Docket: 2004-4446(IT)G

BETWEEN:

HERITAGE EDUCATION FUNDS INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on November 25 and 26, 2009, at Toronto, Ontario.
Before: The Honourable Justice Lucie Lamarre

Appearances:

Counsel for the Appellant:	William I. Innes Angelo Gentile
Counsel for the Respondent:	Eric Noble Bobby Sood

AMENDED JUDGMENT

The appeal against the reassessment dated August 27, 2004, in respect of the appellant's 1999 taxation year, made by the Minister of National Revenue (**Minister**) under the *Income Tax Act*, is allowed and the reassessment is referred back to the Minister for reconsideration and reassessment on the basis that the revised taxable income of $13,305,885 is not representative of the appellant's profit for that year. The net income of $2,009,856 reported by the appellant shall be restored with the addition, however, of an amount of $104,593 representing convention expenses that were disallowed and whose disallowance was not challenged by the appellant in this appeal. The deduction of $3,076 for charitable donations allowed by the Minister in the above-mentioned reassessment is also maintained.

The additional permissive deductions, being the increased deduction in respect of prior years' losses carried forward and the increased capital cost allowance granted by the Minister in order to reduce the overall tax liability

resulting from the reassessment under appeal (as referred to in paragraph 5 of the Notice of Appeal), shall be reversed as requested in subparagraph 36(b) of the Notice of Appeal.

At the request of the parties, representations on costs shall be made to the Court either in writing or orally, as the parties wish, within 30 days of the date of the **amended** judgment.

Signed at Ottawa, Canada, this **16th** day of **April** 2010.

"Lucie Lamarre"

Lamarre J.

Citation: 2010 TCC 161
Date: 2010**0416**
Docket: 2004-4446(IT)G

BETWEEN:

HERITAGE EDUCATION FUNDS INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

AMENDED REASONS FOR JUDGMENT

Lamarre J.

[1] This is an appeal against a reassessment made by the Minister of National Revenue (**Minister**) for the appellant's 1999 taxation year. In reassessing, the Minister adjusted the appellant's income by the addition of $11,842,789 in respect of an "enrolment fees deduction disallowed" and the deduction of $651,353 in respect of "reserves for doubtful debts allowed".

[2] The appellant, Heritage Education Funds Inc. (formerly known as Allianz Education Funds Inc. and, prior to that, as Canadian American Financial Corp. (Canada) Limited (**CAFC**)) carried on business in Canada distributing units of the Heritage Scholarship Trust Plan (**Plan**), a savings plan that qualifies as a registered education savings plan (**RESP**) under the *Income Tax Act* (**ITA**). In its return of income for the 1999 taxation year, the appellant reported net income of $2,009,856. In computing its income from its business, the appellant excluded enrolment fees earned but not received by it as at its December 31 year end ($11,842,789). The appellant had been reporting its enrolment fees in this manner for a number of years prior to 1999. As a result, the closing receivables balance at the end of 1998, i.e. all enrolment fees from sales made in 1998 and before (the 1998 enrolment fees receivable), was included in income for 1999. The 1998 enrolment fees receivable amount added to the appellant's income for 1999 was $13,442,628 (see Exhibit A-3).

[3] In adjusting the appellant's 1999 net income, the Minister included the enrolment fees earned but not received for 1999 ($11,842,789) without adjusting or reducing that net income through the exclusion of the amount of $13,442,628 that was included in income by the appellant in 1999 but which had been earned in 1998 and prior years. As a result, the Minister increased the appellant's net income for 1999 from $2,009,856 to $13,305,885 (Exhibit A-3).

[4] In its financial statements, the appellant reported income for 1999 of $225,731, which income was computed on an accrual basis and included the 1999 enrolment fees receivable of $11,842,789, but not the 1998 enrolment fees receivable of $13,442,628.

[5] In the introduction to its Notice of Appeal, the appellant states that the sole issue in this appeal is whether the enrolment fees in question ($11,842,789) were required to be included in computing the income of the appellant for its 1999 taxation year. Under the heading "Issues to Be Decided", the appellant states the issue as follows: "Was the Membership [Enrolment] Fee Revenue based on Possible Future Deposits [deposits which had not been made by Plan Members as at December 31, 1999] required to be included in computing the income of the appellant in its 1999 taxation year?"

[6] In its pleading, the appellant answered this question in the negative, basing its contention on the fact that the appellant had no legal entitlement to enrolment fees based on such possible future deposits unless and until such deposits were in fact made by the plan members. The appellant relied on sections 9 and 12 of the ITA.

[7] In the Amended Reply, the respondent states the issue as being whether the enrolment fees receivable were properly included in computing the appellant's income. The respondent answered that question in the affirmative and submitted that the inclusion of the enrolment fees receivable in computing the appellant's income is consistent with generally accepted accounting principles (**GAAP**) and provides a more accurate picture of the appellant's income.

Facts

[8] The Plan was established by the Heritage Scholarship Trust Foundation (the **Foundation**), a non-profit corporation without share capital incorporated under the

laws of Canada. The Foundation was responsible for the administration of the Plan with respect to which the appellant provided services to the Foundation. Those services included the distribution of units of the Plan, pursuant to the terms of a Franchise Agreement, which provided for the payment of enrolment (membership) fees to the appellant.

[9] Persons who purchased units in the Plan (called "Members" or "Subscribers") agreed to be bound by the terms of a Scholarship Agreement entered into with the Foundation. That Scholarship Agreement had to be filed along with a prospectus in accordance with provincial securities law, more precisely in accordance with National Policy Statement 15 (**National Policy 15**) (Exhibit A-1, Tab 1). The prospectus (which had to clearly indicate the speculative nature of the scholarship plan and the real cost of participation in the plan to the subscriber) was part of the Scholarship Agreement. The 1998 and 1999 prospectuses provided that a member had to subscribe for a minimum of two units in the Plan and agree to make predetermined deposits with the depository [the bank responsible for receiving deposits]. It also provided that a membership (enrolment) fee of $100 per unit together with certain other amounts was to be deducted from the deposits to cover the costs of administering the Plan. More particularly, the prospectus indicate the following:

> **Membership Fee and other deductions**
>
> The Agreement authorizes the Depository to deduct the following amounts from the Deposit and/or Savings as applicable:
>
> (a) A fee (the "Membership Fee[1]") of $100.00 per Unit is payable to the Distributor [Appellant] as follows:
>
> (i) the first $50 per Unit deposited; and
> (ii) the remainder of the Membership Fee is paid by the deduction of 50% of subsequent Deposits until the total Membership Fee is paid.
>
> (b) An annual depository fee per Agreement (the “Depository Fee”[2]) of:
>
> (i) Single Deposit Method - $3.50 plus GST
> (ii) Annual Deposit Method -$6.50 plus GST
> (iii) Monthly Deposit Method - $9.50 plus GST

[1] "Membership Fee" means the $100 per Unit fee deducted from Deposits by the Depository.
[2] “Depository Fee” means the annual depository fee paid to the Foundation to reimburse it for its expenses.

(See 1998 Prospectus, Exhibit A-1, Tab 2, page 9 and 1999 Prospectus, Exhibit A-1, Tab 3, page 10.)

[10] In the Scholarship Agreements, paragraph 2(a) states the following:

> **2. Deposits**
>
> (a) the Member, by executing the [Scholarship] Application agrees:
>
> (i) to enrol in the Plan;
> (ii) to make deposits with the Depository ("Deposits") to the account maintained by the Depository in accordance with the Deposit method identified on the Application; and
> (iii) to subscribe for the number of Units in the Plan identified in the Application.
>
> (b) The Member authorizes the Depository and the Depository Trustee to deduct the following from Deposits or Savings, as applicable;
>
> (i) the first $50 of Deposits for each Unit and 50% of the subsequent Deposits until a Membership Fee of $100 per Unit is paid;
> (ii) the Depository fee, as outlined in the Prospectus;
> (iii) group insurance premiums, if applicable
> (iv) an annual operating fee to constitute the operating account used to pay future expenses of administration of the Foundation. The annual amount is ½ of 1% of principal and interest on deposit, calculated annually and deducted monthly from interest; and
> (v) additional individual charges for any special services requested by a Member, as outlined in the Prospectus.

[See Exhibit A-1, Tabs 4 and 5.]

[11] Mr. Onofrio Loduca, the chief financial officer of the appellant testified at the hearing. He said that, in fact, members had various options with respect to making deposits; they could be made, in one payment or in monthly or annual payments, as set out in a contribution schedule. Payments were thus made over a period of up to 3 years typically, depending on the age of the child and how fast the member wanted to accumulate interest in the Plan (Transcript, pages 91 and 92).

[12] The prospectus and the Scholarship Agreement also provided that a member could withdraw from the Plan at any time during the 60-day period following the later of the date on which the application was signed by the member and the date of

the initial deposit under the agreement upon giving written notice, which had to be received by the Foundation's head office within those 60 days. Upon such withdrawal, all deposits made by the member were returned to the member, except for insurance premiums and any interest earned on the deposits. Membership fees had to be returned to the member.

[13] After the 60-day period referred to above, a member could still terminate his or her interest in the Plan. Upon such withdrawal, all deposits were to be returned to the member less the deductions made therefrom, including the membership fees, which were not returned to the member (see 1998 Prospectus, Exhibit A-1, Tab 2, pages 9-10; 1999 Prospectus, Exhibit A-1, Tab 3, page 2; 1998 Scholarship Agreement, Exhibit A-1, Tab 4, paragraphs 5(a) and (b); 1999 Scholarship Agreement, Exhibit A-1, Tab 5, paragraphs 5(a) and (b)).

[14] Furthermore, in the event that a member failed to make a deposit when required, the Foundation would provide notice to the member of such failure, normally within 30 days. Failure by the member to remit the required deposit within 60 days following such notice would result in the termination of the member's interest in the Plan, in which case the member could either elect within a three-year period to have his or her interest in the Plan reinstated, or require the return of all savings, without interest, less deductions already made (including the membership fees). Upon failure by the member to make any election within the three-year period, the savings would be transferred into the Enhancement Fund (a fund consisting of the interest accruing on funds in the Scholarship Fund) (see 1998 and 1999 prospectuses, Exhibit A-1 Tab 2, page 10, and Tab 3, page 11; 1998 and 1999 Scholarship Agreements, Exhibit A-1, Tab 4, section 1 and paragraph 5 (c), and Tab 5, paragraph 5(c)).

[15] Mr. Loduca explained that the deposit schedule agreed upon by a member had to be adhered to by the member or his assignee in the event of the disability or the death of the member (paragraph 4(a) of the Scholarship Agreements, Exhibit A-1, Tabs 4 and 5), in order to get full value back for the nominee upon the maturity of the Plan (see Transcript, pages 129-130).

[16] Ms. Doreen Johnston, who, as vice-president of administration and a director of the appellant during the taxation year in question supervised the scholarship committee, also testified. She explained that the deposit schedule set out due dates for contributions, since all plans are designed to earn approximately the same amount of interest by their maturity date. The predetermined schedule is in effect a forced savings program for people who want to stay in the Plan, but there is no obligation to

make contributions if, for any reason, someone wishes to withdraw from the Plan (See Transcript, pages 160-161.)

[17] The Franchise Agreement entered into between the Foundation and the appellant (see Exhibit A-1, Tab 6), provided as follows with respect to the enrolment (membership) fees:

> Rescission Right
>
> 6. If any subscriber to a scholarship agreement requests that the Foundation terminate the agreement within 60 days after the Acceptance of a scholarship agreement, then notwithstanding that the agreement may have been executed by the Foundation, the Foundation shall have the right to terminate the agreement and to cause to be returned to the subscriber all funds deposited with the Depository in respect of that agreement. If the Foundation exercises this right, then CAFC shall not be entitled to any payment whatsoever in respect to the agreement and shall repay to the Foundation all funds received by it in respect to the agreement, failing which the Foundation may deduct the amount of these funds from other payments due from it to CAFC.
>
> . . .
>
> Foundation Payments to CAFC
>
> 8. (a) The Foundation shall pay to CAFC an amount equal to the enrolment fees in respect of all scholarship agreements sold by CAFC, as they fall due.
>
> . . .

[18] Mr. Loduca explained that from a financial accounting perspective, the appellant included the $100 membership (enrolment) fee in income immediately while for income tax purposes it only included in income those fees it collected from members' deposits as they were made by the members. The appellant took the approach that it did not have legal entitlement to the membership fees until the deposits were actually made by the members.

[19] Mr. Loduca explained that they took that approach because of the wording of paragraph 8(a) of the Franchise Agreement, which says that the enrolment fees are to be paid to the appellant "as they fall due", meaning when the deposits were received by the Foundation (Transcript, p. 36). In cross-examination Mr. Loduca said that the appellant interpreted "as they fall due" thus:

> as the Foundation is able to receive those deposits [from the Members] and membership fees and enrolment fees are withdrawn from those deposits, that they are in a position to pass on those fees to the distributor. [transcript page 82.]

[20] Ms. Johnston also testified that the Foundation's right to receive membership fees only arose when a contract was signed or on the date of the cheque, whichever was more recent. She then elaborated by stating that the membership fee could only be deducted from deposits, that until there were deposits no membership fees were paid and that there was no way to compel a member to make a deposit. (Transcript, pages 169 and 173).

[21] She interpreted "as they fall due" as meaning that the payment to the appellant would not be made until deposits were made and the membership fees deducted therefrom. She said that if there were no deposits there were no enrolment fees and that the appellant could not enforce payment because the regulations under which the Foundation and the appellant operated only permitted the collection of fees if deposits were made. (Transcript, pages 177 and 178.)

[22] As a matter of fact, the appellant never invoiced the Foundation and it never asked the Foundation to pay funds or monies that had not been received from the members. Mr. Loduca did acknowledge, however, that once a member's application and Scholarship Agreement was accepted by the Foundation, this automatically triggered the appellant's right to receive the $100 commission amount (Transcript, page 86). In the notes to the appellant's financial statements for the year ended December 31, 1999, it is stated (at Note 1.(b)) that membership fees are earned by the appellant as remuneration for its services in distributing the Plan. These fees are recorded at the time of sale and are collected as deposits are made under the Plan (Exhibit A-1, Tab 7, page 4).

[23] In fact, for the purpose of reporting in its financial statements, the appellant kept a running tally throughout the year of each unit sold and each sale accepted by the Foundation. For accounting purposes, such as in the preparation of financial statements, a predictive model was used in which the probability of receiving enrolment fees over time was taken into account in the computation of income (enrolment fees receivable also being treated as assets - Exhibit A-1, Tab 7, balance sheet, page 1), and adjustments were made through an allowance or a reserve for fees that would not be collected over time (statement of retained earnings in the financial statements, Exhibit A-1, Tab 7, page 2; Transcript, pages 9-10, 100 and 101). The historical average receivables becoming uncollectible was 5½ per cent (Transcript, page 99).

[24] For tax purposes, in a case where the appellant had to reimburse a membership fee to a member who elected to withdraw from the Plan in the first 60 days, the appellant would report that membership fee as having been received and make a deduction of the same amount when it returned the money to the member. There was no contingent deduction made for tax purposes (Transcript, pages 26-27).

[25] Mr. Kenneth Daniel Devine, who was the tax director for Allianz Life Insurance Co. and an officer of the appellant, also testified. He said that he reviewed the appellant's tax returns. His testimony did not add much to the other witnesses' testimony. He acknowledged that the Franchise Agreement between the Foundation and the appellant was intended to be a legally enforceable agreement but stated that the appellant did not have entitlement to the commissions when the units were sold. They were recorded as "cash received" (Transcript, pages. 212 and 213).

[26] Furthermore, Mr. Loduca acknowledged that expenses incurred by the appellant in connection with the sale of the units sold in 1999 (Exhibit R-2) were deducted in the computation of income for tax purposes. Approximately $15 or $16 million out of $18 million in salaries and commissions was related to commissions paid to salespersons on sales made in 1999 (Transcript, page 108).

[27] The evidence also revealed that the appellant entered into factoring agreements with its affiliated US parent company, selling its accounts receivable (including the enrolment fee receivable) to finance its operations. The parent company looked at the probability of collecting these receivables in the future and discounted the purchase price by an interest rate charge that included the risk in that regard (Transcript, pages 43, 122 and 123). The discount rate was determined after taking into account the appellant's historical doubtful debt experience, the historical average collection period for membership fee receivables and the bank prime rate on the date of the transaction (see note 4 to the financial statements, Exhibit A-1, Tab 7, page 7).

[28] Under the documents entitled Agreements – Sale of Accounts (the Factoring Agreements) filed as Exhibit R-2, Tabs 4 and 5, the appellant sold to Allianz Life (its parent company) present and future enrolment fees earned and to be earned by the appellant through the sale of scholarship plans in the regular course of its business, and Allianz Life was then to have the full risk and obligation with respect to the collection of those fees. Mr. Loduca explained that the appellant was passing the risk on to its parent company, ant that this risk was factored into the discount rate at an estimated rate, which meant that the risk could actually be greater or lower (Transcript, pages 120-121). Mr. Loduca stated that in case of non-payment of the

receivables, Allianz Life could not collect any money from the Foundation because the Foundation, being a not-for-profit incorporated entity, had neither money nor assets (Transcript, pages 125, 140).

[29] Counsel for the appellant read into evidence excerpts from the transcript of the examination for discovery of Ms. Vanda Yantsis, an appeals officer with the Canada Revenue Agency (**CRA**). She had testified at discovery that at the time she confirmed the reassessment at issue she was of the view that the appellant did not have a legal right to enforce payment. The respondent has since changed her mind and is of the view that although the appellant did not have a legal right to sue the members, it did have a legal right under the Franchise Agreement to enforce payment of any amounts owing to it by the Foundation under the terms of that agreement (Transcript, pp. 253 to 257).

Statutory Provisions

[30] ITA

SECTION 9

(1) Income. Subject to this Part, a taxpayer's income for a taxation year from a business or property is the taxpayer's profit from that business or property for the year.

SECTION 12

(1) Income inclusions. There shall be included in computing the income of a taxpayer for a taxation year as income from a business or property such of the following amounts as are applicable:

. . .

(1)(b) Amounts receivable - any amount receivable by the taxpayer in respect of property sold or services rendered in the course of a business in the year, notwithstanding that the amount or any part thereof is not due until a subsequent year, unless the method adopted by the taxpayer for computing income from the business and accepted for the purpose of this Part does not require the taxpayer to include any amount receivable in computing the taxpayer's income for a taxation year unless it has been received in the year, and for the purposes of this paragraph, an amount shall be deemed to have become receivable in respect of services rendered in the course of a business on the day that is the earlier of

(i) the day on which the account in respect of the services was rendered, and

(ii) the day on which the account in respect of those services would have been rendered had there been no undue delay in rendering the account in respect of the services.

Appellant's Submissions

[31] It was the appellant's submission that it did not have a clear legal and unconditional right to collect or receive the enrolment fees. According to the appellant, the right to those fees was dependent entirely on the occurrence of an uncertain event outside its control, i.e. the right to receive those fees was based entirely on the unilateral decision of members to continue making deposits. Counsel for the appellant referred to the case of *M.N.R. v. John Colford Contracting Co.* 60 DTC 1131, (1960), 26 D.L.R. (2d) 15 (Ex. Ct. of Canada) in which Kearney J. interpreted the expression "amount receivable" as follows at pages 1134 and 1135 DTC:

> As "amount receivable" or "receivable" is not defined in the Act, I think one should endeavour to find its ordinary meaning in the field in which it is employed. If recourse is had to a dictionary meaning, we find in the *Shorter Oxford*, Third Edition, the word "receivable" defined as something "capable of being received." This definition is so wide that it contributes little towards a solution. It envisages a receivable as anything that can he transmitted to anyone capable to receiving it. It might be said to apply to a legacy bestowed in the will of a living testator, but nobody would regard such a legacy as an amount receivable in the hands of a potential legatee. In the absence of a statutory definition to the contrary, I think it is not enough that the so-called recipient have a precarious right to receive the amount in question, but he must have a clearly legal, though not necessarily immediate, right to receive it. A second meaning, as mentioned by Cameron J., is "to be received," and Eric L. Kohler, in *A Dictionary for Accountants*, 1957 edition, p. 408, defines it as "collectible, whether or not due." These two definitions, I think, connote entitlement.
>
> This leads to a consideration of whether, legally speaking, each of the holdbacks in the instant case possessed the quality required to bring it within the meaning of a receivable. Speaking of the quality required to constitute income, the learned president of this Court stated in *Robertson Ltd. v. Minister of National Revenue*, [1944] Ex. C.R. 170,182 [2 DTC 655, 660]:
>
> Did such amounts have, at the time of their receipt, or acquire, during the year of their receipt, the quality of income, to use the phrase of Mr. Justice Brandeis in *Brown v. Helvering*, (1934) 291 U.S. 193. In my judgment, the language used by him, to which I have already referred, lays down an important test as to whether an amount received by a taxpayer has the quality of income. Is his right to it absolute and under no restriction, contractual or otherwise, as to its disposition, use or enjoyment? To put it in another way, can an amount in a taxpayer's hands be regarded as an item of profit or gain from his business, as long as he holds it subject

> to specific and unfulfilled conditions and his right to retain it and apply it to his own use has not yet accrued, and may never accrue?

[32] The test in *Colford* was adopted by the majority in the Supreme Court of Canada in *Maple Leaf Mills Limited v. The Minister of National Revenue*, 76 DTC 6182. The majority stated the following at page 6186:

> . . . The right to receive this third element so as to reach the plateau of the guaranteed minimum income never was a precarious one. At all material times appellant had a clearly legal right to receive all the benefits that together would bring its income to the guaranteed minimum. There is also no doubt that the right of appellant to the amount of the debt resulting from the deficiency in any given year was held by it unconditionally. That amount was bound to accrue though not necessarily immediately. I accept without question the test expressed by Kearney J. in *The Minister of National Revenue v. John Colford Contracting Company Limited* [60 DTC 1131] (1960) Ex. C.R. 433, at pages 440 and 441. An appeal to this Court from this judgment was dismissed without written reasons [62 DTC 1338] (1962) S.C.R. viii.

[33] Applying this test to the facts of this appeal, the appellant argued that it did not have a clear legal and unconditional right to the unpaid enrolment fee revenue from possible future deposits. According to the appellant, any rights it may have had were precarious and the fees cannot be construed as being unconditionally "collectible", as having been "received" or as being "bound to accrue". It argued that its entitlement to receive and enforce payment of enrolment fees only arose when a deposit was actually made by a member. The appellant relied on National Policy 15, paragraphs 7, 9 and 10, which set out the right of members to withdraw or to cease making deposits at any time, without incurring future obligations. The appellant further relied on the express terms of the prospectus and the Scholarship Agreements, which had to be in accordance with National Policy 15. It relied as well on what it termed the only reasonable interpretation of the Franchise Agreement and on the evidence given by Doreen Johnston and Onofrio Loduca. As a result, the appellant contended, the enrolment fees relating to possible future deposits were not receivable under paragraph 12(1)(b) of the ITA and should not be included in the appellant's income for 1999. Indeed, according to the appellant, an amount which it had no clear and unconditional right to collect or receive did not need to be included in its income when the entitlement to that amount was entirely dependent upon outside parties, i.e. the members, who were at complete liberty to make or not make future deposits.

[34] Furthermore, the appellant argued, the Minister's reporting method resulted in a grossly inaccurate picture of its income for its 1999 taxation year insofar as it failed to exclude enrolment fees relating to plans sold in 1998 and prior taxation years.

Respondent's submissions

[35] The respondent submitted that $11.8 million in uncollected commissions was receivable in 1999 even though payment was not due until a subsequent year; hence those commissions had to be included in income for the 1999 taxation year pursuant to paragraph 12(1)(b) of the ITA.

[36] In support of her submissions, the respondent relied mainly on the terms of the Franchise Agreement. The respondent argued that the appellant had a clear legal, though not necessarily immediate, right to receive the enrolment fees once a Scholarship Agreement had been sold, and that the Foundation incurred an obligation to pay those fees upon acceptance of a new unit sale. According to the respondent, the Foundation's obligation to pay the appellant came into existence at that time irrespective of whether payment of the fees was required immediately or in the future. That obligation to pay did not come into existence at the time the members made their deposits, as argued by the appellant. The respondent argued that her submissions are supported by the following points:

- the appellant described the enrolment fee amounts as "receivables" for accounting purposes and reported them as assets on its balance sheet;

- the appellant sold portions of the enrolment fees receivable to its parent company (Allianz). The factoring of those receivables is irreconcilable with the appellant's assertions that it had no right to the amounts unless and until deposits were made by members.

[37] According to the respondent, the appellant understood its entitlement to the full amount of its enrolment fees to arise upon making a sale of units to a member. This is reflected in the wording employed in various Factoring Agreements and in the financial statements approved by the appellant and its parent company.

[38] The preamble to the Factoring Agreements stated that the appellant was selling to its parent company accounts receivable which represented "present and future bona fide enrolment fees earned and to be earned by the appellant through the sale of scholarship plans in the regular course of its business". Paragraph 3 of the Factoring Agreements also stated that the purchase price for outstanding accounts sold to the parent was to be payable to the appellant at the end of the month in which said

accounts became a receivable through the sale of one or more scholarship plans (Exhibit R-2, Tabs 4 and 5).

[39] In the respondent's view, this wording is evidence that the sale of a scholarship plan was the event triggering the appellant's entitlement to the enrolment fees under paragraph 8(a) of the Franchise Agreement.

[40] With respect to the appellant's obligation under paragraph 6 of the Franchise Agreement, in the event of the termination of a subscriber's Scholarship Agreement within 60 days, to refund the Foundation any amounts received from the Foundation, the respondent is of the view that it is a condition subsequent (not a condition precedent), the existence of which does not detract from the status of the uncollected enrolment fees as receivables. The respondent referred to the Federal Court of Appeal decision in *Commonwealth Construction Co. v. The Queen*, 84 DTC 6420 at page 6424:

> . . . the record discloses that the rights of the Appellant to the amounts paid to it in 1974 and 1975 were "absolute and under no restriction, contractual or otherwise, as to its disposition, use or enjoyment." They were not held subject to any specific and unfulfilled conditions. Once the conditions precedent imposed in the letter agreements between the parties, *supra*, had been fulfilled, as they were, the right to receive the monies and to retain them had accrued and was absolute. True, it might be necessary to return the monies in whole or in part if the appeal were successful. But, as I see it, that was a condition subsequent which did not affect the unrestricted right of the Appellant to use them until such a requirement occurred. It did not, as I see it, affect their quality as income upon receipt.
>
> [*Condition subsequent*]
>
> As to the difference in effect of a condition precedent from a condition subsequent on the question of an accrual to income, the learned Trial Judge relied on a quotation from *Meteor Homes Ltd. v. Minister of National Revenue*, 61 DTC 1001 at 1007 & 1008 which substantiates the view which I expressed *supra*:
>
> . . . Mertens, Law of Federal Income Taxation, Vol. 2, c. 12, p. 127, considers "the problem of *when* items are . . . deductions to the taxpayer on the accrual basis", and deals with it at p. 132 in these terms:
>
> > Not every contingency prevents the accrual of income: the contingency must be real and substantial. A condition precedent to the creation of a legal right to demand payment effectively bars the accrual of income until the condition is fulfilled, but the possible occurrence of a condition *subsequent* to the creation of a liability is not grounds for postponing the accrual. (Emphasis mine)

[41] Finally, the respondent is of the view that the appellant is precluded from asking this Court to remove from income the receivables amount that it deducted in the prior taxation year and which it brought into income in the year under appeal (the amount of $13,442,628).

[42] The respondent argued that this argument should not be entertained by this Court as it was not raised by the appellant in its pleading. The respondent referred to the case of *Santoro et al. v. The Queen*, 2004 DTC 3684, 2004 TCC 764, in which Rip J., as he then was, described the function of pleadings as follows at paragraphs 43 and 44:

> [43] Messrs. Williston and Rolls[7], describe the function of pleadings as fourfold:
>
> 1. To define with clarity and precision the question in controversy between litigants.
>
> 2. To give a fair notice of the case which has to be met so that the opposing party may direct his evidence to the issues disclosed by them. A defendant is entitled to know what it is that the plaintiff asserts against him; the plaintiff is entitled to know the nature of the defence raised in answer to his claim.
>
> 3. To assist the court in its investigation of the truth of the allegations made by the litigants.
>
> 4. To constitute a record of the issues involved in the action so as to prevent future litigation upon the matter adjudicated between the parties.
>
> [44] The function of pleadings is to permit opposing parties to know what they are required to meet at trial. Each party sets out the facts of his or her case in a pleading so that their cases are well defined and the proper evidence can be led. It is not open to a trial judge to make a finding on a point not raised in the pleading and where no evidence has been particularly directed to it.

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[7] *The Law of Civil Procedure*, Butterworth & Co. (Canada) Ltd., Toronto (1970), p. 637.

[43] The respondent also invoked subsections 169(2.1) and 165(1.11) of the ITA in stating that the appellant, as a large corporation, could not amend its Notice of Appeal to seek relief that was not identified in its Notice of Objection (reference was made to the decision of the Federal Court of Appeal in *The Queen v. Potash Corp. of Saskatchewan Inc.*, 2004 DTC 6002, 2003 FCA 471).

Appellant's rebuttal

[44] With respect to this latter argument, the appellant replied that it was not raising new issues or seeking new forms of relief, that is, issues and relief not referred to in its Notice of Objection. In arguing that the Minister's method of computing income presents a grossly misleading picture since that method does not remove from the computation amounts in respect of plans sold prior to 1999, the appellant, so it contends, is responding directly to the assumptions of fact in subparagraphs 10h) and j), and to an argument put forward in paragraph 17, of the Amended Reply, which read as follows:

> 10.h) The inclusion of the Enrolment Fees Receivable in computing the Appellant's profit from its business provided an accurate picture of the Appellant's income.
>
> . . .
>
> 10.j) The exclusion of the Enrolment Fees Receivable in computing the Appellant's profit from its business provided an inaccurate picture of the Appellant's income.
>
> . . .
>
> 17. He submits that the inclusion of the Enrolment Fees Receivable in computing the Appellant's income is consistent with GAAP and provides a more accurate picture of the Appellant's income.

[45] The appellant only adduced evidence to rebut the respondent's assumptions of fact. With respect to the "large corporation rule" relied upon by the respondent, the appellant argued that this rule does not preclude a taxpayer from raising new facts or new reasons to demolish the Minister's assumptions and respond to the Minister's argument (reference was made to the decision of this Court in *British Columbia Transit v. Canada*, [2006] G.S.T.C. 103, 2006 TCC 437, in which was discussed the position adopted by the Federal Court of Appeal in the *Potash* decision, referred to by the respondent).

Analysis

I. Are the enrolment fees earned but not yet received amounts receivable to be included in income pursuant to paragraph 12(1)(b) of the ITA?

[46] As stated in *Colford*, amount receivable is not a term that is defined in the ITA. It was determined in that case that an amount will be receivable if the recipient has a clear legal, though not necessarily immediate, right to receive it.

[47] The question in *Colford* was whether the issuance of an architect's certificate constituted a condition precedent binding on the taxpayer corporation which prevented it from claiming a holdback until the certificate was issued. In Ontario, it has been held that a contractor has no legal right to the amount of a holdback until the issuance of the certificate, and that no suit can properly be commenced by the contractor before certification unless it is clear that the certificate has been improperly withheld by the architect. The Exchequer Court stated that completion of the work and acceptance by the architect were conditions precedent which had to be fulfilled before the taxpayer was entitled to payment of the holdback. As a corollary, the Court concluded that the holdback did not take on the quality of a receivable until the work had been accepted by the architect.

[48] Here, the question that must be asked is whether the appellant became entitled to the enrolment fees at the time the Scholarship Agreements were sold or only at the time the members made their deposits. Can it be said that the payment by the members of the deposits pursuant to the Scholarship Agreements constituted a condition precedent binding on the appellant which prevented it from claiming the enrolment fees until the deposits were made by the members? Did the appellant have a legal right to the enrolment fees before the payment of the deposits, and could the appellant have properly commenced a suit against the Foundation before those deposits were actually made by the members?

[49] The appellant's entitlement to receive enrolment fees in relation to the sale of Scholarship Agreements has its source in the combination of the provincial regulation (National Policy 15), the prospectus, the Scholarship Agreements entered into between the Foundation and the members, and the Franchise Agreement signed between the Foundation and the appellant. All of these documents are to be looked at as a whole, as they are interdependent and none of them would exist without the others.

[50] Hence, the Franchise Agreement exists to give the appellant the authority and exclusive right to sell Scholarship Agreements to be entered into between members and the Foundation upon acceptance of those agreements by the latter, all in accordance with a prospectus that must be in conformity with the provincial regulation.

[51] The provincial regulation (National Policy 15) requires that the prospectus filed with respect to the sale of Scholarship Agreements must draw a very clear distinction between the Foundation, which is a body without any profit motive, and the distributor, who sells the Plan under a commission arrangement (here, the appellant). National Policy 15 establishes a maximum fee (including commission) for a plan and requires that the Plan grant the subscriber the right to withdraw from the Plan without any cost to the subscriber within 60 days from the execution of the contract, and that the subscriber not be obliged to pay any fees in addition to those already paid if he or she wishes to withdraw from the Plan after that 60-day period (Exhibit A-1, Tab 1).

[52] The preamble to the Franchise Agreement (Exhibit A-1, Tab 6) states that the appellant (CAFC) "desires to assist the Foundation in promoting the objects of the Foundation by encouraging persons to enter into scholarship agreements".

[53] The Franchise Agreement goes on to state that the parties agree as follows:

Paragraph 2: "The Foundation grants to [the appellant] the exclusive worldwide right to encourage persons to enter into Scholarship Agreements with the Foundation."

Paragraph 3: "[The appellant] shall use its best efforts to promote the objects of the Foundation and the . . . Plan by encouraging persons . . . to enter into scholarship agreements."

Paragraph 6: "If any subscriber to a scholarship agreement requests that the Foundation terminate the agreement within 60 days after the Acceptance of a scholarship agreement, then . . . the Foundation shall have the right to terminate the agreement and to cause to be returned to the subscriber all funds deposited with the Depository in respect of that agreement. If the Foundation exercises this right, then [the appellant] shall not be entitled to any payment whatsoever in respect to the agreement and shall repay to the Foundation all funds received by it in respect to the agreement, failing which the Foundation may deduct the amount of these funds from other payments due from it to [the appellant]."

Paragraph 8**:** "(a) The Foundation shall pay to [the appellant] an amount equal to the enrolment fees in respect of all Scholarship Agreements sold by [the appellant], as they fall due.

(b) [The appellant] agrees that it will render all necessary assistance to the Foundation to enable the Foundation to administer the Plan. In consideration of [the appellant's] assistance, the Foundation shall pay to [the appellant], or as [the appellant] may direct, the full amount of the annual fee deposited in the Operating Account with the Scholarship Trustee and the full amount of any Depository Fees received by the Foundation in respect of Scholarship Agreements entered into after the date hereof and prior to the date of termination."

[54] The Franchise Agreement is drafted in a way that respects the provincial regulation's objectives, giving leeway to subscribers, not forcing them either to participate or to stay in the Plan.

[55] However, the provisions of the Franchise Agreement dealing with the remuneration of the appellant for the sale of Scholarship Agreements are drafted, in my view, in such a fashion that the appellant may claim that it is entitled to that remuneration from the moment a scholarship agreement is sold. I say so for the following reasons.

[56] First, paragraph 6 of the Franchise Agreement states that if the Foundation exercises its rescission right where a subscriber withdraws from the Plan within the first 60 days, "then [the appellant] shall not be entitled to any payment whatsoever", meaning in my view that, *a contrario*, the appellant is entitled to that payment if the subscriber does not exercise his or her right to withdraw from the Plan.

[57] Second, paragraph 8 states that the Foundation is to pay to the appellant, not "the enrolment fees", but an "amount equal to the enrolment fees" in respect of all scholarship agreements sold. Comparing this with the provision regarding the remuneration to be paid to the appellant for its assistance in administering the Plan, we see that under paragraph 8b) the Foundation is to pay "the full amount of the annual fee deposited in the Operating Account . . . and the full amount of any Depository Fees received by the Foundation in respect of scholarship agreements". Paragraph 8(b) does not say "an amount equal to", it speaks rather of "the full amount of the annual fee deposited" and "the full amount of any Depository Fees received".

[58] In my view, the Franchise Agreement was worded in such a way that the administration fees were to be paid when they were deposited or when the Foundation received them, something which was not specified for the enrolment fees. Paragraph 8(a) instead uses the phrase “an amount equal to the enrolment fees in respect of all scholarship agreements sold”.

[59] The fact that the Foundation was to pay the enrolment fees as they fell due does not mean that the appellant was entitled to receive them only upon receipt of those fees by the Foundation. An amount equal to the enrolment fees was payable by the Foundation as soon as Scholarship Agreements were sold, but that amount did not have to be paid until the enrolment fees fell due.

[60] In my view, the payment of the deposits by members did not constitute a condition precedent binding on the appellant that prevented it from claiming the amount equal to the enrolment fees until the deposits were made. The appellant had a legal right to an amount equal to the enrolment fees as soon as the Scholarship Agreements were sold. As stated by the Supreme Court of Canada in the *Maple Leaf Mills* case, for an amount to become receivable in any taxation year, two conditions must coexist: (1) a right to receive compensation; (2) a binding agreement between the parties (76 DTC 6182 at page 6186).

[61] As *Mertens* said in the excerpt from *Law of Federal Income Taxation* quoted in the passage from the *Meteor Homes* decision cited by the Federal Court of Appeal in *Commonwealth Construction supra*, at page 6424, not every contingency prevents the accrual of income. The possible occurrence of a condition subsequent to the creation of a liability is not grounds for postponing the accrual (*ibid.*). Applying the principle adopted by the Federal Court of Appeal in *Commonwealth Construction*, I find from the record that the right of the appellant to an amount equal to the enrolment fees was subject to no restriction even though it might have been necessary to return the enrolment fee money if the subscriber withdrew from the plan during the first 60 days, and even though the appellant might never receive the enrolment fee in the event that the subscriber did not make the deposits. The fact that subscribers could opt out of the Plan constitutes in my view a condition subsequent which did not prevent the accrual of income in the year the Scholarship Agreements were sold by the appellant.

[62] This conclusion is, in my view, not contradicted by the testimony of either Mr. Loduca or Ms. Johnston. Mr. Loduca acknowledged in his testimony that it was the sale of the Scholarship Agreements that triggered the right to receive enrolment fees. Ms. Johnston testified that the Foundation’s entitlement to the enrolment fees

arose at the time a contract was signed or upon the signature of the cheque, whichever was more recent, and that the Foundation could not compel a member to make a payment. In her testimony regarding her interpretation of the Franchise agreement, she referred to the time at which the enrolment fees became payable to the appellant, not the time at which the appellant became entitled to them.

[63] That the appellant was to be paid when the deposits fell due does not alter the fact that its right to receive the amount came into being as soon as the Scholarship Agreement was signed and not when the Foundation was required to pay (see *The Queen v. Derbecker*, 84 DTC 6549 (FCA)). Nor does the possibility that the subscriber might cancel the plan mean that the appellant's entitlement was uncertain or conditional (see *The Queen v. La Capitale, Compagnie d'Assurance Générale*, 98 DTC 6428 at page 6430).

[64] I also agree with the respondent that the sale by the appellant of its accounts receivable to its parent company and the fact that it recorded those accounts receivable as assets in its financial statements are also an indication that the appellant did consider that it was entitled to receive the enrolment fees in the year they were earned, that is, the year in which the agreements were sold.

[65] This conclusion accords with the principles governing the interpretation of commercial contracts as reproduced in this Court's decision in *Costco Wholesale Canada Ltd. v. Canada*, [2009] G. S. T.C. 38, 2009 TCC 134:

> 17. In answering this question, and in interpreting these contracts, the parties agreed that the principles of contractual interpretation to be relied upon are well summarized by the Ontario Court of Appeal in *3869130 Canada Inc. v. I.C.B. Distribution Inc*.:
>
> 31 ...
>
> Broadly stated ... a commercial contract is to be interpreted,
> (a) as a whole, in a manner that gives meaning to all of its terms and avoids an interpretation that would render one or more of its terms ineffective;
> (b) by determining the intention of the parties in accordance with the language they have used in the written document and based upon the "cardinal presumption" that they have intended what they have said;
> (c) with regard to objective evidence of the factual matrix underlying the negotiation of the contract, but without reference to the subjective intention of the parties; and (to the extent there is any ambiguity in the contract),
> (d) in a fashion that accords with sound commercial principles and good business sense, and that avoids a commercial absurdity.

[66] Finally, the fact that the Foundation was a non-profit corporation and did not have any assets does not affect my conclusion. Indeed, National Policy 15 provided that sufficient funds must be set aside in trust to pay the costs of administering the trust funds held by the Depository, and the Scholarship Agreements provide that the Depository is authorized to constitute an operating account to be used to pay future expenses of administration of the Foundation (paragraph 2(b)(iv*)*. Therefore, while the Foundation had no assets, the operating fund existed precisely for the purpose of paying the expenses, including, in my view, the enrolment fees earned that were to be paid when they fell due.

[67] I therefore conclude that the enrolment fees had to be reported in income on an accrual basis in the year they were earned, which is not necessarily the year they fell due or the year they were paid.

II. Did the inclusion of the enrolment fees receivable in computing the appellant's income for the 1999 taxation year provide a more accurate picture of the appellant's income?

[68] The short answer is that if the Minister was right in including the enrolment fees receivable in income in the year they were earned, he ought to have excluded the enrolment fees earned in prior years in order to present an accurate picture of the appellant's income in 1999. Evidence supporting this is that, in its financial statements, the appellant adopted the predictive method that is recognized by the Minister, and it reported income before taxes in the amount of $225,731 in 1999. If the appellant had used the same method for income tax purposes, making the appropriate adjustments, its net income would have been $514,610 (as I will explain later on) instead of the $2,009,856 reported by the appellant (arrived at by taking out the enrolment fees earned in 1999 and including the enrolment fees earned prior to 1999).

[69] The Minister, in adopting the predictive method without taking out the enrolment fees earned in prior years, arrived at an income figure of $13,305,885. This is clearly not an accurate picture of the appellant's income for 1999.

[70] In *Canderel Limited v The Queen*, 98 DTC 6100, the Supreme Court of Canada said at page 6110:

> (1) The determination of profit is a question of law.

> (2) The profit of a business for a taxation year is to be determined by setting against the revenues from the business for that year the expenses incurred in earning said income: *M.N.R. v. Irwin, supra, Associated Investors, supra.*
>
> (3) In seeking to ascertain profit, the goal is to obtain an accurate picture of the taxpayer's profit for the given year.
>
> (4) In ascertaining profit, the taxpayer is free to adopt any method which is not inconsistent with
>
> (a) the provisions of the *Income Tax Act*;
> (b) established case law principles or rules of law; and
> (c) well-accepted business principles.
>
> (5) Well-accepted business principles, which include but are not limited to the formal codification found in G.A.A.P., are not rules of law but interpretive aids. To the extent that they may influence the calculation of income, they will do so only on a case-by-case basis, depending on the facts of the taxpayer's financial situation.
>
> (6) On reassessment, once the taxpayer has shown that he has provided an accurate picture of income for the year, which is consistent with the Act, the case law, and well-accepted business principles, the onus shifts to the Minister to show either that the figure provided does not represent an accurate picture, or that another method of computation would provide a more accurate picture.

[71] In my view, the appellant has shown that the financial statements prepared using the predictive method, and relied upon by the Minister in including in income the enrolment fees earned in 1999 but not yet received, provided an accurate picture of income for 1999. As I said earlier, the income before taxes reported in the financial statements is $225,731.

[72] For income tax purposes, if adjustments are made without deducting the enrolment fees earned in 1999 ($11,842,789), the income reported should be around $410,017, as can be seen from Exhibit A-3. The first column of Exhibit A-3 shows the before-tax income reported in the financial statements ($225,731). The first item in the second column is the after-tax income shown in the financial statements ($75,245). I take into account the fact that the amount of $75,245 does not include the amount of $13,442,628 (the enrolment fees earned prior to 1999), but does include the amount of $11,842,789 (the enrolment fees earned in 1999 but not received in 1999). Thus, if we add all the adjustments in the second column (with the exception of the $13,442,628 that should not have been included for 1999 as it represents enrolment fees earned prior to 1999) to the net income of $75,245 and do

not deduct the $11,842,789, we arrive at an income of $410,017. If we add to that the amount of $104,593 (shown as the second to last item of the third column) representing convention expenses disallowed and not at issue before me, the income to be reported should be $514,610.

[73] The Minister determined the appellant's income for tax purposes to be $13,305,885[3] (see Exhibit A-3, third column).

[74] In my view, on a balance of probabilities the amount of $514,610 provides an accurate picture of the appellant's income for the 1999 taxation year. As a matter of fact, except for those with respect to the enrolment fees, the Minister has accepted all the adjustments to income shown in Exhibit A-3. As we know, the appellant chose to report its income without including enrolment fees earned but not yet received from subscribers, which resulted in its reporting income for tax purposes of $2,009,856. Thus, the appellant has already penalized itself by reporting that amount of income instead of $514,610.

[75] The figures referred to above show without any doubt that the income amount assessed by the Minister does not present an accurate picture of the appellant's income for 1999. There is a huge difference between the amount that should have been reported in the first instance ($514,610) or even the income actually reported by the appellant ($2,009,856) and the income assessed by the Minister ($13,305,885).

[76] The respondent contented that the appellant was precluded from arguing that the enrolment fees earned prior to 1999 should be subtracted from income because that point was not raised in its pleading. The respondent relied on an excerpt from *The Law of Civil Procedure* by Williston and Rolls, cited with approval by Rip J. of this Court in *Santoro,* in stressing the importance of pleadings. The function of pleadings was therein described as fourfold:

1. to define with clarity and precision the question in controversy between litigants;
2. to give a fair notice of the case which has to be met so that the opposing party may direct his evidence to the issues disclosed by them;
3. to assist the Court in its investigation of the truth of the allegations made by the litigants;
4. to constitute a record of the issues involved in the action so as to prevent future litigation upon the matter adjudicated between the parties.

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[3] This figure includes the enrolment fees earned prior to 1999.

[77] It is true that the appellant's argument on objecting to the reassessment was that the enrolment fees earned in 1999 should not be included in income as it had no entitlement to those fees. However, the appellant relied on sections 9 and 12 of the ITA in asking this Court to vacate the reassessment under appeal.

[78] Moreover, the respondent herself, in her Amended Reply to the Notice of Appeal, opened the door to an argument that income should be calculated in such a manner as to provide an accurate picture of the appellant's income.

[79] In the end, I must decide whether to confirm the reassessment or not. In this particular case, the method of computing income is the basis for reassessment. The determination of profit pursuant to section 9 of the ITA is a question of law. In computing the reassessed income, the Minister, deliberately or not, did not exclude from income the enrolment fees earned prior to 1999.

[80] In the circumstances, I find it somewhat dishonest to argue that the assessment should be confirmed on the basis that the appellant did not specifically raise the issue that the enrolment fees earned prior to 1999 should be subtracted from income. In my view, it is implicit that if the appellant failed to convince the Court that it was right in excluding from its income for 1999 the enrolment fees earned in that same year, then, for the purpose of the computation of profit, the enrolment fees earned prior to 1999 should be excluded.

[81] The respondent cannot claim that she was caught by surprise, or that she was not given fair notice of the case which had to be met. The question in controversy was the method to be used to compute income. It was certainly open to the appellant for the purpose of rebutting the allegation that its income as reassessed provided an accurate picture of its profit for the 1999 taxation year, to raise the fact that the enrolment fees earned prior to 1999 were not subtracted from income by the Minister.

[82] To draw a parallel with the situation in *Argus Holdings Limited v. The Queen*, 2000 DTC 6681 (FCA), it would be a gross distortion of the appellant's income picture if the enrolment fees earned prior to 1999 were to be included in income for that year, for that income does not represent profit for the 1999 taxation year but is profit for prior years. Accordingly, an accurate picture of income would not be provided if both the enrolment fees earned in 1999 and those earned prior to 1999 were taxed in the appellant's 1999 taxation year.

[83] Furthermore, the fact that, unless the reassessment is upheld, the appellant may escape taxation on the amount that was not included in income in prior years due to the method adopted by the appellant in reporting income for tax purposes is not relevant. It cannot be used as a justification for a reassessment that the Minister does not have the power to make under the ITA (see *Trom Electric Co. Ltd. v. The Queen*, 2005 DTC 62, 2004 TCC 727).[4]

[84] Finally, with respect to the respondent's argument that, pursuant to subsections 169(2.1) and 165(1.11) of the ITA, the appellant, being a large corporation, could not raise a new issue, that is, one not raised in its Notice of Objection, the appellant replies that it is not raising a new issue, but is only bringing forward new facts or new reasons to demolish the Minister's assumptions and respond to the Minister's argument.

[85] In *British Columbia Transit v. Canada*, [2006] G.S.T.C. 103, 2006 TCC 437, C. Miller J. of this Court, commenting on the *Potash* case relied upon by the respondent, stated the following:

> 39 In the case before me, the Respondent has identified BC Transit's failure as failing to provide any facts respecting the property tax and sublease payments, and failing to provide any reasons as to the "nominal consideration" issue in the Notice of Objection. It did not argue that there have been any failures with respect to the issue or to the relief sought.
>
> 40 I do not find the Respondent's argument persuasive. The *Potash* case was not about the lack of facts or reasons: it was about not allowing an increase in the amount at issue. There is no change to the amount at issue before me from what was set out in the Notice of Objection, nor has the issue changed. The issue has always been the entitlement to the ITCs. The Respondent is correct that the property tax was not raised as part of the facts or reasons, but I find this is not fatal.
>
> 41 In the *Potash* case, the Court quoted comments from Mr. R.M. Beith, an official from Department of Finance, made at the 1994 Canadian Tax Foundation Conference:
>
> > One of the reasons for the legislation is to identify disputed issues much sooner so that a taxation year's ultimate tax liability can be determined in a timely way.

[4] I must say here that the appellant did not really escape taxation on the amount of enrolment fees earned prior to 1999. It is true that in 1998 the appellant deducted the amount of $13,442,628, but it included in its income for 1998 the enrolment fees earned prior to 1998 (see Exhibit R-1).

> Owing to the complexity of the law and the number of issues, for many years a number of large corporations have had some of their taxation years left open through outstanding notices of objection or appeals, so that they have been able to raise new issues based on emerging interpretations and the outcome of court decisions challenged by other taxpayers.
>
> Recently, a particular problem was identified by the auditor general and the Public Accounts Committee. A case dealing with the calculation of the "resource allowance" which was decided against the department, resulted in claims not only based on the particular facts decided by the court but in respect of a new issue concerning the calculation of the "resource allowance". These claims, both directly and indirectly from the court decision, involved significant amounts of tax and interests [*sic*].
>
> In summary, it is essential that revenues be more predictable and therefore that potential liabilities be identified and resolved within a more reasonable time.

42 This emphasizes that it is the issue and quantum that is of significance to the Minister, not the facts and reasons that the Respondent points to as the failure. It would prohibitively handcuff the large corporation to read these provisions as limiting the large corporation to only those facts identified at the Notice of Objection stage. That does not appear to be the thrust of the section as supported by Mr. Beith, nor the interpretation of this section by the Federal Court of Appeal in *Potash*. The very words of section 306.1 itself refer only to the issues and the relief. Interestingly, at the 1994 Tax Conference Mr. Beith went on to say this about paragraph 165(1.11)*(c) (Income Tax Act* equivalent to paragraph 301(1.2)*(c)*):

> This requirement is no different from what the law currently requires from all taxpayers. In addition, in contrast to the requirements with respect to issue and quantum, additional facts and reasons can be raised in appeals.

This is certainly a sensible point of view, and one which I adopt. I find BC Transit is not in breach of subsection 301(1.2) and, therefore, section 306.1 is not invoked. BC Transit is free to argue that property tax and sublease payments are facts that go to the consideration for the lease.

[86] In the present case, the Minister reassessed the appellant’s income at $13,305,885. If the appellant had reported income on an accrual basis for income tax purposes, as it did for accounting purposes, its income should have been around $514,610. The appellant reported income of $2,009,856. It is not asking to reduce its income to $514,610. It is only asking to have vacated the reassessment, which shows

an income of $13,305,885. I do not find to be fatal the fact that the appellant did not mention specifically in its pleadings that the enrolment fees earned prior to 1999 were not subtracted by the Minister in reassessing the appellant's income for 1999. As I said before, it is implicit in this case, and it can be inferred from the pleadings, that the appellant did not accept the income amount computed by the Minister. The facts brought forward by the appellant proved on a balance of probabilities that the income as reassessed by the Minister does not present an accurate picture of the appellant's income for the 1999 taxation year.

[87] For the foregoing reasons, the appeal against the reassessment dated August 27, 2004 in respect of the appellant's 1999 taxation year made by the Minister under the ITA is allowed and the reassessment is referred back to the Minister for reconsideration and reassessment on the basis that the revised taxable income of $13,305,885 is not representative of the appellant's profit for that year. The net income of $2,009,856 reported by the appellant shall be restored with the addition, however, of an amount of $104,593 representing convention expenses that were disallowed and whose disallowance was not challenged by the appellant in this appeal. The deduction of $3,076 for charitable donations allowed by the Minister is not at issue. **The additional permissive deductions, being the increased deduction in respect of prior years' losses carried forward and the increased capital cost allowance granted by the Minister in order to reduce the overall tax liability resulting from the reassessment under appeal (as referred to in paragraph 5 of the Notice of Appeal), shall be reversed as requested in subparagraph 36(b) of the Notice of Appeal.**

[88] At the request of the parties, representations on costs shall be made to the Court either in writing or orally, as the parties wish, within 30 days of the date of the **amended** judgment.

Signed at Ottawa, Canada, this **16th** day of **April** 2010.

"Lucie Lamarre"

Lamarre J.

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