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SETBACK IN BATTLE AGAINST DONATION SCAMS

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A. INTRODUCTION

On October 2, 2012, the Tax Court of Canada released its decision in *Guindon v. The Queen*.[1] The case dealt with whether the third party penalties provided under section 163.2 of the *Income Tax Act* could be assessed against the appellant. The basic purpose of s. 163.2 is to provide for monetary penalties assessable against third parties who knowingly, or in circumstances amounting to gross negligence, participate in, promote, or assist conduct that results in another taxpayer making a false statement or omission in a tax return.

In a decision that bodes enormous implications for the future of s. 163.2, Justice Bédard concluded that the provision creates a criminal sanction that can only be prosecuted in provincial court in accordance with criminal procedure and *Charter* protections. This *Charity Law Bulletin* reviews the decision and its implications for charities.

B. THE FACTS

The case dealt with a buy-low, donate-high arrangement involving time share units. Like other donation arrangements of this nature, the arrangement was fairly complex, involving a number of foreign and domestic entities. The bottom line was that donors could in effect purchase time share units for a low price and then donate them to a particular charity for a donation receipt reflecting a much a higher value.

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[1] *Guindon v. The Queen* (2012) TCC 287.

Although the appellant lacked expertise in tax law, she agreed to provide the promoters with a legal opinion representing that participants in the donation arrangement would be considered for income tax purposes to have made charitable gifts (presumably at the higher value, though the facts are not explicit on this point). Although the appellant knew that the opinion would very likely be relied upon by participants in the arrangement, she provided it without ever having reviewed all of the underlying documentation.

Further, the appellant was the president of the charitable donee participating in the arrangement. She signed 135 donation receipts acknowledging that the time share units had been donated to the charity under the arrangement. In signing the gift receipts, the appellant relied upon the verbal representations of the promoters that title to the time share units had been transferred to the charity. As it turns out, the transfers never occurred.

The Minister of National Revenue assessed penalties against the appellant under s. 163.2 totalling $546,747 for making false statements that she either knew, or, in effect, should have known, would result in other taxpayers making false statements or omissions in their tax returns. The alleged false statements included her legal opinion and the improperly issued 135 donation receipts.

C. THE HOLDING

Justice Bédard concluded that *if the penalties under s. 163.2 were civil in nature* then they were properly assessed. Two issues were highlighted as being of particular concern to the court.

The first issue was that the appellant prepared her legal opinion in support of the donation arrangement without reading all of the relevant documentation. This was problematic because she knew that participants in the program would be relying upon an improperly prepared opinion. The appellant could not deny knowing that the opinion was misleading because it contained the express statement that she had reviewed all of the principal documents even though she had not.

The second issue was that appellant (in her capacity as an officer of the participating charity) issued donation receipts solely in reliance upon the representations of the promoters of the donation arrangement that the property transfers to the charity had indeed occurred. No steps were taken to independently verify the advice received. Justice Bédard held that, although s. 163.2 does not create an across the board requirement for

charities issuing gift receipts to confirm representations of advisors that title transfers have occurred, it was inappropriate in these circumstances for the appellant to take no steps to confirm the information received. The court's reasoning on this point was not entirely clear. The concern appeared to be that the appellant had reason to be suspicious of the promoters because they pressured her into providing a supportive legal opinion without providing her all of the background materials.

Ultimately, however, the court concluded that none of these were controlling considerations because s. 163.2 created what was in substance a criminal rather than a civil sanction. The penalties would therefore have to be prosecuted not in a tax court but instead in a provincial court in accordance with criminal procedure and applicable *Charter* protections.

In coming to the conclusion that the penalties under s. 163.2 are criminal in nature, the court relied upon the following considerations:

- the penalties are not subject to an express time limit;
- the penalties are of a potentially enormous magnitude (as evidenced by the $546,747 penalty assessed against the appellant); and
- the breadth of s. 163.2 suggests that it is more akin to a statutory provision aimed at promoting public order and welfare (that is, a penal provision) than a regulatory scheme designed to ensure compliance with tax legislation (that is, a civil penalty).

On the last point, the court emphasized that s. 163.2 applies where a third party makes a false statement that "could" be relied upon regardless of whether it was ever actually relied upon by anyone. It is difficult to interpret s. 163.2 as a scheme designed to ensure compliance with tax legislation, the court reasoned, when the provision is broad enough to apply even where a false statement had not resulted in non-compliance

D. REFLECTIONS

The holding in *Guindon* will almost certainly be appealed.

If the decision is left to stand, it will become significantly more difficult to impose penalties on advisors backing abusive donation schemes (or other forms of excessively aggressive tax planning). It means that such penalties can only be prosecuted in provincial court in accordance with criminal procedure and applicable *Charter* rights. Further, the standard of proof will be raised from that of proof on a balance of probabilities to proof beyond a reasonable doubt. The outcome is so significantly damaging to the future viability of s. 163.2 that a failure to appeal would be shocking.

If the decision is not appealed (or an appeal is unsuccessful) it is likely that s. 163.2 will be amended. The provision was very broadly drafted, presumably so that it could be applied to abusive circumstances not specifically within the contemplation of Parliament at the time it was adopted. That strategy has now come back to haunt the architects of the provision. Nevertheless, the *Guindon* decision contains a number of clues regarding how the provision could be narrowed so as to avoid the character of a penal provision.

The timing of the judgment is somewhat unfortunate in that it was released while the Standing Committee on Finance is completing its study of donation incentives. The decision not only brings attention to abuses of donation incentives at a crucial moment of policymaking in this area of law, it also calls into question the current capacity of the Canada Revenue Agency to police such abuses.

The *Guindon* decision was no doubt received with some element of frustration by tax authorities. One might have thought that the facts, involving as they did a lawyer lacking expertise in tax law providing a supportive tax opinion for a donation scheme without ever reading all of the background documentation, represented exactly the kind of circumstance within the contemplation of s. 163.2. But as is so often the case, there is more than one side to this story. Assessing well over a half million dollars of fines against the appellant personally was more or less an invitation for the court to very carefully consider whether proper protections are in place. The case tells a story of overreach as much as anything else.

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