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INCOME TAX

PRACTICE

Appeal from Tax Court of Canada decision (2022 TCC 43) awarding respondent partial indemnity costs equal to 75 percent of actual legal expenses, 100 percent of disbursements — Tax Court had previously allowed respondent's appeal from Minister of National Revenue's assessment of penalty for gross negligence in making false statement in income tax return — Issues herein whether Tax Court: (1) fettered its discretion in deciding *a priori* that costs should fall within given range; (2) erred in principle in its treatment of three factors to be considered in award of costs (i.e. result of proceeding, settlement offer, pre-litigation conduct); (3) breached appellant's right to procedural fairness in considering factor not raised in submissions — Tax Court first considered basis upon which lump sum costs could be awarded, concluding that 50 to 75 percent range of solicitor-client costs should be used — Tax Court then proceeded to review factors set out in *Tax Court of Canada Rules (General Procedure)*, SOR/90-688a, s. 147, holding that success of respondent at trial, importance of amount at issue for respondent weighing heavily in favour of award of costs at upper-limit of partial indemnity costs range, importance of issue decided, offer to settle made by the respondent, conduct of Minister before commencement of proceeding all favouring increased partial indemnity costs award — Tax Court fettered its discretion, erred in law by establishing range before even considering factors set out in s. 147(3) — Such approach precluding possibility of lower range following review of like cases — In addition, ranges considered not consistent — Tax Court erred in principle in not addressing it's own case law in setting range of possible awards — With respect to result of the proceeding, Tax Court quoted *Lux Operating Limited Partnership v. The Queen*, 2018 TCC 214, 2018 D.T.C. 1156 — However, it proceeded to take position at odds with *Lux*, finding that fact respondent achieved 100 percent success weighed heavily in favour of increased costs — Respondent's success was factor that could be taken into consideration, but only on issue of entitlement to costs, reason being that factors which might favour increase or decrease in successful party's costs set out in remaining s. 147(3) factors — Tax Court thus erred in defining scope of this factor — Tax Court also erred in failing to justify departure from *Lux* as it was required to do pursuant to principle of judicial comity — With respect to respondent's offer of settlement, Tax Court wrong to say it was principled — Respondent's offer requiring Minister to vacate penalties assessed under *Income Tax Act*, R.S.C., 1985 (5th Supp.), c. 1, s. 163(2) — According to respondent, her negligence made her liable for lesser penalty set out in Act, s. 162(7) — Respondent further argued that since there was no other provision in Act that provided penalty for negligently making false statements in income tax return, s. 162(7)(b) applied — However, general language of s. 162(7)(b) limited to instances of failure to file returns or to provide information not specifically enumerated in balance of s. 162 — Therefore, notwithstanding its broad words, s.162(7)(b) limited to obligations to file returns or to provide information as and when required — S. 162(7)(b) would not apply to returns filed when required but negligently prepared — That being the case, respondent's settlement proposal was not one which Minister could have accepted as lower penalty under s. 162(7)(b) not

available to respondent — Respondent's offer also not principled in that respondent not prepared to admit she had in fact been negligent, only that she could have been — In those circumstances, respondent's offer consisted of pointing out weaknesses of appellant's case, offering him compromise based upon possibility of her liability for lesser penalty — Thus difficult to see how respondent's offer could be principled — Respondent's alternate submission was that matter could be settled on basis of Minister's cancellation of penalty assessed under Act, s. 163(2) pursuant Act, s. 220(3.1) on basis penalty grossly excessive, disproportionate, overly punitive —- However, penalty imposed by s. 163(2) statutory penalty, not discretionary penalty which can be imposed or not at Minister's discretion — Must be assumed herein that in assessing respondent in the way he did, and given fact matter proceeded to trial despite offer to settle, appellant's view was that facts and law justified conclusion that respondent's conduct in relation to her income tax return amounted to gross negligence — As long as appellant was satisfied that respondent had been grossly negligent, was bound to give effect to statutory penalty — Respondent's settlement offer was not principled offer in the sense it was not one which the appellant could accept — As a result, failure to accept offer was neutral factor in determination of appropriate award of costs —Consequently, Tax Court's conclusion that appellant's failure to accept respondent's offer of settlement justified increase in costs contained an extricable error of law, namely scope of s. 162(7)(b) — With respect to pre-litigation conduct, Tax Court concluded that failure of Minister's representatives to interview respondent before commencement of proceedings was conduct prior to the litigation that prolonged proceeding, weighed heavily in favour of increased costs — Appellant argued that Tax Court breached duty of procedural fairness in depriving him of opportunity to address this matter before Tax Court relied upon it as a factor justifying an increase in costs — In this case, both parties were no doubt aware that Tax Court was entitled to work its way down list of factors in s. 147(3), that it was not unusual for Tax Court to touch upon factors which were not specifically pleaded by parties — Tax Court cited *Canada v. Martin*, 2015 FCA 95 as authority for proposition that in exceptional circumstances, party's conduct prior to proceeding can be considered — However, passage quoted by Tax Court does not authorize inquiry into pre-litigation conduct — Pre-litigation conduct not stage in proceeding — In the circumstances, appellant could not be faulted for failing to recognize that Tax Court would consider pre-litigation conduct in assessing costs — While a court may exercise its discretion to not grant a remedy for breach of procedural fairness where result inevitable, issue of pre-litigation conduct weighed heavily in favour of increased costs — Other factors that weighed heavily in favour of increased costs found to be either incorrectly understood or incorrectly applied — As a result, it could not be said that result upon reconsideration was inevitable —Breach of procedural fairness justified remitting matter to Tax Court for reconsideration — Other errors discussed above (fettering of discretion as to range of partial indemnity, effect of success at trial, conclusion that respondent's offer to settle was principled) also justified returning matter to Tax Court — Appeal allowed.

CANADA V. BOWKER (A-82-22, 2023 FCA 133, Pelletier J.A., reasons for judgment dated June 8, 2023, 29 pp.)