Date: 20080213

Docket: A-437-06

Citation: 2008 FCA 59

CORAM: **NADON J.A.**
SEXTON J.A.
RYER J.A.

BETWEEN:

BRUNO HARTRELL

Appellant

and

HER MAJESTY THE QUEEN

Respondent

Heard at Toronto, Ontario, on February 13, 2008.

Judgment delivered from the Bench at Toronto, Ontario, on February 13, 2008.

REASONS FOR JUDGMENT OF THE COURT BY: RYER J.A.

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REASONS FOR JUDGMENT OF THE COURT
(Delivered from the Bench at Toronto, Ontario, on February 13, 2008)

RYER J.A.

[1] This is an appeal from a decision of Paris J. of the Tax Court of Canada (the "TCC") (2006 TCC 480) dismissing the appeal of Mr. Bruno Hartrell against an income tax assessment, pursuant to subsection 227.1(1) of the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) (the "ITA"), in relation to his 1998 taxation year. The assessment arose out of the failure of Toronto Lynx Soccer Club Inc. ("LYNX") to remit source deductions, in the amount of $47,434.46, to the Canada Revenue Agency (the "CRA") in 1998, as required by section 153 of the ITA.

[2] The appellant argues that the TCC erred in upholding the assessment against him on the basis that subsection 227.1(1) of the ITA was not applicable to him because he was never formally appointed, and did not, in fact, function as a director of LYNX in 1998. In the alternative, the appellant argues that if he did function as a director in 1998, he was entitled to rely on the due diligence defence under subsection 227.1(3) of the ITA.

[3] The determinations of the TCC as to whether Mr. Hartrell was liable, pursuant to subsection 227.1(1) of the ITA, for the 1998 source deductions that LYNX failed to remit, on the basis that he, in fact, functioned as a director of LYNX and whether the due diligence defence that is contained in subsection 227.1(3) of the ITA, has been established require the application of a legal standard to a set of facts. Accordingly, these determinations constitute questions of mixed fact and law that are reviewable on a standard of palpable and overriding error, unless it is clear that there has been an extricable error of law, in which event a standard of correctness will apply. (See *Housen v. Nikolaisen*, [2002] 2 S.C.R. 235.)

[4] The TCC determined that in accordance with the decision in this Court in *Wheeliker v. R.*, [1999] 2 C.T.C. 395 (F.C.A.), a person who was not formally appointed as a director can nonetheless have liability pursuant to subsection 227.1(1) of the ITA if that person has, in fact, functioned as a director of the corporation in question.

[5] We are of the view that in making this determination on the basis of *Wheeliker*, the TCC correctly apprehended the proper legal standard with respect to the issue of whether liability under subsection 227.1(1) of the ITA can be assessed against a person who has not formally been appointed as a director.

[6] The TCC reviewed the evidence of several witnesses, including Mr. Hartrell, and numerous documents. Based upon that review, the TCC concluded that Mr. Hartrell had played a significant role in the affairs of LYNX and that the Minister's assumption that Mr. Hartrell performed the function of a director of LYNX had not been shown to be incorrect. In so finding, the TCC declined to accept Mr. Hartrell's assertion that he was no more than a passive investor in LYNX.

[7] We are of the view that the evidence before the TCC was sufficient to enable the TCC to conclude that Mr. Hartrell had, in fact, functioned as a director of LYNX in 1998. Moreover, it was open to the TCC to decline to accept Mr. Hartrell's testimony to the effect that he was a mere passive investor in LYNX. Accordingly, we are unpersuaded that the TCC committed any palpable and overriding error in reaching its conclusion that Mr. Hartrell was subject to liability under subsection 227.1(1) of the ITA on the basis that he, in fact, functioned as a director of LYNX in 1998.

[8] Pursuant to subsection 227.1(3) of the ITA, liability in respect of a failure to remit source deductions will not be imposed on a person who has, in fact, functioned as a director, if that person

has exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances.

[9] The TCC determined that the legal test with respect to the defence of due diligence under subsection 227.1(3) of the ITA was to be interpreted in accordance with paragraph 30 of the decision of this Court in *Soper v. R.*, [1997] 3 C.T.C. 242 (F.C.A.) which the TCC reproduced in paragraph 37 of its reasons. That paragraph reads as follows:

> The standard of care set out in subsection 227.1(3) of the *Act* is, therefore, not purely objective. Nor is it purely subjective. It is not enough for a director to say he or she did his or her best, for that is an invocation of the purely subjective standard. Equally clear is that honesty is not enough. However, the standard is not a professional one. Nor is it the negligence law standard that governs these cases. Rather, the *Act* contains both objective elements embodied in the reasonable person language – and subjective elements inherent in individual considerations like "skill" and the idea of "comparable circumstances" Accordingly, the standard can be properly described as "objective subjective".

[10] The principles with respect to the test for the due diligence defence in subsection 227.1(3) of the ITA that were laid down in *Soper* have been affirmed by this Court in *Worrell v. R.*, [2000] 1 C.T.C. 79 (F.C.A.).

[11] The appellant submits that the TCC erred by not adopting the test in *Worrell*. We are of the view that this argument must fail. By adopting the test in *Soper*, which was approved in *Worrell*, the TCC has adopted the test that the appellant advocates. We agree with the respondent that the TCC did not adopt the decision in *Thibeault v. The Queen*, 2005 TCC 393, [2006] G.S.T.C. 165, with

respect to the test for the due diligence defence, and that by its reliance on *Soper*, the TCC adopted the proper legal test with respect to the due diligence defence under subsection 227.1(3) of the ITA.

[12] The appellant argued that the decision of the Supreme Court of Canada in *Peoples Department Stores Inc. (Trustees of)* v. *Wise* 2004 SCC 68 changed the test with respect to the due diligence defence from the "objective subjective" test, in *Soper*, to simply an "objective" test. Whether *Peoples Department Stores* can be said to have eliminated the subjective aspects of the due diligence defence in subsection 227.1(3) of the ITA is not entirely clear since that the decision dealt with a provision of the *Canada Business Corporation Act* R.S.C. 1985, c. B-3. In that regard, the Supreme Court of Canada, in paragraph 63 of the decision, stated that:

> With respect, we feel that Robertson J.A.'s characterization of the standard as an "objective subjective" one could lead to confusion. We prefer to describe it as an objective standard. To say that the standard is objective makes it clear that the factual aspects of the circumstances surrounding the actions of the director or of the officer are important in the case of the s.122(1)(b) duty of care, as opposed to the subjective motivation of the director or officer, which is the central focus of the statutory fiduciary duty of s.122(1)(a) of the CBCA.

If *Peoples Department Stores* did change the test to be applied under subsection 227.1(3) of the ITA to one that requires due diligence to be demonstrated on a purely objective standard, such a new test would be more difficult to meet than a test that contains some elements of subjectivity. As such, we are unable to see how the potential application of *Peoples Department Stores* could be helpful to the appellant.

[13] The TCC found that Mr. Hartrell, an experienced chartered accountant, was aware that LYNX had failed to remit the correct amount of source deductions in a number of months in 1998

and that he did nothing to prevent those failures. The TCC based this finding on the evidence before it, in particular Mr. Hartrell's testimony, as well as correspondence between Mr. Hartrell and Mr. Iantorno, the president of LYNX. The TCC rejected Mr. Hartrell's argument that because he caused LYNX to provide post-dated cheques to the CRA in 1999, after the deficiencies had arisen, he had taken reasonable efforts to prevent the deficient remittances that arose in 1998. The TCC held that these cheques were provided long after the deficient remittances had occurred and that the due diligence defence requires steps to be taken to prevent such occurrences. Moreover, the TCC found that Mr. Hartrell could have caused LYNX to pay the arrears out of the funding that was provided to LYNX between January and August of 1999.

[14] Based upon the evidence before the TCC, we are of the view that it was open to the TCC to make these factual findings. Accordingly, we are not persuaded that the TCC made any palpable and overriding error in applying due diligence defence in *Soper* to these factual findings and in reaching the conclusion that Mr. Hartrell had failed to exercise the degree of care, diligence and skill that a reasonably prudent person would have exercised in comparable circumstances to prevent the source deduction remittance shortfalls that occurred in 1998.

[15] For these reasons, the appeal will be dismissed with costs.

"C. Michael Ryer"

J.A.

FEDERAL COURT OF APPEAL

NAMES OF COUNSEL AND SOLICITORS OF RECORD

DOCKET:	A-437-06
(APPEAL FROM A JUDGMENT OF THE TAX COURT OF CANADA, DATED SEPTEMBER 11, 2006, FROM THE HONOURABLE MR. JUSTICE PARIS – TCC NO. 2002-281 (IT) G.)	
STYLE OF CAUSE:	BRUNO HARTRELL v. HER MAJESTY THE QUEEN
PLACE OF HEARING:	TORONTO, ONTARIO
DATE OF HEARING:	FEBRUARY 13, 2008
REASONS FOR JUDGMENT OF THE COURT BY:	(NADON, SEXTON, RYER JJ.A.)
DELIVERED FROM THE BENCH BY:	RYER J.A.

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