

Docket: 2017-3210(IT)I

BETWEEN:

BOREALIS GEOPower INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on June 22, 2018, at Calgary, Alberta

Before: The Honourable Justice Diane Campbell

Appearances:

Counsel for the Appellant: Melanie Pituch

Counsel for the Respondent: Peter Basta

JUDGMENT

The appeal with respect to a tax assessment dated August 12, 2016 and a reassessment dated August 22, 2016 for the 2014 taxation year is dismissed, without costs, in accordance with the attached Reasons for Judgment.

Signed at Summerside, Prince Edward Island, this 13th day of September 2018.

“Diane Campbell”

Campbell J.

Citation: 2018 TCC 189

Date: 20180913

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BETWEEN:

BOREALIS GEOPOWER INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Campbell J.

[1] This appeal is in respect to a tax assessment dated August 12, 2016 and a reassessment dated August 22, 2016 for the Appellant’s 2014 taxation year.

[2] The Appellant is a privately owned Canadian corporation involved in geothermal power exploration, development and utilization in Canada. The Appellant was involved in 2014 in a project involving extensive field exploration, scientific analysis and proof of a geothermal resource at its properties in British Columbia. The Appellant received government assistance from Sustainable Development Technology Canada (“SDTC”) in respect to this project.

[3] SDTC is a “not for profit foundation constituted for the purpose of fostering the development and adoption of technologies that contribute to Sustainable Development Technologies infrastructure in Canada by contributing to the rapid development, demonstration and pre-commercialization of technological solutions which address climate change, clean air, clean water and clean soil;...”. (Exhibit A-1, Contribution Agreement, page 3, paragraph 2)

[4] The Contribution Agreement between SDTC and the Appellant set out the terms and conditions respecting this project. In August, 2014, the Appellant received an advance of \$528,560.00 from SDTC. The Appellant deposited the cheque into a trust account established for this purpose at CIBC. The Minister of National Revenue (the “Minister”) determined that this project met the definition

of Scientific Research & Experimental Development (“SR&ED”), pursuant to subsection 248(1) of the *Income Tax Act* (the “Act”) and this is not at issue in this appeal.

[5] On December 23, 2015, the Appellant late filed its income tax return for the taxation year ending December 31, 2014. However, the Appellant was required to file its return on July 2, 2015. In its return, the Appellant reported net taxable income of over \$91,000.00, claimed the SR&ED Investment Tax Credit (“ITC”) and also filed a SR&ED Expenditures Claim Form. **The Appellant’s position is that the SDTC funds were not received nor were they entitled to be received in 2014 as the funds were in a trust account. Consequently, it did not include the funds advanced from SDTC in its 2014 income tax return. Therefore no tax was owing by the Appellant due to the tax credit.**

[6] After an audit review, the Minister accepted the SR&ED expenditures of approximately \$373,000.00 but the Appellant was assessed on the basis that it had received government assistance of \$528,560.00 from SDTC in the 2014 taxation year. Due to the Minister’s inclusion of this amount in respect to the 2014 taxation year, the allowable SR&ED expenditures were reduced and a recapture of SR&ED expenditures in the amount of \$188,704.00 was assessed. As a result, the Minister made total adjustments to the Appellant’s net income in the amount of \$494,066.00. In addition, an ITC in the amount of \$108,657.00 was denied due to the inclusion of the government assistance amount. (This amount should actually be \$102,497.00 instead of \$108,657.00 as the Appellant did not consider the receipt of non-government assistance of \$17,600.00 in calculating the qualified expenditures for ITC purposes). All of this resulted in tax payable of \$67,907.00, a repeat late filing penalty of \$13,581.40 together with accrued interest on the outstanding tax arrears.

[7] Subsequently, the Appellant submitted a request for a loss carryback in the amount of \$240,686.00 from its 2015 taxation year to the 2014 taxation year. On August 22, 2016, the Minister reassessed the Appellant’s 2014 taxation year to give effect to the Appellant’s request resulting in a reduction of the amount of taxable income and a corresponding reduction of the assessed tax payable from \$67,907.00 to \$37,989.00. The late filing penalty amount remained the same.

[8] **The issue before me is whether the Appellant is liable for the late filing penalty and the interest that was assessed against it.** This issue is dependent on whether the Appellant received the amount of \$528,560.00 from SDTC in the 2014 taxation year. If the amount of \$528,560.00 was not received by the Appellant in

the 2014 taxation year, then it would not be included in the 2014 taxation year calculations of the Appellant's SR&ED expenditures, ITC and recapture. It would follow that the penalties would be removed and the interest would be recalculated on the revised amount of tax owing on the due date.

[9] As a secondary issue, the Appellant also submitted that both the penalty and interest were incorrectly calculated by the Minister and should be reduced due to the non-capital loss carryback from the Appellant's 2015 taxation year which reduced its taxable income for the 2014 taxation year.

[10] The Appellant's position is that, in the 2014 taxation year, it had a limited amount of income which was offset by the SR&ED ITC resulting in the Appellant owing no tax. While the Appellant admits to late filing its 2014 income tax return, it did not anticipate that a penalty and interest would be assessed because it believed that it did not owe any taxes. **The Appellant submits that it did not "receive" the funding from SDTC in 2014 and therefore those funds should not be used in the calculation and reduction of SR&ED credits.** According to paragraph 37(1)(d) of the *Act*, government assistance, such as the SDTC funding, is to be attributed in the year that "the taxpayer has received, is entitled to receive or can reasonably be expected to receive the funds". **Since the Appellant deposited the funds in a trust account and had not met the conditions set out in the Contribution Agreement, the SDTC funds had not been received by the Appellant in 2014.**

[11] The Respondent submits that the Minister correctly reassessed the Appellant's SR&ED expenditures and the corresponding ITC because the SDTC funding of \$528,560.00 was government assistance within the meaning of subsection 127(9) of the *Act* that the Appellant received, was entitled to receive or could reasonably be expected to receive in its 2014 taxation year. The Minister correctly applied this amount to reduce the Appellant's pool of deductible SR&ED expenditures pursuant to paragraph 37(1)(d) of the *Act* and correctly assessed a recapture of SR&ED expenditures in the amount of \$188,704.00 which resulted in the Appellant not being entitled to the SR&ED ITC. The penalty of \$13,581.40 was justified due to the late filing of the 2014 income tax return pursuant to subsection 162(2) of the *Act*. Interest was correctly assessed for the period during which the Appellant was liable to pay taxes.

[12] While the Respondent spent considerable time reviewing case law that addressed whether funds meet the definition of government assistance, this was not in issue. In fact, the Appellant counsel, in her submissions on behalf of the corporation, pointed out that it had never argued that the SDTC funds were

anything but government assistance. The only issue is whether the Appellant owes the assessed penalty and interest and that answer depends entirely on when the Appellant received the SDTC funds of \$528,560.00.

[13] The Appellant late filed its 2014 income tax return on December 23, 2015 because it did not believe it owed any tax. The Appellant believed that it had not received the SDTC funds in 2014 because they were voluntarily deposited in a trust account and were subject to conditions that had to be met before they could be withdrawn and used by the Appellant. If the funds were received by the Appellant in 2014, then it will impact the pool of deductible SR&ED expenditures and the tax payable with the result that the Appellant will owe the assessed penalty and interest. Put another way, has the Appellant "...received, is entitled to receive or can reasonably be expected to receive" [paragraph 37(1)(d)], the SDTC funds in the 2014 taxation year.

[14] According to the Contribution Agreement, certain "Milestones" had to be achieved prior to the Appellant submitting a claim to SDTC for payment of an instalment of the project contribution amount. Pursuant to C.3, Schedule of Payments, the first advance from SDTC in the amount of \$528,560.83 was payable upon the occurrence of two events:

Payable upon:

1. Execution of the Contribution Agreement, and
2. Providing evidence satisfactory to SDTC that Enbridge has submitted their criteria for proceeding with Phase 2 activities.

(Contribution Agreement, page 43)

This second condition had not been fulfilled at the time of the advance of funds from SDTC because Enbridge, one of the funding partners of the project, had decided not to proceed in late 2014.

[15] The Appellant submits that according to the Contribution Agreement, since not all of the conditions for receipt of the funds from SDTC had been satisfied, the \$528,560.00 cannot have been "received" in the 2014 taxation year even though it transferred to the Appellant and was placed in a trust account.

[16] The Supreme Court of Canada in *Canada Trustco Mortgage Co v Canada*, [2005] 2 SCR 601, 2005 SCC 54, sets out the principles of statutory interpretation in determining the intent of a provision. It requires a textual, contextual and purposive interpretation approach to find a meaning that will be harmonious with the *Act* as a whole. However, where the text of the provision is clear and unambiguous, its **ordinary meaning** will be of paramount importance particularly where it is supported by the contextual and legislative purpose underlying the wording of the provision.

[17] The word **“receive”** is defined similarly in a number of leading dictionaries.

- (A) 1. acquire or accept (something offered or given)
2. accept delivery of (something sent)

Canadian Oxford Dictionary, Second Edition

- (B) 1. come into possession of: acquire (a gift)

Webster's Ninth New Collegiate Dictionary

- (C) 1. take or accept into one's hands or one's possession (something offered or given);
2. accept delivery of (a thing sent); be a recipient (of)...

- (D) Be provided with or given; acquire; get

The New Shorter Oxford English Dictionary, Volume 2, N-Z

- (E) To get or be given something

Cambridge Dictionary On Line

- (F) (1) to take (something offered) into one's hand or possession
(2) ...
(3) to accept delivery or transmission of

Collins English Dictionary On Line

[18] Black's Law Dictionary, Tenth Edition, also defines the word "receive" in a manner similar to the dictionary definitions:

1. To take (something offered, given, sent, etc.); to come into possession of or get from some outside source...

[19] A number of cases have dealt with the word "receive" particularly in the context of bursary awards. Appellant's counsel suggested that such case law could be distinguished because they dealt with different types of transfers than the transfer in this appeal of government assistance from SDTC to the Appellant. In addition, the Contribution Agreement outlined various contractual conditions governing the spending of those funds. However, although those decisions are factually different, they can provide guidance on how the Court has treated the definition of "receive" generally.

[20] In *Jean-Paul Morin v The Queen*, [1974] FCJ No. 907, the Federal Court (Trial Division) found that an employee, who never actually had possession of the funds, withheld by his employer at source to pay taxes fixed by regulation, had nevertheless "received" the funds:

[24] ...the word 'receive' obviously means to get or to derive benefit from something, to enjoy its advantages without necessarily having it in one's hands....

...

[26] ...the expressions "to benefit from, to gain advantage from or to profit from" are included under the generic term "to receive".

[21] The decision in *Timothy S. Jones v The Queen*, [2002] TCJ No. 338, [2002] 3 CTC 2483 (T.C.C.), quoted with approval the *Morin* reasoning in concluding that, scholarship funds credited toward tuition via book entries had been received by the taxpayer because he had derived benefits or advantages from those funds even though they were never in his physical possession. The Court in *Jones*, at paragraph 59, referred to a number of cases and stated that they all stood "...for the proposition that one need not actually receive the money in his hand in order for there to be a benefit received by him but it is sufficient that he received moneys' worth and that he derived benefits from something or he enjoyed its advantages."

The Federal Court of Appeal in *Scott Irwin Simser v The Queen*, 2004 FCA 414, quoted with approval the reasoning in *Jones*.

[22] Bell J. in *Jean-Calvin Mbarga v The Queen*, 2005 TCC 595, followed the reasoning in both *Morin* and *Jones* in concluding at paragraph 5 that “receipt” includes constructive receipt.

[23] In *Her Majesty the Queen v Jean Livingston*, 2008 FCA 89, the Federal Court of Appeal considered whether there had been a “transfer” of property under section 160 of the *Act*. At paragraph 21, the Court stated:

[21] The deposit of funds into another person’s account constitutes a transfer of property. To make the point more emphatically, the deposit of funds by Ms. Davies into the account of the respondent permitted the respondent to withdraw those funds herself anytime. The property transferred was the right to require the bank to release all the funds to the respondent. The value of the right was the total value of the funds.

Based on the Court’s conclusions, if funds “transferred” into an individual’s bank account constitutes a “transfer”, similarly it would also constitute a “receipt” of those funds by that individual.

[24] Applying the foregoing to the facts before me, I conclude that the Appellant received the SDTC funds in the amount of \$528,560.00 in the 2014 taxation year. SDTC issued a cheque to the Appellant in 2014. It was issued despite the fact that the second condition precedent to the advance of that amount had not and never has been fulfilled (Schedule C.3, Contribution Agreement). At paragraph 3.5 of the Contribution Agreement, the obligation of SDTC to make an instalment payment to the Appellant:

...is subject to the fulfillment, or the waiver by SDTC, in its sole discretion, of each of the following conditions on or before the time of each such payment:

- a) *Accuracy of Representations and Warranties*....
- b) *Performance*. The Eligible Recipient shall have performed and complied with all agreements and conditions contained in this Agreement required to be performed or complied with by the Eligible Recipient prior to or on the Payment Date; and
- c) *Disbursement*....

(Emphasis Added)

[25] According to the wording in this provision, SDTC could advance and transfer an instalment under the Contribution Agreement prior to the completion of the Milestone objective established in the Agreement. This is what occurred here. When the Appellant received the advance, the funds were deposited to a CIBC trust account. On cross-examination, Mr. Timothy Thompson, the current Chairman of Borealis Geopower, testified that the funds were left in the trust account “until such a time as we were allowed to withdraw”. (Transcript, page 38, lines 21-22). The Contribution Agreement however is silent respecting Milestone achievements once such an advance is made and it is also silent in respect to advances that are deposited to a trust account set up by an eligible recipient.

[26] The Appellant had sole access to the funds in this trust account. It had the authority to deposit and withdraw. There was no trust agreement between SDTC and the Appellant. There may have been an informal agreement respecting those funds but there was no obligation for the Appellant to notify SDTC when it transferred amounts from the trust account to another account. (Transcript, page 40). The Appellant notified SDTC “...occasionally when upon their request what the balance was...” (Transcript, page 40, lines 21-22). In fact it does not appear that SDTC placed any formal restrictions on the use of the remaining funds in this trust account until September 16, 2016 when in a letter to the Appellant, it instructed that no further funds were to be withdrawn from the account without written consent from SDTC. (Exhibit A-3).

[27] Further evidence of the control that the Appellant exercised over the funds in the trust account was Mr. Thompson’s testimony in re-direct where he stated that withdrawals were made as the work continued but at year end some money was redeposited because of overdraws. “...we put ourselves in the position where we had taken less than what we were obliged, and that’s kind of how we did it.” (Transcript, page 48, lines 13-15).

[28] In accordance with the ordinary dictionary meaning of “receive”, the Appellant physically acquired and accepted an advance of funds by way of a cheque from SDTC. The advance was given prior to the completion of the first Milestone and no conditions were superimposed on the transfer. The Appellant accepted delivery. It had possession of the cheque. It was the Appellant’s decision to open a trust account and deposit those funds to that account. It exercised control over the funds in relation to expenditures in the work project, when to withdraw and how much to withdraw.

[29] The Appellant's second argument, that the late filing penalty and interest were incorrectly calculated, also fails. The Appellant was required to file its income tax returns for the 2011 and 2013 taxation years on July 3, 2012 and July 2, 2014, respectively. However, those returns were not filed until June 30, 2015. For the 2014 taxation year, the Appellant filed its income tax return on December 23, 2015 when it was required to be filed on July 2, 2015. The penalty was calculated pursuant to subsection 162(2) of the *Act* in respect to a period of five months beyond the filing due date. This resulted in a late filing penalty of \$13,581.00.

[30] Subsection 162(11) of the *Act* addresses the effect of subsequent events on a taxpayer's tax payable for the year including the calculation of a penalty:

Effect of subsequent events

(11) For the purpose of computing a penalty under subsection 162(1) or 162(2) in respect of a person's return of income for a taxation year, the person's tax payable under this Part for the year shall be determined before taking into consideration the specified future tax consequences for the year.

[31] The term "specified future tax consequences" referred to in subsection 162(11), is defined in subsection 248(1) to include the consequences of a deduction or an exclusion of an amount referred to in paragraph 161(7)(a) of the *Act*:

Effect of carryback of loss, etc.

(7) For the purpose of computing interest under subsection 161(1) or 161(2) on tax or a part of an instalment of tax for a taxation year, and for the purpose of section 163.1,

(a) the tax payable under this Part and Parts I.3, VI and VI.1 by the taxpayer for the year is deemed to be the amount that it would be if the consequences of the deduction, reduction or exclusion of the following amounts were not taken into consideration:...

[32] Accordingly, the Appellant's tax payable for the purposes of calculating the late filing penalty for the 2014 taxation year cannot take into account either the non-capital loss carryback or ITC carryback. This application of the provisions to the calculation of the penalty in this appeal is supported as well by the jurisprudence (*Hazhir Zandi v The Queen*, 2012 TCC 259, 2012 DTC 1246). The late filing penalty was correctly calculated by the Minister in accordance with

those provisions. The non-capital loss carryback incurred in 2015 cannot be taken into account when considering the Appellant's tax payable for the 2014 taxation year for the purpose of calculating the late filing penalty amount.

[33] Similarly, pursuant to subsection 161(7) of the *Act*, carryback deductions used to reduce income tax in a preceding taxation year will not affect the calculation of interest for that year. The Federal Court of Appeal in *Connaught Laboratories Ltd. v The Queen*, [1994] FCJ No. 1681, 94 DTC 6697, concluded that there was no ambiguity in the wording of subsection 161(7), nor was the provision offensive to the intent and purpose of the *Act*. The Minister correctly calculated the interest payable on the tax that would have been payable by the Appellant except for the non-capital loss carryback to the 2014 taxation year. Interest will not be retroactively removed on an outstanding tax balance that is calculated prior to a loss carryback or an ITC from a subsequent taxation year.

[34] For these reasons, the appeal is dismissed, without costs.

Signed at Summerside, Prince Edward Island, this 13th day of September 2018.

“Diane Campbell”

Campbell J.

CITATION: 2018 TCC 189
COURT FILE NO.: 2017-3210(IT)I
STYLE OF CAUSE: BOREALIS GEOPOWER INC. AND HER MAJESTY THE QUEEN
PLACE OF HEARING: Calgary, Alberta
DATE OF HEARING: June 22, 2018
REASONS FOR JUDGMENT BY: The Honourable Justice Diane Campbell
DATE OF JUDGMENT: September 13, 2018

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