court—Trial Division[32] and the Federal Court of Appeal[33] both upheld the minister's determination, which was based on certain provisions of the Excise Tax Act. However, the minister made an alternative submission before the latter court based on different provisions. British Columbia Telephone Co. contended that the Federal Court of Appeal should not give effect to this submission because the point had not been taken at trial and was raised for the first time on appeal, to its prejudice.[34] The Federal Court of Appeal agreed:

> While it was touched upon by counsel for the appellant obliquely during argument in the court below and then dropped for tactical reasons when questioned about it by the trial judge, it was seriously raised for the first time toward the end of Mr. Millar's submissions before us. The argument has no support in the pleadings or in the evidence and appears to us to be a belated attempt to put the appellant's case on a new footing.[35]

The conclusion is grounded in the principles governing the circumstances in which a new issue may be raised before an appellate court.[36] The Federal Court of Appeal did not consider, and its decision therefore did not turn on, whether or

30 Supra footnote 18, at 6284.

31 RSC 1970, c. E–13, as amended.

32 (1992), 59 FTR 176 (FCTD).

33 Supra footnote 19.

34 Ibid., at 115.

35 Ibid., at 115-16.

36 As Lord Herschell stated in *The Owners of the Ship "Tasmania" and Owners of Freight v. Smith and Others, Owners of the Ship "City of Corinth"* (1890), 15 App. Cas. 223, at 225 (HL),

> [m]y Lords, I think that a point such as this, not taken at trial, and presented for the first time in the Court of Appeal, ought to be most jealously scrutinized. The conduct of a cause at the trial is governed by, and the questions asked of the witnesses are directed to, the points then suggested. And it is obvious that no care is exercised in the elucidation of facts not material to them.

not the limitation period for issuing an assessment under the Excise Tax Act had expired. The Supreme Court of Canada's reliance on the *British Columbia Telephone Co.* case therefore begs the question why the expiration of this period is relevant to judging the Crown's entitlement to raise new legal bases in support of an assessment during the course of tax litigation.[37]

QUESTIONS

It is submitted that, by relying on the *McLeod* case, without considering the jurisprudence ignored by Collier J, and by also relying on the *British Columbia Telephone Co.* case, without close examination of the Federal Court of Appeal's judgment, the Supreme Court of Canada left taxpayers and the Crown alike wondering about its motivation for effecting a significant change in the conduct of tax litigation. It raised, but then failed to answer, the fundamental question why tax litigation should be subject to different rules from those governing civil litigation generally. It is submitted that there should be no difference and that Parliament was correct to step in with remedial legislation.

DISTINGUISHING BETWEEN AN ASSESSMENT AND A LEGAL PROCEEDING

The alternative ground put forward by the Supreme Court of Canada for disallowing the amendment proposed by the Crown—namely, that it did not have before it all the facts necessary to consider the argument—raises the following question: if the matter could have been disposed of on this ground, why was it necessary to propound a further restriction for the purposes of tax litigation? One answer to this question is that proposed by Meghji and Grenon:

> As the courts that have prohibited the Attorney General from raising new grounds to defend assessments have recognized, there is a fundamental and critical principle involved, the goal of finality. Parliament has recognized the importance of this principle by restricting the time limit for reassessment in subsections 152(4) and (5) of the Income Tax Act. The same values embodied in the time limits in

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> It appears to me that under these circumstances a Court of Appeal ought only to decide in favour of an appellant on a ground there put for the first time, if it be satisfied beyond doubt, first, that it has before it all the facts bearing upon the new contention, as completely as would have been the case if the controversy had arisen at trial; and next, that no satisfactory explanation could have been offered by those whose conduct is impugned if an opportunity for explanation had been afforded them when in the witness box.

37 In *The Queen v. Hollinger Inc.*, 99 DTC 5500, the Federal Court of Appeal considered the scope of the *Continental Bank* case and concluded that, in order for the Crown to defend an assessment on an alternative basis before the expiry of the statutory period for issuing reassessments, the minister need not reassess the taxpayer.

> subsections 152(4) and (5) have inspired the courts to refuse to allow the Crown to circumvent the restrictions by issuing, not a formal reassessment, but instead an effective reassessment by pleading a new ground. The courts' concern with the circumvention of time limits is reflected in both *McLeod* and *Lutheran Life*, where subsections 152(4) and (5) are explicitly cited in refusing leave for the Minister to bring arguments other than those on which the assessment was based. This refusal on the part of the courts is, it is suggested, wholly appropriate. Where Parliament has intentionally limited the Minister of National Revenue's power to reassess, the Attorney General should not be allowed to use the courts to do an "end-run" around Parliament's will. In addition, there is a clear distinction between the powers of the Minister of National Revenue as found in the Income Tax Act and the powers of the Attorney General as found in the *Department of Justice Act*. The Minister is granted the powers to "assess" and "reassess." The Act requires him, however, to complete the assessing function within the statutory time limit. In the context of income tax litigation, the Attorney General is charged with the role of, *inter alia*, "regulation and conduct of . . . [the] . . . litigation." It is suggested that courts must distinguish between the assessing and litigation functions lest the Attorney General simply picks up where the Minister left off in the assessing exercise.[38]

It is submitted, however, that it is precisely because of the distinction between the minister and the attorney general that Meghji and Grenon suggest that the time limit prescribed in subsections 152(4) and (5) for issuing reassessments[39]

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38 Al Meghji and Gerald Grenon, "New Arguments in Support of an Assessment: More than an Issue of Onus" (1997), vol. 5, no. 4 *Tax Litigation* 344-47, at 345–46.

39 Under subsection 152(4), the Minister may make an original assessment, reassessment or additional assessment for taxes, interest or penalties at any time. However, the Minister may assess, reassess or make additional assessments, as a general rule, only within the "normal reassessment period" (defined in subsection 152(3.1)) for the taxpayer with respect to the year in question. For mutual fund trusts and corporations other than Canadian-controlled private corporations, this reassessment period is four years from the earlier of (i) the date of mailing of an original assessment, and (ii) the date of mailing of an original notification that no tax is payable for the taxation year. For all other taxpayers the normal reassessment period is three years from the earlier of the two above-stated dates. . . .

> In circumstances involving paragraph 152(4)(a), an assessment, reassessment or additional assessment of a taxpayer may be made after the taxpayer's normal reassessment period to the extent it can be reasonably regarded as relating to (i) misrepresentations attributable to neglect, carelessness or willful default; (ii) fraud committed in filing a return or supplying information under the Act; or (iii) a matter specified in a waiver filed with the Minister.
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> In situations where paragraph 152(4)(b) applies, an assessment, reassessment or additional assessment of a taxpayer may be made after the taxpayer's normal reassessment period to the extent they can be reasonably regarded as relating to a matter specified in any of subparagraphs 152(4)(b)(i) to (iv). These subparagraphs deal with reassessments resulting from (i) taxpayers wishing to carry back certain deductions as specified in subsection 152(6) to previous taxation years; (ii) transactions involving a

should not be imported into the litigation process. The suggestion that the attorney general is making an "end-run" around Parliament's will when he attempts to uphold the validity of an assessment on an alternative basis, after the expiry of the reassessment period, presumes that Parliament's intention vis-à-vis the assessment process and tax appeals is the same. It is submitted, however, that the nature and purpose of assessments and appeals are fundamentally different and therefore not governed by the same policy considerations.

An assessment is the product of an administrative process that fixes the amount of a taxpayer's liability.[40] Neither the reasons for it nor the materials on which it is based constitute part of an assessment. As Hugessen JA explained in *The Queen v. The Consumers' Gas Company Ltd.*,

> [w]hat is put in issue on appeal to the courts under the *Income Tax Act* is the Minister's assessment. While the word "assessment" can bear two constructions, as being either the process by which tax is assessed or the product of that assessment, it seems to me clear, from a reading of sections 152 to 177 of the *Income Tax Act*, that the word is there employed in the second sense only. This conclusion flows in particular from subsection 165(1) and from the well established principle that a taxpayer can neither object to nor appeal from a nil assessment.[41]

In conducting an assessment, the minister is accorded a wide latitude. As the Exchequer Court explained in *Provincial Paper, Ltd. v. MNR*,

> [t]here is no standard in the Act or elsewhere, either express or implied, fixing the essential requirements of an assessment. . . . [I]t is exclusively for [the minister] to decide how he should, in any given case, ascertain and fix the liability of the taxpayer.[42]

By enacting subsections 152(4) and (5), Parliament effectively decreed that, after a certain period, taxpayers should be relieved from the burden of having

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> non-arms length non-resident; (iii) a payment or reimbursement of an income or profits tax to or by a government other than the Canadian government; (iv) a reduction under subsection 66(12.73) of an amount purported to be renounced under section 66 in respect of a flow-through share; and (v) a gift to which subsections 118.1(15) or (16) applies. . . .
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> Subsection 152(5) provides that there may not be included in income any amount that was not included in computing the taxpayer's income for the purpose of assessment of tax made prior to the expiration of the taxpayer's normal reassessment period.

Canadian Tax Reporter, vol. 5 (North York, Ont.: CCH Canadian) (looseleaf), paragraphs 22,222b and 22,247. Subsection 152(4.01) limits the circumstances in which the minister can reassess under paragraph 152(4)(a) or (b) where the reassessment is made beyond the normal reassessment period. See also subsections 152(4.2), (4.3), and (6).

40 Supra footnote 24.

41 87 DTC 5008, at 5012 (FCA).

42 54 DTC 1199, at 1201 (Ex. Ct.).

to maintain personal and financial records, as well as from the worry of having to marshal evidence in response to a potential challenge to their self-assessment by the minister.[43] The subsections do not, however, relieve taxpayers from the legal and evidentiary burden associated with the decision to challenge an assessment. Once a taxpayer appeals to the Tax Court of Canada, the fairness concerns that underlie subsections 152(4) and (5) no longer apply,[44] and the ensuing dispute is instead governed by a framework that reflects the aims of litigation. In that regard, appeals to the Tax Court of Canada constitute legal proceedings authorized under the Act. They are governed by a specified procedure of civil litigation[45] whose purpose is the same as all litigation—namely, the identification and resolution of the real controversy between parties to a dispute.[46]

In the *McLeod* case, Collier J distinguished between an assessment, as that term is defined in the *Consumers Gas* case, and an appeal from an assessment, by considering how the basis of the former informs and affects proceedings in the latter. That is,

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43 Supra footnote 39.

44 Except, of course, the prohibition against the minister's appealing his own assessment.

45 The right to appeal from assessments of tax, interest, and penalties is set out in section 169 of the Act. The procedure governing such appeals was considered by the author in "The Requirement of Confidentiality Under the Income Tax Act and Its Effect on the Conduct of Appeals Before the Tax Court of Canada" (1996), vol. 44, no. 3 *Canadian Tax Journal* 680-722, at 682-83:

> While both the Federal Court—Trial Division and the Tax Court of Canada are empowered to hear tax appeals commenced before January 1, 1991, only the Tax Court of Canada has the jurisdiction to hear appeals filed on or after that date. Appeals to the Tax Court of Canada commenced after December 31, 1990 are dealt with pursuant to the informal or general procedures of the Tax Court of Canada Act. Section 18 of this Act authorizes an appeal under the informal procedure where
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> • federal income tax and penalties are $12,000.00 or less,
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> • the amount of the loss determined by subsection 152(1.1) of the Income Tax Act is $24,000.00 or less, or
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> • the only matter in issue is interest.
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> Section 17 of the Tax Court of Canada Act provides that the general procedure applies in all other cases. No special form of pleading is required to initiate appeals under the informal procedure. Appellants may appear personally or by agent, and at the hearing the court is not bound by any legal or technical rules of evidence. In contrast, appeals under the general procedure are commenced by an originating document of specified form and content. The proceedings are subject to the rules of evidence and the usual procedures of civil litigation governing actions before the Federal Court—Trial Division and provincial courts of superior jurisdiction.

46 *The Queen v. Canderel Limited*, 93 DTC 5357 (FCA); *Francoeur v. The Queen*, [1992] 2 FC 333 (FCA); *Gavin Enterprises Ltd. v. The Queen* (1992), 53 FTR 306 (FCTD); and *Sorbara v. MNR*, 63 DTC 1271 (Ex. Ct.).

> whereas an assessment constitutes the findings of an amount of tax payable, the appeal from that assessment arises out of one or more disputes between the taxpayer and the Minister of National Revenue as to the facts and law entering into the determination of that amount. It is for that reason the courts have held that the Minister must, as a general rule, set out the assumptions on which the assessment was based.[47]

The minister's assumptions, which are set out in his reply to notice of appeal, are lent evidentiary significance by the presumption of correctness. The rationale for this presumption was first spelled out by the Supreme Court of Canada in *Johnston v. Minister of National Revenue*.[48] Although the primary issue was one of statutory construction, Johnston had raised a secondary issue that turned on whether or not he supported his wife. Johnston had argued that he did not support his wife, a claim that, if true, may have put him in a lower tax bracket. In making the assessment, the minister had assumed the opposite. There was no evidence at trial on which the Exchequer Court could decide the matter, and thus the question became one of onus—that is, who must establish the positive or negative of this fact? Rand J, writing for the majority, held as follows:

> Notwithstanding that it is spoken of in section 63(2) as an action ready for trial or hearing, the proceeding is an appeal from the taxation; and since the taxation is on the basis of certain facts and certain provisions of law, either those facts or the application of the law is challenged. Every such fact found or assumed by the assessor or the Minister must then be accepted as it was dealt with by these persons unless questioned by the appellant. If the taxpayer here intended to contest the fact that he supported his wife within the meaning of the Rules mentioned he should have raised that issue.[49]

Another reason for putting the onus on taxpayers to challenge the validity of an assessment stems from the system of self-assessment on which the Canadian tax system is based and the resulting expectation that taxpayers are in the best position to put the true facts before the court.[50] One reflection of this is that the

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47 Supra footnote 18, at 6285.

48 (1948), 3 DTC 1182 (SCC).

49 Ibid., at 1183. Since the *Johnston* case, the rule regarding who, as between the Crown and taxpayers, bears the burden of proof has remained essentially unchanged. For example, in *Youngman v. The Queen*, 90 DTC 6322, at 6325 (FCA), Pratte JA stated, "I will deal first with the question of onus of proof. The rule is well known. When the Minister has, in his pleading, disclosed the assumptions of facts on which that assessment was made, and when, as is the case here, it is not contested that the assessment was in fact based on those assumptions, the taxpayer has the onus of disproving the Minister's assumptions."

50 "The most important distinguishing feature between a hearing under the Act and an ordinary civil trial is the nature of the onus that rests on the taxpayer. An income tax appeal is an 'appeal from taxation,' as distinct from a civil proceeding in which each party has independent knowledge of the facts underlying the dispute. In Canada's self-assessment system, where the

taxpayer's notice of appeal is drafted and filed before the Crown's reply, which contains the minister's assumptions.

Nothing in the relationship between assessments and appeals under the Act restricts either party as to the facts they can allege and seek to prove, or the legal submissions they can advance in support of their position. The onus that taxpayers bear in appeals to the Tax Court of Canada gives rise to three ways in which they can contest an assessment. They can

1) challenge the minister's allegations that he assumed the facts pleaded in the reply as assumptions;

2) assume the onus of showing that one or more of the assumptions was wrong; or

3) contend that, even if the assumptions were correct, they do not themselves support the assessment.[51]

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facts 'are in a special degree if not exclusively, within the [taxpayer's] cognizance,' the minister is obliged to rely, as a rule, on the taxpayer's disclosures. As a consequence, when assessing the taxpayer, the minister may have to assume certain matters to be different from, or additions to, what the taxpayer has disclosed. The issues in dispute will often deal with subjective elements such as the taxpayer's knowledge, intention, or motives. The equities between the parties, in terms of knowledge of the facts, are therefore skewed in favour of the taxpayer. The taxpayer is contesting the assessment in relation to his or her own affairs and is therefore in the best position to adduce the relevant evidence to prove the material facts. Were the minister to bear the burden of proving facts of which he or she had no firsthand knowledge, the system would not function effectively (if at all). Thus, given the nature and structure of the income tax regime and the taxpayer's degree of access to and control over the relevant information, the taxpayer must bear the initial burden in contesting the minister's assessment." William Innes and Hemamalini Moorthy, "Onus of Proof and Ministerial Assumptions: The Role and Evolution of Burden of Proof in Income Tax Appeals" (1998), vol. 46, no. 6 *Canadian Tax Journal* 1187-1211, at 1191-92. See also *Pollock v. The Queen*, 94 DTC 6050, at 6053 (FCA); and *First Fund Genesis Corporation v. The Queen*, 90 DTC 6337, at 6340 (FCTD).

51 *MNR v. Pillsbury Holdings Ltd.*, 64 DTC 5184, at 5188 (Ex. Ct.). The onus on taxpayers is to make out a prima facie case. As L'Heureux-Dubé J explained in *Hickman Motors Limited v. The Queen*, 97 DTC 5363, at 5376 (SCC):

> It is trite law that in taxation the standard of proof is the civil balance of probabilities: *Dobieco v. Minister of National Revenue*, [1966] S.C.R. 95, and within that balance of probabilities, there can be varying degrees of proof required in order to discharge the onus, depending on the subject matter: *Continental Insurance Co. v. Dalton Cartage Ltd.*, [1982] 1 S.C.R. 164; *Pallan v. M.N.R.*, 90 DTC 1102 (T.C.C.) at p. 1106. The Minister, in making assessments, proceeds on assumptions (*Bayridge Estates v. M.N.R.*, 59 DTC 1098 (Ex. Ct.), at p. 1101) and the initial onus is on the taxpayer to "demolish" the Minister's assumptions in the assessment (*Johnston v. M.N.R.*, [1948] S.C.R. 486; *Kennedy v. M.N.R.*, 73 DTC 5359 (F.C.A.), at p. 5361). The initial burden is only to "demolish" the *exact* assumptions made by the Minister *but no more*: *First Fund Genesis v. The Queen*, 90 DTC 6337 (F.C.T.D.), at 6340.

The minister has the burden of establishing facts that he did not find or assume in assessing the taxpayer and which he pleads in the alternative or in addition to the facts assumed.[52]

The principle that a party is entitled to raise any legal argument that the facts will support[53] has been altered in litigation before the Tax Court of Canada by provisions such as sections 48 and 49 of the Tax Court Rules (General Procedure).[54] They require parties to plead not only facts but also the statutory provisions and the reasons on which they intend to rely.[55] Parties nonetheless remain

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> This initial onus of "demolishing" the Minister's exact assumptions is met where the appellant makes out at least a *prima facie* case: *Kamin v. M.N.R.*, 93 DTC 62 (T.C.C.); *Goodwyn v. M.N.R.*, 82 DTC 1679 (T.R.B.).

52 *Pillsbury*, supra footnote 51. In the *Hickman Motors* case, L'Heureux-Dubé J also considered the position of the minister after a taxpayer makes out a prima facie case. That is,

> [w]here the Minister's assumptions have been "demolished" by the appellant, "*the onus shifts to the Minister to rebut the prima facie case*" made out by the appellant and to prove the assumptions: *Maglib Development Corp. v. The Queen*, 87 DTC 5012 (F.C.T.D.), at p. 5018. . . .
>
> As Brulé, T.C.J. stated in *Kamin*, *supra*, at p. 64:
>
> The Minister should be able to rebut such [*prima facie*] evidence and bring forth some foundation for his assumptions. . . .
>
> The Minister does not have a *carte blanche* in terms of setting out any assumption which suits his convenience. *On being challenged by evidence in chief he must be expected to present something more concrete than a simple assumption*.

Hickman Motors, supra footnote 51, at 5377.

53 The principle, as stated by Lord Denning in *Re Vandervell's Trusts (No. 2)*, [1974] 3 All ER 205, at 213 (CA), was applied by MacGuigan JA in *The Queen v. Imperial General Properties Ltd.*, [1985] 1 FC 344, at 351-52 (FCA), as follows: "It is sufficient for the pleader to state the material facts. He need not state the legal result. If for convenience he does so, he is not bound by, or limited to, what he has stated. He can present, in argument any legal consequence of which the facts permit." See also *Canadian National Ry Co. v. Saint John Motor Line Ltd.*, [1930] SCR 482, at 485-87.

54 Tax Court of Canada Rules (General Procedure), SOR/90-688 (1990), vol. 124, no. 22 *Canada Gazette Part II* 4376-4463, as amended.

55 Rule 48 of the Tax Court Rules (General Procedure) stipulates that every notice of appeal shall be in form 21(1)(a), which requires taxpayers, inter alia, to relate the material facts relied on, specify the issues to be decided, and refer to the statutory provisions relied on. Rule 49 similarly provides that every reply shall state, inter alia, the issues to be decided, the statutory provisions relied on and the reasons the respondent intends to rely on. As regards appeals in the Tax Court of Canada governed by the informal procedure, rules 4(1) and (2) of the Informal Procedure Rules (SOR/90-688, ibid., at 4464-76) provide as follows:

> (1) An appeal instituted under these rules shall comply with section 18.15 of the Act which reads in part, as follows:

free to challenge or defend assessments on any basis they choose as long as this is reflected in the pleadings. Their entitlement to rely on additional or alternative grounds to those originally pleaded depends on when those grounds are advanced in the proceedings.

Litigation is largely an educative process. What parties understand to be the dispute between them at the outset of an action often changes as the litigation progresses. After the exchange of pleadings, the preparation and exchange of affidavits or lists of documents, and the conduct of examinations for discovery, parties take stock of what they have learned and adjust their case accordingly. To that end, the rules of procedure allow taxpayers and the Crown to amend their pleadings[56] subject to certain restrictions, the principal one being that an amendment will be permitted only if it can be made without prejudice to the other side.[57]

> "18.15 (1) An appeal referred to in section 18 shall be made in writing and shall set out, in general terms, the reasons for the appeal and the relevant facts, but no special form of pleading is required unless the Act out of which it arises expressly provides otherwise.
>
> (2) An appeal referred to in section 18 may be brought in the form set out in the rules of Court.
>
> (3) An appeal referred to in section 18 shall be instituted by filing in, or mailing to, an office of the Registry of the Court the original of the written appeal referred to in subsection (1)."
>
> (2) The appeal may be brought in the form set out in Schedule 4 to these rules.

Rule 6 of the Informal Procedure Rules is identical to rule 49(1) of the General Procedure Rules.

56 Rule 54 of the Tax Court Rules (General Procedure) provides, "A pleading may be amended by the party filing it, at any time before the close of pleadings, and thereafter either on filing the consent of all other parties, or with leave of the Court, and the Court in granting leave may impose such terms as are just." Although there is no comparable provision in the Informal Procedure Rules, the Tax Court of Canada nonetheless has jurisdiction to allow amendments to pleadings filed under this procedure. In *Blais v. MNR*, 79 DTC 745, at 750 (TRB), in granting the minister's application to amend the reply to notice of appeal that he had filed with the Tax Review Board, which operated according to rules similar to those of the Tax Court of Canada under the informal procedure, Chairman Chardin stated, "It is perhaps worth noting here that the Board is not only a court of first instance but a court which, according to the statute which created it and for practical reasons, enjoys a certain flexibility and informality which could not properly be exercised by the ordinary courts. The Board's flexibility allows taxpayers who in some cases have only a vague knowledge of the Act and the procedure to be followed in tax matters, to present their grievances nonetheless to an independent tribunal and to obtain, not an administrative opinion, but a purely judicial decision on a legal basis for their claims. In order for the Board's flexibility to be equitably exercised, it must be applied equally to both parties."

57 As Décary JA stated in *The Queen v. Canderel Limited*, supra footnote 46, at 5360, "[W]hile it is impossible to enumerate all the facts that a judge must take into consideration in determining whether it is just, in a given case, to authorize an amendment, the general rule is that an

This will be the case where a court is satisfied that, had the opposing party been given timely notice of the new allegation, he or she would not have led different or additional evidence, or taken a different approach in examinations for discovery or cross-examination.[58] While this approach implies that amendments will be permitted at a very late stage in the proceedings—for example, near the end of a trial or even in argument—the likelihood that such amendments can be made without prejudice to the other side is significantly diminished. As the Federal Court of Appeal explained in *The Queen v. Canderel Limited*,

> [a]s regards interests of justice, it may be said that the courts and the parties have a legitimate expectation in the litigation coming to an end and delays and consequent strain and anxiety imposed on all concerned by a late amendment raising a new issue may well be seen as frustrating the course of justice. . . .
>
> While it is true that leave to amend may be sought at any stage of a trial, it is safe to say that the nearer the end of the trial a motion is made, the more difficult it will be for the applicant to get through both the hurdles of injustice to the other party and interests of justice.[59]

The goals of finality and fairness, which Meghji and Grenon cited as one reason for precluding the Crown from changing the basis on which it defends an assessment after the period prescribed in subsections 152(4) and (5) has expired,[60] are therefore factors that a judge already takes into account in determining whether or not it is just to allow an amendment. Similar considerations apply in determining a party's entitlement to raise new issues before an appellate court.[61]

The reasons given by the Supreme Court of Canada in the *Continental Bank* case for prohibiting the Crown from defending an assessment on an alternative basis are not only at odds with the principles that govern the entitlement of parties to amend their pleadings, but also ignore the principle that, when the Crown defends an assessment on a different basis from that relied on by the minister,

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amendment should be allowed at any stage of an action for the purpose of determining the real questions in controversy between the parties, provided, notably, that the allowance would not result in an injustice to the other party not capable of being compensated by an award of costs and that it would serve the interests of justice."

58 For example, in *Conmac Western Industries etc.* (1993), 9 Alta. LR (3d) 232, at 306 (QB), Chrumka J stated, "Even though the application to amend is being made for the first time in argument, the amendment may be granted if it does not prejudice the Robinsons, in the sense that, had they been aware of this evidence at trial, they might have led different evidence or a different emphasis would or might have been given or a different approach taken in cross-examination or on examination for discovery."

59 Supra footnote 46, at 5361-62.

60 Supra footnote 39.

61 Supra footnote 36.

the burden shifts to the Crown.[62] The effect is to undermine the litigation process. Since the minister's knowledge of a taxpayer's affairs is limited and often wholly dependent upon the taxpayer's cooperation, the assumptions underlying an assessment are sometimes more a matter of conjecture than fact. Only when the dispute reaches the Tax Court of Canada does the Crown have the opportunity to fully ascertain and assess the taxpayer's position.[63] Depending on when an appealed assessment is issued, some or all of the litigation may take place after the statutory period for reassessing has passed. While taxpayers would presumably still be entitled to challenge assessments on any basis they wished, and to act on what they had learned during the litigation process by changing their position accordingly, the Crown would be precluded from doing so. The Crown would also be prohibited from responding to new submissions by taxpayers or to additional issues raised by a judge,[64] or even from making

62 As Robert McMechan and Gordon Bourgard indicated in *Tax Court Practice* (Scarborough, Ont.: Carswell) (looseleaf), 4-107, this principle has been affirmed in the following cases, as well as many others: *Youngman v. The Queen*, supra footnote 47; *Maroist v. MNR*, 90 DTC 1524 (TCC); *Wolofsky et al. v. MNR*, 90 DTC 1345 (TCC); *Wise et al. v. The Queen*, 86 DTC 6023 (FCA); *Smythe et al. v. MNR*, 67 DTC 5334 (Ex. Ct.); and *Nicholson v. Minister of National Revenue* (1945), 2 DTC 735 (Ex. Ct.).

63 "While it is true that the minister has broad powers of investigation under the Act, the self-assessment system would collapse if the minister were required to prove the facts underlying every disputed assessment." Innes and Moorthy, supra footnote 50, at 1189.

64 Judges have an inherent power to raise matters with counsel that they believe are relevant to the litigation. The power was exercised, for example, by the Saskatchewan Court of Appeal in *Barrett v. Nor. Lights, etc.*, [1988], 3 WWR 500. Sherstobitoff JA, on behalf of the majority of the court, wrote at 512, "An issue not raised at the trial, nor at the first hearing of the Appeal, which is of crucial importance to the case is whether the position held by Barrett was a statutory office and, if so, whether administrative law principles which require that he be treated fairly apply, as opposed to the law governing ordinary employment. The Court raised the issue suo motu, and a second hearing was held to deal with it. This issue determines the outcome of the case." Rule 60 of the Federal Court Rules, 1998, SOR/98-106, gives a trial judge of the Federal Court—Trial Division the power to reopen a trial on his own motion or on a motion from one of the parties and to draw the attention of the parties to any gap in the proof or in the proceedings and permit them to fill it, on such conditions as he or she may determine. The decision of Pratte J (as he then was) in *Couture v. The Queen* is illustrative of how the predecessor to rule 60, rule 496 of the Federal Court Rules, CRC 1978, c. 663, was applied in circumstances where it was anticipated that the raising of a new issue would give rise to a need for further evidence. In that case, rule 496(2) was invoked after reasons for judgment were given to permit the plaintiff to allege an additional ground of negligence in his pleading. The plaintiff was a cable television operator who spent a substantial amount of money in the construction of facilities in the mistaken belief that he had received authorization to operate a receiving station. He claimed to be entitled to compensation from the Crown to the extent that the damage suffered by him was caused by the fault of the employees of the Canadian Radio-Television and Telecommunications Commission (CRTC) in the performance of their duties. While Pratte J concluded that the Crown was not liable for the acts of the

concessions[65] if this involved defending an assessment on an alternative basis. The Crown might even be precluded from dealing with an issue that arose as a result of an appellate court's referring a matter back to the Tax Court of Canada for a rehearing. Such constraints are contrary to the public interest. They unfairly favour taxpayers and create an incentive on their part to delay the litigation so that as much of it as possible is conducted after the expiry of the reassessment period. These constraints also frustrate the identification and resolution of the real controversy between taxpayers and the Crown. Faced with these potential consequences, Parliament had little choice but to respond with remedial legislation.

RESTORING THE CROWN'S ENTITLEMENT TO RELY ON ALTERNATIVE GROUNDS TO SUPPORT AN ASSESSMENT

Efficacious remedial legislation necessarily proceeds from a proper understanding of the decision sought to be reversed. For example, the *Continental Bank* case could be interpreted as a decision by the Supreme Court of Canada to redefine the meaning of an assessment to include both a person's liability under the Act and the process by which it was reached. If correct, it would then have made the rules governing pleadings and their amendment, as well as the circumstances in which a new issue can be raised before an appellate court, subject to subsections 152(4) and (5), even when the minister is not seeking to appeal his assessment. To reverse such a result and at the same time affirm the validity of the jurisprudence apparently ignored in the *McLeod* and *Continental Bank* cases, Parliament could have introduced a provision that defined an assessment as only including the amount of a taxpayer's liability under the Act. Of course, if the courts subsequently disagreed with Parliament's interpretation of the *Continental Bank* case, the amendment would then be rendered ineffective. As it turns out, the Supreme Court of Canada appears indeed to have reached its decision through a different route.

The Supreme Court's reliance on the *British Columbia Telephone Co.* case suggests that it did not redefine the meaning of an assessment. Rather, it limited

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employees of the CRTC, he found that the Department of Transport was negligent in issuing an invalid licence and that it was the duty of the CRTC, in so far as it knew or ought to have known that such a licence had been issued, to make clear that it was invalid. However, the latter grounds of negligence were not pleaded by the plaintiff. As a result, Pratte J held, "Because of this, and taking into advantage of Rule 496(2), I shall not give judgment immediately in this case, so that suppliant, if he sees fit, may submit a motion for permission to amend his pleadings and reopen the hearing." Reasons for judgment filed April 7, 1972. See also [1972] FC 1137 (TD), aff'd. [1974] FC 107 (CA). Rule 138 of the Tax Court Rules (General Procedure) similarly empowers a judge of the Tax Court of Canada.

65 Supra footnote 18.

the Crown's ability to defend an assessment by restricting its procedural entitlement either to amend its pleadings at trial or to raise an issue for the first time before an appellate court after the expiry of the statutory period for issuing reassessments. The Federal Court of Appeal appears to share this view. In *The Queen v. Hollinger Inc.*,[66] the court concluded that the principle enunciated in the *Continental Bank* case—namely, that the Crown is not permitted to advance a new basis for an assessment after the statutory period has expired—does not mean that the Crown can do so only if the minister issues a reassessment before the expiry of this period. As Létourneau JA explained,

> [u]nder the existing law at the time, if the Minister was entitled to change the basis of the reassessment within the limitation period, counsel claimed, he could only do that formally by either issuing a new reassessment or amending the existing reassessment. Consequently, the mere pleading of such new basis in the Reply is not sufficient to validly raise the issue and prevent the limitation period from expiring. He relied to sustain his claim upon the following passage from Bastarache, J.:
>
> > The Crown is not permitted to advance a new basis for reassessment after the limitation period has expired.
> >
> > With respect, I do not read this statement of Bastarache, J. as imposing a formal procedure or a procedural restriction of the kind suggested by the Respondent.
> >
> > First, the quoted passage refers to the Crown, not the Minister. Had Bastarache, J. mentioned the Minister, it could have been a possible indication that he had in mind the procedure itself. Second, it speaks of "advancing a new basis for reassessment," thereby referring to the Crown's actual practice of advancing a new argument in its pleadings in support of the assessment.[67]

In other words, as long as the Crown seeks only to support an assessment on a different factual, legal, or statutory basis, and does not attempt to increase the amount of the assessment, it can attempt to do so through procedural means. A reassessment is unnecessary. As Létourneau JA noted, what the Supreme Court of Canada is concerned with "is the possible unfairness to the taxpayer when notification of the new basis, whatever form it may take, is either inadequate or given too late and, as a result, the taxpayer is not afforded a proper opportunity to respond."[68]

Further to the notice of ways and means motion tabled in the House of Commons on December 10, 1998,[69] the Finance minister announced on December 23, 1998 that Parliament intended to amend the Act "to clarify that Revenue

66 Supra footnote 37.

67 Ibid., at 5504.

68 Ibid., at 5505.

69 Canada, Department of Finance, Notice of Ways and Means Motion To Amend the Income Tax Act, To Implement Measures That Are Consequential on Changes to the Canada-U.S. Tax

Canada may, in the course of an income tax appeal, rely on alternative grounds to support its assessment."[70] The proposed amendment read as follows:

> 1. (1) Section 152 of the *Income Tax Act* is amended by adding the following subsection:
>
> (9) Subject to subsection 152(5), an assessment shall not be vacated, varied, or referred back to the Minister for reconsideration and reassessment by reason only of the identification by the Minister of an alternative basis of liability for the assessment.
>
> (2) Subsection (1) applies to appeals disposed of after Royal Assent.[71]

A question arose, however, as to whether or not prohibiting a court from allowing an appeal by reason only of the identification of alternative grounds for supporting an assessment also entitled the Crown to defend the assessment on this basis. For example, if the proposed amendment had been in force when the *Continental Bank* case was under consideration, and if the Supreme Court of Canada had found that Leasing had entered into a partnership with Central, it is arguable that, even though the court would have been prohibited from dismissing the Crown's appeal solely because the Crown had raised an alternative basis of liability for the assessment, it could still have declined to consider the submission and, as a result, dismissed the appeal on other grounds.

On March 10, 1999, the Finance minister tabled a revised notice of ways and means motion that incorporated changes made in response to comments received in relation to the December 10, 1998 motion.[72] The motion also included legislation containing a new amendment aimed at allowing the minister to advance alternative arguments after the expiry of the reassessment period.[73] The

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Convention (1980) and To Amend the Income Tax Conventions Interpretation Act, the Old Age Security Act, the War Veterans Allowance Act and Certain Acts Related to the Income Tax Act, December 10, 1998.

70 Canada, Department of Finance, *Release*, no. 98-134, December 23, 1998.

71 Ibid.

72 Canada, Department of Finance, Notice of Ways and Means Motion To Amend the Income Tax Act, To Implement Measures That Are Consequential on Changes to the Canada-U.S. Tax Convention (1980) and To Amend the Income Tax Conventions Interpretation Act, the Old Age Security Act, the War Veterans Allowance Act and Certain Acts Related to the Income Tax Act, March 10, 1999.

73 The explanatory notes to the proposed amendment described its purpose as follows: "New subsection 152(9) of the Act is intended to ensure that the Minister of National Revenue may advance alternative arguments in support of an income tax assessment after the normal assessment period has expired. This amendment is proposed in light of remarks by the Supreme Court of Canada in the case of The Queen v. Continental Bank of Canada to the effect that the Crown is not permitted to advance a new basis for assessment after the limitation period has expired." Canada, Department of Finance, *Revised Explanatory Notes Relating to Income Tax* (Ottawa: the department, March 1999), clause 63.1.

amendment presumes that the right to advance an argument imposes a concomitant obligation on the courts to consider it. In that regard, section 63.1(2) of the Income Tax Amendments Act, 1998 provides as follows:

> Section 152 of the Act is amended by adding the following after subsection (8):
>
> (9) The Minister may advance an alternative argument in support of an assessment at any time after the normal reassessment period unless, on an appeal under this Act,
>
> (a) there is relevant evidence that the taxpayer is no longer able to adduce without the leave of the court; and
>
> (b) it is not appropriate in the circumstances that the evidence be adduced.[74]

The amendment received royal assent on June 17, 1999.[75]

Under subsection 152(9), the minister, and therefore the Crown,[76] is entitled to support an assessment on an alternative basis where further taxpayer evidence is unnecessary, or as long as taxpayers can still lead evidence without having to seek leave of the court, or if leave is necessary, as long as a court determines that it is appropriate in the circumstances for evidence to be adduced. Whereas leave might be needed, for example, if the Crown raises a submission for the first time at trial after the close of a taxpayer's case, it might not be needed if this is attempted before the outset of the hearing. Given the basis for the Supreme Court of Canada's decision in the *Continental Bank* case, it arguably follows that the principles governing the ability of parties to amend their pleadings or to raise matters for the first time before an appellate court[77] are subsumed under subsection 152(9). This may be the case even though the terms of subsection 152(9) do not expressly refer to the issue of prejudice and focus only on whether or not it is appropriate for the taxpayer to adduce evidence. As Létourneau JA stated in the *Hollinger* case,

> Subsection 152(9) assented to on June 17, 1999 allows for an alternative argument in support of an assessment to be advanced at any time after the normal reassessment period, subject to a discretion given to the Court to refuse it *if prejudice could result to the taxpayer from the late change* [emphasis added].[78]

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74 SC 1999, c. 22, section 63.1(2).

75 Ibid.

76 "[I]t is common form for statutes to impose obligations and confer rights on Her Majesty by requiring the Minister who is in charge of the particular part of Her Majesty's affairs to make a payment or do something, or by authorizing such Minister to do something. Obviously such a statute does not impose an obligation or confer a right on the person who happens to be a Minister in his private capacity. All such statutes are merely using a device to impose duties or confer rights on Her Majesty in what is regarded as a more dignified way." *In re Mastino Developments Ltd. v. The Queen et al.*, 72 DTC 6211, at 6214 (FCTD).

77 Supra footnotes 36 and 58.

78 Supra footnote 37, at 5505.

However, if subsection 152(9) leaves room for separate consideration of whether or not, for example, taxpayers would have taken a different approach on examinations for discovery or cross-examination, it does not mean that these questions will be dealt with separately. As a matter of practice, any and all issues touching upon the Crown's entitlement to defend an assessment on an alternative basis will be canvassed when the Crown applies to amend its pleadings or to raise a new issue before an appellate court. The result is in keeping with the desire expressed by Létourneau JA in the *Hollinger* case to avoid "an unnecessary measure of formalism, unwarranted by the decision of the Supreme Court and the subsequent amendment to section 152."[79]

ADDENDUM

Following the submission of this article for publication, the Tax Court of Canada and the Federal Court of Appeal had occasion to consider subsection 152(9). In *Smith Kline Beecham Animal Health Inc. v. The Queen*,[80] the Crown applied for leave to amend its reply to notice of appeal in order to plead an "'alternative legal basis' for defending certain assessments of Part XIII tax."[81] In support of its application, the Crown argued that

- the amendment was necessary to determine one of the questions in issue, namely, whether or not an alleged overpayment by the taxpayer to an affiliated corporation resulted in liability for part XIII tax;[82]
- the amendment does not result in a claim for more tax than has already been assessed;[83] and
- the taxpayer would not be prejudiced by the amendment because its counsel was advised of the Crown's intention to seek the amendment during the discovery process.[84]

Counsel for the taxpayer argued that

> the amendment sought would "fundamentally alter" the Part XIII assessments under appeal; that the Part XIII limitation period expired at least two years ago and that new subsection 152(9) does not assist the Minister for it permits the Minister to advance new arguments in support of assessments but does not permit the Minister to advance a "new basis of assessment" following expiry of the

79 Ibid.

80 2000 DTC 1527 (TCC).

81 Ibid., at 1527.

82 Ibid., at 1529.

83 Ibid.

84 Ibid.

> section 152 limitation period. The latter, according to the Appellant, is what the Respondent seeks to do but may not do.[85]

The presiding motions judge, Bonner TCJ, agreed with the Crown's position and allowed the amendment. After concluding that the situation in the *Smith Kline Animal Health Inc.* case was not analogous to that before the Supreme Court of Canada in the *Continental Bank* case, which involved the application of the rule that prevents parties from "raising points on appeal which were not pleaded or argued at trial,"[86] and that the court likely did not intend to preclude the minister from defending an assessment on a different provision of the Act from that relied on by the assessor,[87] Bonner TCJ stated:

> In any event, I disagree with the Appellant's argument which essentially asserts that subsection 152(9) of the Act is inapplicable because the Minister is attempting by amendment to change the basis of assessment at a time when it is too late to do so by reason of subsection 152(4). When subsection 152(4) is read in the new statutory context which includes subsection 152(9) it is evident that it cannot be said that the legislature intended that the advancing of arguments in support of an existing assessment can constitute the exercise of the power to reassess. Section 152 differentiates between assessment and reassessment on the one hand and the appeal process on the other. What the Respondent seeks is an amendment to the Reply which will permit him to do precisely what the plain language of subsection 152(9) permits, namely, advance an alternative argument in support of the Part XIII assessment. He seeks to argue in the alternative that the existing assessment of tax is supported by provisions of the Act other than those relied upon by the assessor and this he is entitled to do.[88]

Bonner TCJ then considered whether or not leave to amend the reply to notice of appeal should be granted under rule 54 of the Tax Court Rules (General Procedure).[89] He held that it should since the taxpayer would not suffer prejudice if the amendment were allowed. That is,

> [a]llowing the amendment now will do nothing more than place the parties in the same position as if the Respondent had adequately raised section 245 in the first place. Counsel for the [taxpayer] did not suggest that the discovery process would have to be reopened if leave to amend is granted. Nothing in the material suggests that the amendment sought would delay the expeditious trial of the matter.[90]

85 Ibid.

86 Ibid., at 1530.

87 Ibid.

88 Ibid., at 1531.

89 Supra footnote 56.

90 Supra footnote 80, at 1531.

Bonner TCJ further noted that not to allow the amendment would prevent "the court from considering a possibly relevant provision of the Act when deciding the case on its merits."[91]

On appeal to the Federal Court of Appeal, Sharlow JA, on behalf of a unanimous bench, held:

> We are all of the view that the Tax Court Judge was correct in characterizing the proposed amendment to the Crown's pleadings as a new argument in support of the assessment, and that subsection 152(9) of the Income Tax Act permitted the argument to be made. . . . The appeal will be dismissed.[92]

CONCLUSION

The principles and rules by which a legal claim is enforced and a proceeding is conducted, including appeals from assessments under the Act, are fundamental aspects of the rule of law. Hence, the enactment by Parliament of subsection 152(9), which incorporates a principle that the Supreme Court of Canada has struck down in the *Continental Bank* case on the grounds that it is unfair to taxpayers, calls for an inquiry into the reasons for this difference of views. Having undertaken such an inquiry, the author submits that, although the court's desire to ensure fair treatment for taxpayers is laudable, the same cannot be said about its reasoning for precluding the Crown from defending an assessment on an alternative basis. The failure of the court to canvass the extensive jurisprudence relevant to the question, coupled with its narrow reliance on the *McLeod* and *British Columbia Telephone Co.* cases, appears to have caused it to posit the same policy concerns for a legal proceeding as for an assessment. However, these procedures are governed by different considerations and therefore are subject to different rules for weighing the equities between taxpayers and the minister. The failure of the Supreme Court of Canada to observe this distinction undermined the cause of fairness and necessitated the passage of remedial legislation.

91 Ibid.

92 Unreported, February 11, 2000, A-721-99.