

Court orders delivery of tax planning memo prepared by accountants to CRA

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Overview

The recent Tax Court of Canada decision in [Gaudreau v. The King](#) demonstrates the ability of the Canada Revenue Agency (CRA) to obtain sensitive non-lawyer work product. In Gaudreau, the taxpayer was assessed under s. 84(2) of the Income Tax Act, (Tax Act) regarding their sale of an interest in an insurance company. The taxpayer vendor and the purchaser agreed on a hybrid sale, i.e., a sale of both assets and shares. The main substantive issue in the appeal, which is ongoing before the Tax Court of Canada, is whether the CRA was justified in applying subsection 84(2) of the Tax Act to the transactions in question, to produce a deemed dividend rather than a taxable capital gain for the taxpayer.

Tax Court proceedings

In the course of the Tax Court proceedings, the taxpayer was examined for discovery and asked to provide a “a tax planning document implying in particular the possibility of a hybrid transaction or other, whether it be a memo, an exchange of emails, letters, or any other form whatsoever, and provide it” and “provide the exchanges between the sellers and the planners who did the tax planning, gave the figures, whether in the form of exchanges, letters, emails or any other form.”¹

In response, the taxpayer identified the existence of a document relating to the hybrid sale prepared by the accounting firm for the purchaser, which had been shared with them as vendor and their advisor’s (the Accountant’s Memorandum). The taxpayer asserted that they were not required to produce the Accountant’s Memorandum. The basis for resisting production of the Accountant’s Memorandum was two-fold: First, that it was not relevant to the issue on audit, and second that, consistent with the teachings of the Federal Court of Appeal in *BP Energy Company v. Canada*, 2017 FCA 61, there is no obligation on a taxpayer to self-audit. As the Court observed at paragraph 44:

“... in his written submissions, the Appellant asserts that the Memorandum is not relevant to the litigation, insisting that it does not deal with, discuss or analyze subsection 84(2) of the Law. Still according to the appellant, the respondent’s

request for disclosure of the Memorandum, a document of which he is neither the author nor the recipient, indicates that the respondent is seeking to establish a new basis for assessment. He submits that the examination for discovery cannot be used to conduct fishing expeditions.”

In contrast, in response to the resistance to producing the Accountant’s Memorandum, the CRA acknowledged that the existence of the transactions was not in issue but nevertheless argued that there was a debate “on the circumstances surrounding the transactions” (para. 45). Further, the CRA relied upon Rule 82 of the Tax Court Rules, which provides that the full disclosure of documents is required subject only to relevance. Thus, the fact that the CRA may already have the information contained in the Accountant’s Memorandum is not a reason justifying the refusal to produce it at the Discovery stage.

The Court readily agreed with the CRA, accepting the proposition that the fact that a document may contain previously obtained information does not justify refusing to disclose it at the discovery stage, and noting that “this aspect in itself supports a conclusion that the Memorandum might be relevant to the issues in dispute”.

Notably, while the parties also agreed that the Accountant’s Memorandum was not subject to solicitor-client privilege, the taxpayer nonetheless argued it should not be disclosed because of a form of accountant-client privilege. The Tax Court categorically rejected this argument, addressing it as follows at paragraph 59:

“I will briefly discuss the appellant’s comments that accountants must be able to inform taxpayers of the tax risks incurred without the risk of disclosure to the tax authorities discouraging the preparation and communication of their analysis. According to the appellant, if this advice must be systematically disclosed, the quality of communication between accountants and their clients and compliance with the Act will be reduced. The courts have confirmed that there is no accountant-client privilege with respect to tax advice given by a public accountant. I note that the appellant has made no submissions with respect to privilege based on the circumstances of each case in respect of which the Supreme Court of Canada has held that the principles enunciated by Professor Wigmore provide the general framework for analysis to determine whether or not a communication is privileged. In these circumstances, I cannot conclude that the communication of the Memorandum is privileged on a case-by-case basis and since there is no accountant-client privilege, this is not a ground that could justify the refusal to communicate in this case, even though in certain cases, the communication of tax advice could, according to the appellant, discourage the communication of advice by accountants to their clients.” [citations omitted]

Following this rejection of privilege as a basis for resisting disclosure of the Accountant’s Memorandum, the Tax Court proceeded to find the document relevant and therefore, producible, particularly in the context of an examination for discovery where the question of relevant must be interpreted “broadly and liberally” (para. 62). It remains with the CRA, however, to establish that the document is relevant to its pleadings at trial.

Conclusion

The Court's recognition that in certain cases, privilege may attach to the work product of accountants is a nod to the fact that had the Accounting Memorandum been prepared on behalf of a taxpayer for use by its legal counsel in providing legal advice, its disclosure could have been prevented based on solicitor-client privilege. In Canada, solicitor-client privilege has been repeatedly recognized by the courts as a quasi-constitutional right which is "essential to the effective operation of the legal system" (R. v. Gruenke, [1991] 3 SCR 263 at 289; Canada (A.G.) v. Federation of Law Societies, 2015 SCC 7 at para. 82). The Supreme Court of Canada has determined that solicitor-client privilege is "integral to the workings of the legal system itself" (R. v. McClure, 2001 SCC 14 at para. 31). In undertaking tax planning which requires the interpretation and application of complex legislation, and which may attract the attention of the CRA, it behooves a taxpayer to consult with legal counsel. Working with tax counsel helps to ensure that the resulting work product is protected from disclosure to third parties such as tax authorities. Gaudreau is a good reminder that solicitor-client privilege is the only reliably available way in which to protect sensitive legal analysis from the curious eyes of the CRA.

If you have questions about the TCC's decision or tax disputes in general, reach out to your BLG lawyer, the authors of this piece, any of the key contacts below or a member of [BLG's Tax Group](#).

¹ The Judgment was published in French. The quotations are from an unofficial translation into English.

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