

Tax Dispute Insights

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Federal Court Sets Higher Bar for CRA: A Win for Taxpayers in Disputes

How *Onex v. Canada* Helps Taxpayers Overturn CRA Decisions

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The Federal Court of Canada's decision in *Onex Corporation v. Canada (Attorney General)*¹ highlights a meaningful development for taxpayers challenging the Agency's discretionary decisions. The FC's ruling encourages a higher standard for the Canada Revenue Agency, requiring it to more carefully consider and justify its interpretations when they result in significant consequences for taxpayers.

Justice Régimbald found that he lost confidence in the Agency's decision due to the Agency's failure to consider and explain why its more restrictive interpretation best reflected the legislature's intent. The Federal Court's ruling critiques the Agency's approach, suggesting it must adopt a more transparent and justifiable method when interpreting tax legislation.

In particular, Justice Régimbald emphasized that the greater the impact of a decision on a party's rights and interests, the more detailed and sufficient the reasoning must be. Specifically, the Court stated that "the decision-maker must clearly explain why their interpretation best reflects the legislature's intent."² And the Court reinforced the expectation that the Agency must not only justify its chosen interpretation but also demonstrate why it prevails over other possible interpretations, reflecting the Federal Court's guidance for a "reasonable decision".

We believe that Justice Régimbald's decision acknowledges the significant consequences of the Agency's discretionary powers. The decision may prompt future challenges, especially when the Agency fails to address less restrictive interpretations.

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As these developments unfold, taxpayers and their counsel should carefully consider how their circumstances align with those in *Onex*. When the Agency interprets the relevant tax acts in exercising discretion, we expect the Federal Court to apply this higher standard of reasoning, which may encourage the Agency to reconsider its established positions.

Given these considerations, we recommend that advisors and taxpayers consult with counsel to assess how this decision might influence current and future disputes.

The Relevant Facts

The Applicant, Onex Corporation, is a global asset management firm specializing in equity and credit investment. Before 2014, Onex established complex structures to receive tax-free dividends from a foreign affiliate, structures governed by the Foreign Accrual Property Income (“FAPI”) rules under the *Income Tax Act* (“ITA”). In 2014, Parliament enacted Bill C-43,³ amending the FAPI rules, with the amendments applying to tax years after July 12, 2013, unless a taxpayer elected to apply the amendments retroactively to 2010.

Onex believed its existing structures already achieved the intended legislative tax benefits under the amended FAPI rules, rendering the retroactive election unnecessary. Consequently, Onex chose not to make the election.

In June 2020, the Canada Revenue Agency reassessed Onex’s 2012 and 2013 tax returns, adding \$102 million and \$92 million to its taxable income due to the absence of the retroactive election. In response, Onex sought relief under subsection 220(2.1) of the ITA, requesting the Minister of National Revenue (the “Minister”) waive the election requirement or, alternatively, under subsection 220(3) of the ITA, requesting permission to amend its tax returns to include the election.

The Agency denied both requests, asserting that the Minister did not have the authority to waive the election requirement or extend the filing deadline. Onex then sought judicial review of the Minister’s decisions.

The Federal Court’s Ruling

The Federal Court began its analysis by confirming that the standard of review in this case was “reasonableness,” following the framework established by the Supreme Court of Canada in *Canada (Minister of Citizenship and Immigration) v. Vavilov*.⁴ Justice Régimbald emphasized that the Supreme Court expects reviewing courts to “develop and strengthen a culture of justification”.⁵



In conducting a “reasonableness review,” the Court explained that it must determine whether the decision is based on an “internally coherent and rational chain of analysis that can be justified in light of the legal and factual constraints to which the decision maker is subjected”.⁶ Further, the Court noted that it should not impose its own standards for assessing the decision, emphasizing that deference is required as long as the decision maker’s “interpretation of the law is reasonable, and the reasons are justifiable, coherent, and intelligible”.⁷

Significantly, Justice Régimbald highlighted,

“the more serious the impact of the decision on the rights and interests of a party, the more the reasons must reflect these issues, be sufficient for the parties, and ‘the decision maker must explain why its decision best reflects the legislature’s intention’”.⁸

Additionally, the Court stressed that when interpreting a statute or exercising discretion, a decision maker must consider the potential “harsh consequences” for those affected. When dealing with particularly severe or harsh consequences, the decision maker must “explain why [their] decision best reflects the legislature’s intention”.⁹

The Agency’s Analysis

The Federal Court summarized the Agency’s interpretations and reasons for not granting relief as follows:

In both decisions, the CRA opined that a harmonious interpretation of subsection [220\(2.1\)](#) and subsection [220\(3\)](#), considered in the context of the scheme set out under section 220 of the ITA as a whole, indicated that the Minister did not have discretion to waive the filing of the Election under subsection [220\(2.1\)](#), nor to accept a new return under subsection [220\(3\)](#) of the ITA. The CRA held that the implied exclusion rule applied, and the existence of ministerial discretion in this case would conflict with subsection [220\(3.2\)](#) of the ITA and section 600 of the Regulations, which set out a closed list of circumstances when a late election is acceptable, and prescribe a penalty in those cases under subsection [220\(3.5\)](#).¹⁰

Justice Régimbald noted that the Agency’s decision reflected one plausible interpretation.¹¹

Further, the Agency offered several alternative arguments that the Court dismissed, including that the Minister did not have the power to waive the election because the election in question originated from Bill C-43, not from the ITA itself, and that the discretion did not extend to allow a late filing of the election under Bill C-43.



The Court's Analysis

The Federal Court found that the Agency's decision-making process was incomplete, lacking a thorough consideration of all relevant interpretive possibilities. The Court highlighted several critical points in its analysis:

1. subsections [220\(2.1\)](#) and [220\(3\)](#) were enacted to “correct injustice” and “must be given a wide and liberal construction so as to enable [them] to effectively serve this remedial purpose”;
2. a remedial interpretation of subsections [220\(2.1\)](#) and [220\(3\)](#) of the ITA, if it exists, could potentially afford a “broad application” to allow it “to blunt the harsh effects of strict filing requirements”;¹² and
3. an interpretation allowing the harmonious and complimentary application of both subsections [220\(2.1\)](#) and (3), and subsection [220\(3.2\)](#) together with the scheme of section 220 as a whole, may be plausible.¹³

The Federal Court concluded that it is not for this Court to determine which of the plausible interpretations is more appropriate – that responsibility rests with the Minister.¹⁴

Calling for a “culture of justification,” Justice Régimbald criticized the Agency's failure to consider the Federal Court's more taxpayer-favourable interpretation. The Court found that the Agency did not adequately justify why a more restrictive interpretation was chosen. This lack of justification led the Court to lose confidence in the Agency's decision.¹⁵ And as a result, the Court overturned the Agency's decision.

Strategic Insights for Taxpayers

The Federal Court's decision places a necessary and significant burden on the Agency, requiring it to seriously consider less restrictive interpretations of tax acts when exercising its discretion. This ruling makes the reasonableness standard explicit and challenges the Agency to align its decision-making process with a more balanced and fair interpretation of the law.

This decision is a critical measure against the “harsh consequences” often associated with the Agency's decisions. Although Justice Régimbald did not explicitly define a harsh consequence, his decision opens the door for future challenges that may draw sharper distinctions. Therefore, taxpayers and their counsel must strategically align their circumstances with those in *Onex* to effectively leverage this precedent.

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We anticipate this decision will compel the Agency to reevaluate its current practices. The Agency will likely need to adjust its interpretation methodologies to withstand increased judicial scrutiny.

Taxpayers anticipating the Agency’s interpretation of legislation as part of its discretionary powers should actively invoke the Federal Court’s guidance. The Court’s reasoning underscores the necessity of a “reasonable decision” that aligns with the legislature’s intent and demonstrates why the chosen interpretation prevails over others. This shift in judicial expectations gives taxpayers a more robust platform to contest Agency decisions that appear overly restrictive or unbalanced.

Moreover, the decision could cast doubt on longstanding Agency positions that have, until now, gone unchallenged. If the Agency fails to address alternative, less restrictive interpretations in its ongoing practices, those “legacy” positions may now be subject to legal challenges. This potential vulnerability in the Agency’s approach presents an opportunity for taxpayers to reassess and possibly challenge the Agency’s interpretations that no longer hold up under this new judicial lens.

Given the profound implications of the Federal Court’s ruling in *Onex*, we strongly recommend that advisors and taxpayers consult with counsel to explore how this precedent might influence current and future disputes. The ruling provides a powerful tool for those seeking to challenge the Agency’s discretionary decisions.

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¹ *Onex Corporation v. Canada (Attorney General)*, 2024 FC 1247.

² *Onex*, at paragraph 46.

³ *Economic Action Plan 2014 Act, No 2* SC 2014, c 39.

⁴ *Onex*, at paragraph 36.

⁵ *Onex*, at paragraph 37.

⁶ *Onex*, at paragraph 41.

⁵ *Onex*, at paragraphs 42 and 43.

⁸ *Onex*, at paragraph 46.

⁹ *Onex*, at paragraph 54.

¹⁰ *Onex*, at paragraph 48.

¹¹ *Onex*, at paragraph 49.

¹² *Onex*, at paragraph 64.

¹³ *Onex*, at paragraph 66.

¹⁴ *Onex*, at paragraph 121.

¹⁵ *Onex*, at paragraphs 92, 105, 121, 144.

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