

SUPREME COURT OF CANADA: THE IMPOSITION OF THIRD PARTY PENALTIES DO NOT CREATE AN “OFFENCE” ENGAGING CONSTITUTIONAL PROTECTIONS

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On July 31, 2015, the Supreme Court of Canada held, in *Guindon v. Her Majesty the Queen*, 2015 SCC 41 that the imposition of penalties under section 163.2 of Canada’s *Income Tax Act* (“**Tax Act**”) on third parties involved in the making of false statements does not involve the commission of an offence and therefore does not attract constitutional protections that are normally afforded to those accused of criminal offences.

Section 163.2 of the Tax Act allows the Canada Revenue Agency (“**CRA**”) to impose penalties on third parties who make (or participate in making) false statements knowingly or in circumstances amounting to “culpable conduct”. Culpable conduct is defined as action or inaction that is tantamount to intentional conduct, shows an indifference as to tax compliance, or shows a “wilful, reckless or wanton disregard of the law”. The penalty was intended to apply primarily to third party tax planners, such as promoters of tax shelters, and to tax return preparers. In the right circumstances, the penalty can be enormous, since it is usually calculated by reference to the third party’s “gross entitlements” or “gross compensation” (such as actual or contingent planning or tax return preparation fees) and/or by reference to gross negligence penalties to which the related taxpayer could be liable.

In *Guindon*, a non-tax lawyer was approached by the promoters of a leveraged charitable donation program. Participants in the program would acquire timeshare units of a resort and then donate the units to a charity at a fair market value that exceeded their cash payment for the timeshares. The non-tax lawyer agreed to provide an opinion on the tax consequences of the program despite her lack of expertise in tax matters and despite not having reviewed the relevant documents. The opinion was intended to be part of the promotional package for the donation scheme. The lawyer, who was also the president and administrator of the charity, also signed many false tax donation receipts. CRA assessed a third party planner penalty in excess of

\$540,000 after the donation scheme was determined to be a sham: in fact, there were no timeshare units, and nothing was donated to the relevant charity.

The assessed lawyer argued, in part, that section 163.2 created a criminal offence, and therefore that she had been deprived various Canadian constitutional protections that are afforded to persons who are charged with a criminal offence, such as the right to be presumed innocent and the right not to have the penalties imposed until after charges are laid and a fair trial is conducted before an independent and impartial tribunal.¹ The Tax Court of Canada accepted these arguments, but the Federal of Appeal did not. The appellate court determined that section 163.2 did not create an offence, but was an administrative provision that was integral to Canada's self-reporting and self-assessing taxation system.

The Supreme Court of Canada upheld the penalties. The majority of the judges agreed that section 163.2 was not, by its nature, a criminal provision and that section 163.2 did not give rise to penal consequences. Instead, section 163.2 was a non-criminal provision that was essential to deter non-compliance with the administrative scheme of the Tax Act. A minority of the Supreme Court judges upheld the penalties on other, procedural, grounds.

Canada's Tax Act is necessarily a dual purpose statute. It is designed to set out an administrative scheme for the assessment and collection of tax, but it is also designed to deter conduct that would lead to an improper loss to the fisc. The line between administrative deterrence and deterrence from criminal wrongdoing in the tax context is sometimes blurry, as *Guindon* aptly illustrates. Taxpayers' advisors should be aware that the imposition of section 163.2 penalties is now definitively considered an administrative deterrence, and therefore that in the right circumstances, enormous monetary penalties can be imposed and upheld on third party tax planners or tax return preparers without the constitutional protections afforded in the penal/criminal context.

¹ These constitutional protections are set out in section 11 of the *Canadian Charter of Rights and Freedoms*, Part I of the *Constitution Act, 1982*, being Schedule B to the *Canada Act 1982 (UK) 1982*, c 11.