MEDIATION OF CANADIAN TAX DISPUTES

by

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Abstract

This paper evaluates mediation as a potential alternative strategy for resolving Canadian tax disputes with the Canada Revenue Agency (CRA). It examines the current notice of objection procedure for resolving tax disputes and reviews its challenges to achieve timeliness and high quality communication and information exchange with Canadian taxpayers. It examines mediation as an alternative dispute resolution strategy and surveys its potential benefits in the tax context. Drawing upon the experiences of the United States, United Kingdom, and Australia with tax mediation, this paper resurrects the idea, last seriously considered by the CRA in 1997, that mediation has the potential to address the deficiencies in the Canadian notice of objection process. Finally, this paper examines the constraints under which the Canada Revenue Agency operates and discusses the types of Canadian tax disputes that are, as a result, both well and ill-suited to resolution by mediation.
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INTRODUCTION

Resolving tax disputes is one of the major functions of revenue bodies.¹ As tax disputes grow in frequency and complexity, revenue bodies confront challenges to effectively and efficiently resolve tax disputes under the constraints of limited resources.² These challenges are but one aspect of the broader administrative and enforcement challenges currently facing many revenue bodies.³ Under the constraints of limited and sometimes squeezed budgets, revenue bodies are required fulfil all aspects of their administration and enforcement mandates in the face of modern pressures brought to bear including globalization, heightened taxpayer mobility, and taxpayers’ creative and sometimes exploitive approaches to personal and business tax minimization.⁴ In order to address these broader challenges, many revenue bodies have taken heed of the recommendation of the Organisation for Economic Co-operation and Development (OECD) to adapt their tax administration and enforcement strategies to meet the demands of the modern tax administration environment and, more specifically, to implement a more efficient, relationship-based, approach to resource allocation.⁵

Against this backdrop, this paper evaluates mediation as an alternative dispute resolution strategy to complement the existing process for resolving Canadian taxpayers’ disputes with the Canada Revenue Agency (the “Agency”). It concludes that, compared to the Agency’s status quo approach to tax dispute resolution, mediation presents itself as a preferable strategy for resolving

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¹ Ernst & Young, Tax Dispute Resolution: A New Chapter Emerges: Tax Administration Without Borders (np: EYGM Limited, 2010).
² Ibid at 4.
³ Ibid.
⁴ Ibid. See also Parliament, “Tax Evasion and the Use of Tax Havens: Report of the Standing Committee on Finance” by James Rajotte in Sessional Papers, No 17 (2013)[Tax Evasion] (providing detailed information of these challenges as they face the Canada Revenue Agency).
several common types of tax disputes. When used in appropriate circumstances, mediation not only delivers on its promise to provide quicker and less expensive dispute resolution, but it does so in a manner that is more compatible with and that advances the objectives of the relationship-based approach to tax administration that the Agency adopted in accordance with the recommendations of the OECD.

The case for tax mediation made in this paper follows the framework used by Canadian author and tax counsel, Deen C. Olsen, in her evaluation of mediation for Canadian tax disputes as presented at the 1997 annual conference of the Canadian Tax Foundation. To facilitate her evaluation, Olsen adopted the four-part framework promulgated by the Dispute Systems Working Group (DSWG) of the Administrative Conference of the United States (ACUS), an organization then devoted to the implementation of alternative dispute resolution programs in the public sector. Using the ACUS framework, Olsen considered the following four factors to evaluate the potential for mediation of Canadian tax disputes: (i) the legal constraints under which the Agency operates; (ii) the existing dispute resolution process of the Agency; (iii) the types of disputes encountered and their likelihood to be settled; and, (iv) the problems and desired improvements identified in the existing dispute resolution process. This paper considers these factors in the following order. Chapter 1 examines the Agency’s current approach to dispute resolution and discusses its problems and the desired improvements. Chapter 2 examines the ways in which mediation has demonstrated the potential to address the problems identified in Chapter 1 and draws upon the experiences of the revenue bodies in the United States, the United Kingdom, and Australia with tax mediation to illustrate. Chapter 3 examines

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7 Ibid at 4.
the legal constraints under which the Agency operates and reviews the types of tax disputes that mediation is, as a result, both well- and ill-suited to resolve. The final chapter concludes. Whereas Olsen’s analysis cautioned that mediation for Canadian tax disputes should not be embraced solely as part of a “theme of change for the sake of change,” this paper argues that mediation of tax disputes should be embraced in Canada in response to change. More specifically, it should be adopted as a rational response to the problems that currently fetter the Agency’s effective administration of the tax dispute resolution process and as a strategic element in the plan to fulfil the Agency’s broader mission to implement a more efficient, relationship-based, approach its more general administration and enforcement mandates.

8 Ibid at 20.
CHAPTER 1

Introduction

This chapter describes the tax dispute resolution process currently administered by the Agency. It surveys its successes as well as its quantitative and qualitative problem areas. In particular, this chapter focuses on two key deficiencies in the Agency’s tax dispute resolution process: (i) its lack of timeliness, and; (ii) its failure to achieve high quality communication and information exchange with taxpayers. This chapter concludes with a discussion of the broader role that a more open and communicative dispute resolution process that better facilitates information exchange can play in achieving greater overall efficiency in the Agency’s approach to administration and enforcement.

Tax Dispute Resolution with the Agency

The administration and enforcement of Canada’s taxing statutes – including, inter alia, the Income Tax Act, Excise Tax Act, Canada Pension Plan, and Employment Insurance Act – is the responsibility of the Canadian federal Minister of National Revenue (the “Minister”). Under the Canada Revenue Agency Act, the mandate of the Agency is, among other things, to support the administration and enforcement of Canada’s taxing statutes. On behalf of the Minister, and as agent of Her Majesty the Queen, the Agency carries out the functions that comprise the

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9 Income Tax Act, RSC 1985, c 1 (5th Supp), s 220(1) [ITA]; Excise Tax Act, RSC 1985, c E-15, s 275 [ETA]; Canada Pension Plan, RSC 1985, c C-8, s 92 [CPP]; Employment Insurance Act, SC 1996, c 23 [EIA].
10 Canada Revenue Agency Act, SC 1999, c 17, s 5.
administration and enforcement of the Canadian taxing statutes.\textsuperscript{11} Resolving tax disputes that arise under these statutes is one of the Agency’s key functions.\textsuperscript{12}

Tax disputes arise in a variety of ways.\textsuperscript{13} In the ordinary course, disputes arise during the Agency’s audit or review of a taxpayer or upon the Minister’s subsequent issuance of an assessment or reassessment.\textsuperscript{14} While there is no formal procedure for resolving disputes with Agency auditors or reviewers, it is the practice of auditors and reviewers to provide taxpayers with an opportunity to preview initial audit or review findings and to provide additional information for consideration in the event that there are disagreements with initial findings.\textsuperscript{15} Upon assessment or reassessment, taxpayers who dispute tax assessed must seek redress by lodging an administrative appeal with the Agency in the form of a “notice of objection” or they must simply abandon the matter.\textsuperscript{16}

The notice of objection procedure is the only administrative procedure for resolving tax disputes \textit{per se}. Though there are other processes and procedures – such as advance rulings and advance pricing agreements – through which taxpayers may engage with the Agency to predetermine tax outcomes, it is only through the notice of objection procedure that taxpayers may dispute assessments of tax.\textsuperscript{17} Taxpayers initiate the process by filing a written notice of objection with the Agency within 90 days of the issuance of a disputed assessment.\textsuperscript{18} Once an objection is lodged, the Minister becomes obliged to reconsider the disputed assessment with “all

\begin{thebibliography}{9}
\bibitem{11}Ibid, s 4.
\bibitem{14}Ibid at 1-4.
\bibitem{15}Ibid at 4. This opportunity is normally provided through the issuance of “30-day letters” which provide taxpayers with a 30-day window within which to provide additional information.
\bibitem{16}Supra note 9. \textit{ITA} s 165; \textit{ETA} s 301(1.1); \textit{CPP} s 36; \textit{EIA} ss 91, 92.
\bibitem{17}Supra note 1, at 31 (for an outline of processes available for predetermining tax outcomes with the Agency).
\bibitem{18}Supra note 9. \textit{ITA} s 165; \textit{ETA} s 301(1.1); \textit{CPP} s 36; \textit{EIA} ss 91, 92.
\end{thebibliography}
due dispatch” and to vacate, confirm, or vary it. Taxpayers may appeal disputed assessments directly to the Tax Court of Canada if their objections are not resolved within 90 days of receipt by the Minister.20

The appeals branch of the Agency administers the notice of objection process.21 Its role is adjudicative in nature. As a division of the Agency that is independent from the audit and other divisions that issue assessments in the first instance, the appeals branch is required to perform fresh and independent reviews of disputed assessments.22 The Minister may not resolve taxpayers’ objections otherwise than in accordance with the facts and law as they are understood.23 Accordingly, reviews performed the Agency’s appeals branch must take into account relevant facts and law and must exclude other considerations such as fairness, collection risk, or litigation risk.24

As part of the notice of objection process, appeals personnel may engage with objecting taxpayers or their representatives by telephone or in writing in order to obtain any additional disclosure or other information required to complete their review.25 Less frequently will appeals personnel engage with taxpayers in person.26 Following the completion of information gathering, appeals personnel then evaluate disputed assessments and adjudicate taxpayers’ disputes in light of the facts and law as they are understood. Written decisions accompanied by notices of

19 Supra note 9. ITA s 165; ETA s 301(1.1); CPP s 36; EIA ss 91, 92.
20 Supra note 9. ITA s 169; ETA s 302; CPP s 36; EIA ss 91, 92.
21 Supra note 13 at 47-51.
22 Ibid. See also Canada Revenue Agency, “RC4067 Protocol - Between the Compliance Programs Branch and the Appeals Branch of the Canada Revenue Agency” (7 July 2005), online: Canada Revenue Agency <http://www.cra-arc.gc.ca/E/pub/tg/rc4067/rc4067-e.html>.
24 Ibid. See also supra note 6 at 15.
25 Supra note 6 at 6. See also supra note 13 at 47-51.
26 This observation is made based on the author’s own experience.
reassessment or notices of confirmation are subsequently issued to objecting taxpayers.27 Taxpayers who disagree with the results obtained through this process must either abandon their disputes or escalate them to the Tax Court of Canada.28

Evaluating the Tax Dispute Resolution Process

The tax dispute resolution process as it is currently administered by the Agency functions reasonably well. As a general rule, the Agency resolves objections to the satisfaction of Canadian taxpayers.29 In this regard, the Agency reports that at least 90 percent of the objections it resolves are concluded without further appeal by taxpayers to the Tax Court of Canada.30 Indeed, during the late 1990s, Canadian taxpayers filed approximately 55,000 objections per year, out of which the Agency resolved over 90 percent either to the satisfaction of taxpayers or without further appeal by taxpayers to the Tax Court of Canada.31 This trend remained stable throughout the early 2000s. Between 2001 and 2003, the Agency received between 59,000 and 73,000 objections per year.32 Of these, the Agency resolved over 93 percent without further litigation.33 As recently as 2011, and despite a notable increase in the number of objections lodged with the Minister, the Agency’s rate of resolution without further litigation showed continued stability. In that year, of the 80- to 110-thousand objections filed by Canadian taxpayers, approximately 92 percent were resolved by the Agency without further litigation.34

27 Supra note 9.
28 Supra note 9. ITA s 169; ETA s 302; CPP s 36; EIA ss 91, 92.
29 Supra note 6 at 7.
30 Ibid at 6.
33 Ibid.
The Agency’s appeals branch also strives to play a more than merely adjudicative role in the dispute resolution process. Though its role is unavoidably and fundamentally adjudicative in nature, the appeals branch additionally strives to achieve the consensus of objecting taxpayers with the results. In this regard, a recent report of the Auditor General of Canada found that appeals branch personnel are required to do more than merely “check the accuracy” of disputed assessments and are expected, impliedly more fundamentally, to in fact “resolve dispute[s]”.

To do this, appeals branch personnel engage with taxpayers in a variety of ways intended to achieve their understanding and agreement. Strategies may include “explaining the basis for an assessment, ... reaching a common understanding of the facts involved and the applicable laws, [or] agreeing on a settlement.”

Finally, the appeals branch of the Agency is, on the whole and as it holds itself out to be, impartial. While systemic factors arising from the lack of formal independence between the appeals branch and the Agency are observed to create incentives that predispose appeals branch personnel to harbour bias in favour of the Minister, reviews by the Auditor General of Canada have found little actual evidence of systemic bias within the appeals branch in favour of confirming disputed assessments. One such review found that outcomes of taxpayers’ objections do not appear to be skewed in favour of the Minister but display relatively even

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36 Ibid at 6.26.
37 Ibid.
38 Ibid at 6.25; 1998 Report, supra note x 5.45; see also supra note 6 at 6.
39 For additional discussion of the lack of independence of the appeals branch, see Karen Sharlow, “Keeping Revenue Canada in Line” (Paper delivered at the 1997 Canadian Tax Foundation National Tax Conference, 1997) Report of Proceedings of Forty-Ninth Tax Conference (Toronto: Canadian Tax Foundation, 1998) 13. (She writes at 7: “… no change to Revenue Canada’s administrative practice can bring true independence to appeals officers as long as appeals officers look forward to long careers in other divisions of Revenue Canada. Appeals officers in that situation cannot reasonably be expected to exercise any significant degree of independence from their employer or their colleagues.”).
distribution between the Minister and objecting taxpayers.\textsuperscript{40} In the two years surveyed by the Auditor General, the appeals branch confirmed just over one-third of taxpayers’ objections in favour of the Minister, allowed just under one-third in favour of objecting taxpayers, and allowed in part the remaining objections.\textsuperscript{41} With this distribution of results, the appeals branch confirmed just less than sixty-percent of the taxes in dispute.\textsuperscript{42} 

Alongside indicators that the notice of objection process functions reasonably well are indicators that aspects of it nonetheless stand to be improved. The process exhibits somewhat significant deficiencies that have historically limited and, it is contended here, continue to limit its overall quality and effectiveness. During the late 1990s, the Agency’s notice of objection process underwent a comprehensive review and, as a result of its less-than-stellar findings, the Agency launched the Appeals Renewal Initiative in 1997.\textsuperscript{43} Through this initiative, the Agency sought to improve several aspects, both measurable and qualitative, of the notice of objection process.\textsuperscript{44} Among the key objectives of the reforms undertaken as part of the Appeals Renewal Initiative were those to “... facilitate earlier resolution of taxpayer disputes, to improve communication between taxpayers and [the Agency], and to improve transparency to the taxpayer.”\textsuperscript{45} Current trends suggest that the Agency has yet to fully achieve these objectives.

\textbf{The Quantitative Challenge: Time}

It is contended here that the key quantitative challenge facing the Agency’s tax dispute resolution process is its lack of timeliness. Unduly delayed tax dispute resolution has important

\textsuperscript{40} 1998 Report, supra note 31 at 5.45.
\textsuperscript{41} Ibid.
\textsuperscript{42} Ibid.
\textsuperscript{43} Revenue Canada, Pamphlet No. 97-107, “Appeals Renewal Initiative – Towards an Improved Dispute Resolution Process” (Ottawa: Revenue Canada, 1997). See also supra note 6 at 7.
\textsuperscript{44} Ibid.
\textsuperscript{45} 1998 Report, supra note 31 at 5.82.
consequences. It prolongs the uncertainty associated with unresolved tax issues and it occupies the resources of revenue bodies and taxpayers alike. Though it was among the objectives of the Agency’s Appeals Renewal Initiative to achieve earlier resolution of tax disputes, the sluggishness of the notice of objection process continues to raise concerns.\textsuperscript{46}

Evaluations of the timeliness of the Agency’s notice of objection procedure consistently suggest that there is a significant opportunity for the process to be improved by earlier and swifter dispute resolution. One year after the Appeals Renewal Initiative commenced, a review of the Auditor General of Canada noted that taxpayer objections were frequently settled late in the dispute resolution process.\textsuperscript{47} The Auditor General accordingly recommended that the Agency implement strategies in order to promote earlier disclosure by taxpayers for the purpose of achieving earlier conclusions to disputes.\textsuperscript{48} The Auditor General raised timeliness as a concern again in 2004.\textsuperscript{49} This time, it found that while the Agency resolved more than half the income and excise tax objections lodged within its internal deadlines, the Agency’s internal deadlines exceeded “by a large margin” the 90 day period after which taxpayers become entitled to appeal directly to the Tax Court of Canada.\textsuperscript{50} In the same report, the Auditor General gave an even bleaker assessment of the Agency’s timeliness in resolving objections filed pursuant to the \textit{Canada Pension Plan} and \textit{Employment Insurance Act}.\textsuperscript{51} For these objections it found that, even when measured against the Agency’s internal deadlines, fewer than half were resolved in a timely manner.\textsuperscript{52}

\textsuperscript{46} \textit{Supra} note 43.
\textsuperscript{47} 1998 \textit{Report, supra} note 31 at 5.62.
\textsuperscript{48} \textit{Ibid}.
\textsuperscript{49} 2004 \textit{Report, supra} note 12 at 6.31-6.33.
\textsuperscript{50} \textit{Ibid}.
\textsuperscript{51} \textit{Ibid} at 6.40-6.44.
\textsuperscript{52} \textit{Ibid} at 6.42.
More recently, the drawn-out periods of time associated with resolving tax disputes was the subject of discussion among Canadian tax professionals at a 2012 conference of the Canadian Tax Foundation. 53 There it was noted that among the key concerns of Canadian tax professionals with the present notice of objection procedure is the undue delay seemingly built into the process.54 Corroborating the complaint, the Agency reported in May of 2012 that in the years 2009 and 2010 it took an average of 299 calendar days to resolve taxpayers’ objections.55

The Qualitative Challenge: Communication and Information Exchange

It is contended here that the Agency’s dispute resolution procedure also fails to achieve high quality communication and information exchange between objecting taxpayers and the appeals branch. Improving communication and information exchange was among the key objectives of the reforms adopted by the Agency’s Appeals Renewal Initiative.56 In order to address these issues, the Agency implemented several reforms intended on its side to facilitate improved transparency and more complete information exchange.57 In particular, the Agency undertook to provide taxpayers with better access to its internal working papers and other documentation prepared in support of disputed assessments.58 The Agency additionally undertook to provide added training to appeals personnel in order “... to assist them in maintaining clear and open communication with taxpayers while they resolve their dispute[s]

54 Ibid.
56 Supra note 43.
57 Ibid. See also Christina Tari, Federal Income Tax Litigation in Canada, loose-leaf (consulted on 19 January, 2013), (Markham: LexisNexis, 1997) at 3.44.
58 Supra note 43. See also 1998 Report, supra note 31 at 5.62.
…”59 Though such reforms have been in place for sixteen years following the commencement of the Appeals Renewal Initiative, there remain signs that the Agency fails through the notice of objection process fails to achieve high quality communication and information exchange with objecting taxpayers. In particular, as set out below, evidence of inadequate communication and information exchange is found in the experience of self-represented taxpayers in the Tax Court of Canada and in rates of pre-hearing settlements and withdrawals of appeals.

Evidence of inadequate communication and information exchange during the notice of objection procedure is witnessed in the experience of self-represented taxpayers in the Tax Court of Canada.60 The experience of self-represented taxpayers in the Tax Court of Canada was the subject of study in a recent paper by André Gallant.61 Gallant’s study revealed that self-represented taxpayers face difficulties in the Tax Court of Canada that taxpayers with legal representation do not. Indeed, as he writes, at “… times it seems the [self-represented] taxpayer is simply at a disadvantage from the moment the hearing begins.”62 While the nature of self-representation is such that it is to be expected that self-represented appellants will experience comparative disadvantages over taxpayers with legal representation, some of the specific difficulties encountered by self-represented taxpayers in the Tax Court are, as advanced below, consequences of low quality information exchange and communication during the earlier notice of objection process.

Litigation commenced by self-represented appellants comprises a significant portion of the Tax Court of Canada docket.63 In 2004, of the over 4000 appeals filed in the Tax Court, 32

59 Supra note 57 at 3.45.
61 Ibid.
62 Ibid at 335.
63 Ibid at 336.
percent were filed by self-represented taxpayers.64 Similarly, in 2011, between 25 and 35 percent of Tax Court appeals involved self-represented litigants.65 Such self-represented taxpayers most frequently appear before the Tax Court pursuant to the *Tax Court of Canada Rules (Informal Procedure)*.66 The purpose of these informal procedure rules, in contrast to the *Tax Court of Canada Rules (General Procedure)*, is to provide an informal judicial process, not unlike a small claims court in efficiency and informality, for resolving appeals that involve less substantial amounts of tax in dispute.67 In particular, under the *Tax Court of Canada Rules (Informal Procedure)*, tax appeals are permitted proceed with relaxed rules of pre-hearing disclosure and evidence.68

Gallant has observed that, among the difficulties encountered by self-represented litigants, such litigants are more likely than taxpayers with legal representation to have an inadequate appreciation of the tax and other legal issues that their appeals raise and for the Minister’s evidence or arguments in support of disputed assessments.69 Self-represented taxpayers are also more likely than taxpayers with legal representation to have an inadequate appreciation for the factual issues raised in their appeals and the evidentiary standards to be met in order to achieve success in the Tax Court of Canada.70 Indeed, self-represented taxpayers’ often deficient appreciation for the nature and source of their disputes can be severe enough in individual cases that judges presiding over their appeals become willing to play a comparatively

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64 *Ibid.*
65 This statistic was derived by the author using data reported by John R. Sorensen in “Tax Court of Canada 2011 Canadian Tax Foundation Update” (2012) 22:2, Ontario Bar Association Taxation Law, online: Ontario Bar Association <www.oba.org/en/pdf/sec_news_tax_jun12_sor_tcc.pdf>.
66 *Ibid.* In 2011, just over three quarters of appeals involving self-represented taxpayers were filed pursuant to the *Tax Court of Canada Rules (Informal Procedure).*
67 *Supra* note 60 at 334, 336-340; *Tax Court of Canada Rules (Informal Procedure).*
68 *Ibid.*.
69 *Supra* note 60 at 335.
70 *Ibid* at 335, 351.
more interventionist role in order to facilitate smoother hearings.⁷¹ As Gallant writes, in such cases, judges “serve as a catalyst” in order to “augment the efficiency of the court’s procedures” and assist with “clarifying the issues.”⁷²

Gallant identifies inadequate disclosure and information exchange during the pre-hearing litigation steps as one of the underlying causes of the difficulties that self-represented taxpayers encounter.⁷³ He writes:

The first step ... is for the taxpayer to know the case against him or her. While things have improved since the time when taxpayers did not even have the benefit of a reply to the notice of appeal, the taxpayer is still in the dark in some instances. [...] The next step is to ensure that the taxpayer brings all relevant documents and witnesses required to argue his or her case.⁷⁴

To address this issue, he recommends, inter alia, that consideration be given to mandatory pretrial conferences and mandatory prehearing disclosure for appeals involving self-represented appellants.⁷⁵

There is no doubt that the implementation of reforms such as these would address one of the underlying causes of the comparative disadvantages faced by self-represented taxpayers in Tax Court of Canada. Such reforms would ensure to some greater degree than that already achieved that self-represented taxpayers are put on a more equal footing with taxpayers with legal representation with respect to disclosure. However, prima facie, Gallant’s observations also invite the conclusion that the difficulties faced by self-represented taxpayers originate in and are symptomatic of low quality communication and information exchange achieved during the earlier notice of objection dispute resolution process.

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⁷¹ Ibid at 344.
⁷² Ibid.
⁷³ Ibid at 363.
⁷⁴ Ibid.
⁷⁵ Ibid at 364.
Evidence of low quality communication and information exchange at the notice of objection stage is also found in rates of out-of-court settlement of Tax Court of Canada appeals following the completion of pre-hearing discovery and disclosure processes. Of the disputes resolved by the Agency and later appealed to the Tax Court of Canada, approximately one-third are resolved ahead of hearings, while another one-third are withdrawn by taxpayers.  

Such out-of-court resolutions are frequently achieved as a result of new information obtained during the pre-hearing disclosure and discovery processes. Indeed, the Agency recently noted in an internal case file review that, among the files reviewed, “... new information was provided [by taxpayers] and considered in 50% of the decisions made by the Tax Court.” These statistics suggest that there is an opportunity, through higher quality communication and information exchange during the notice of objection phase, to prevent a greater number of disputes – disputes that ex post demonstrate the capacity to be resolved without judicial intervention – from escalating into Tax Court litigation in the first place.

Tax disputes that mature into litigation but that are otherwise capable of resolution without court intervention unnecessarily occupy the resources of the Tax Court of Canada. In recent years, the Tax Court has expressed concerns about the impact of unnecessary demands on its resources as it struggles to process the growing accumulation in its inventory of appeals. A recent internal review of case management in the Tax Court concluded somewhat ominously that if delays and backlogs are “... permitted to continue, [the Court] will never be able to reduce [its] inventory of cases.”

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76 This statistic was derived by the author using statistics provided by Sorensen, supra note 65.
77 1998 Report, supra note 31 at 5.60.
78 Tax Appeals Evaluation, supra note 55 at 5.1.4.
While the majority of appeals lodged in the Tax Court are settled out-of-court or withdrawn, the Tax Court now plays a role in encouraging more such out-of-court settlement in order to address its case management issues.\(^{81}\) In particular, it has proposed new rules with respect to the award of costs in order to encourage where possible earlier and more frequent out-of-court settlement.\(^{82}\) The current rules for awarding limited tariff-based costs under the *Tax Court of Canada Rules (General Procedure)* take into account, *inter alia*, written settlement offers and some jurisprudence from the Tax Court suggests that greater weight is now given to written settlement offers than to other factors relevant to award of costs.\(^{83}\) Going further, the newly proposed rules hold out to litigants the potential award of “substantial indemnity costs” to parties that initiate written settlement discussions.\(^{84}\) Where one party initiates settlement discussions by offering terms of out-of-court resolution and the opposing party subsequently rejects the offer, then, in the further event that the matter matures into a hearing before the Tax Court, if the original offering party “… obtains a judgment as favourable as or more favourable than the terms of the offer to settle,” then the Tax Court may award the offering party “substantial indemnity costs.”\(^{85}\) These substantial indemnity costs may be awarded at a value up to 80 percent of the actual legal fees incurred by the offering party from the date of the settlement offer forward.\(^{86}\) Rules for awarding costs in the Federal Court of Appeal are similar.\(^{87}\)

\(^{81}\) Tax Court of Canada, Practice Note 17, “Proposed rules and amendments with respect to Settlement Offers, Lead Cases and Litigation Process Conferences” (13 January 2010); Practice Note 18, “Proposed amendments to Rule 147 with respect to settlement offers” (10 February 2011) online: Tax Court of Canada <http://cas-ncr-nter03.cas-satj.gc.ca/portal/page/portal/tcc-cci_Eng/Process/Practice_Notes>.
\(^{82}\) Ibid.
\(^{83}\) *Tax Court of Canada Rules (General Procedure)* r 147(1)(d). See also *Barrington Lane Developments Limited v Her Majesty the Queen*, 2010 TCC 476, 2010 D.T.C. 1323 at 13.
\(^{84}\) *Supra* note 81.
\(^{85}\) Ibid.
\(^{86}\) Ibid.
\(^{87}\) *Federal Courts Rules* r 419-421.
To the extent that high rates of settlement without judicial intervention of appeals launched in the Tax Court of Canada are indicative of a notice of objection procedure that fails to achieve high quality communication and information exchange, these rates are also *prima facie* indicators of a notice of objection procedure that fails to achieve taxpayer consensus at rates equal or comparable to the observed rates of resolution without further appeal by taxpayers. If indeed there is a gulf between the number of taxpayers that agree with the results of objections as determined by the Agency and the number of taxpayers who choose not to escalate their dispute to the Tax Court of Canada, then additional concerns arise about the efficacy of Agency’s efforts to achieve consensus or understanding with objecting taxpayers. While this paper has focused on timeliness and high quality communication as key priorities for the Agency, it is noted here that deficiencies in the notice of objection procedure cannot be cleanly isolated. Deficiencies in any one aspect of the dispute resolution process imply deficiencies in all its aspects.

**Communication and Information Exchange: Defining the Relationship Paradigm**

While evidence and consequences of inadequate communication and information exchange in the Agency’s notice of objection process are witnessed in and borne by the Tax Court of Canada, the Agency bears a significant, if less directly observable, impact as well. Led by the OECD, current thinking on best-practices for tax administration and enforcement ascribes a pivotal role to high quality communication and information exchange at all points of engagement between revenue bodies and taxpayers, including but not limited to the dispute resolution process. In outline, the theory is that the overall quality of communication and information exchange between revenue bodies and taxpayers is reflected in the bottom-line

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88 *Tax Intermediaries, supra note 5.*
efficacy and efficiency of tax administration and enforcement.\textsuperscript{89} If the theory is correct, then low quality communication and information exchange achieved during the Agency’s dispute resolution process may indirectly but significantly interfere with the overall success of the Agency in fulfilling its administration and enforcement mandates.

The value of high quality communication and information exchange is particularly heightened in light of the modern pressures brought to bear on revenue bodies in the current tax administration environment.\textsuperscript{90} Indeed, it arose primarily out of a need to identify strategies to address the modern pressures facing revenue bodies that the OECD undertook to study and report on the importance to revenue bodies of an open and more communicative relationship with taxpayers.\textsuperscript{91} The modern pressures on revenue bodies are wide-ranging.\textsuperscript{92} Revenue bodies are required to administer and enforce increasingly complex tax laws, in an increasingly globalized and mobile business environment, and against some taxpayers’ creative and sometimes exploitive personal and business tax minimization strategies, all while under the constraints of limited resources.\textsuperscript{93} In order to address the challenges facing revenue bodies in this environment, the OECD has put forward the thesis that high quality communication and information exchange between revenue bodies and taxpayers is a key element in achieving more efficient allocations of the limited resources that revenue bodies have available to bring to bear on tax administration and enforcement.\textsuperscript{94}

In particular, the OECD’s observes that the traditional or “basic” relationship between taxpayers and revenue bodies has “... tended historically to be more confrontational than

\textsuperscript{89} Ibid.
\textsuperscript{90} Ibid.
\textsuperscript{91} Ibid at 9. See also Base Erosion, supra note 5; Tax Evasion, supra note 4.
\textsuperscript{92} Ibid.
\textsuperscript{93} Ibid.
\textsuperscript{94} Tax Intermediaries, supra note 5.
According to the OECD, the nature of basic relationship is characterized by “… parties interacting solely by reference to what each is legally required to do,” which, in many instances, results in an “information gap” for revenue bodies. As a direct result of its minimalist nature, the basic relationship inhibits the free flow of information between taxpayers and revenue bodies. It thereby fails to provide revenue bodies with an epistemic basis upon which to distinguish high- from low-risk taxpayers. As a result, revenue bodies blindly allocate their resources and fail to achieve efficient, risk-based, resource allocations.

Accordingly, the OECD recommends that revenue bodies adopt where possible an approach to tax administration and enforcement that facilitates the transformation of the relationship paradigm with taxpayers from basic to “enhanced.” In contrast to the basic relationship, the enhanced relationship is defined by transparency and open communication. It is a relationship in which “… both the government and the taxpayer trade transparency for certainty.” It is a relationship in which taxpayers “… engage … with revenue bodies based on co-operation and trust, with both parties going beyond their statutory obligations.” The enhanced relationship “…favour[s] collaboration over confrontation, and [is] anchored more on mutual trust than on enforceable obligations.”

If successful, the enhanced relationship approach has the potential to transform the tax administration and compliance environment. In order to facilitate the transformation, the OECD

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95 Ibid at 15.
96 Ibid at 28-30; 39.
97 Ibid at 23-38.
98 Ibid.
99 Ibid at 39-46.
101 Supra note 5 at 5.
102 Ibid at 39.
recommends that revenue bodies take the initial steps.\textsuperscript{103} It recommends that revenue bodies devote resources toward taking on or embodying characteristics and competencies that will encourage taxpayers to engage more openly.\textsuperscript{104} The key such features the OECD expects to encourage more open taxpayer engagement include open disclosure and transparency.\textsuperscript{105} They also include increased commercial awareness, impartiality, proportionality and responsiveness.\textsuperscript{106} The OECD predicts that “…a tax environment in which trust and co-operation can develop” will grow once revenue bodies take steps to improve their competencies in these areas.\textsuperscript{107} In turn, it predicts that taxpayers will reciprocate the efforts of revenue bodies with greater transparency and open communication of their own.\textsuperscript{108}

The intended overall effect of the enhanced relationship approach is to allow revenue bodies to do more with less. The theory is that a mutually more open and transparent relationship with taxpayers will ultimately provide revenue bodies with an epistemic basis upon which to distinguish high- from low- risk taxpayers. Revenue bodies will, as a result, find themselves in a position to liberate resources otherwise inefficiently allocated toward administering and monitoring low risk taxpayers and to more efficiently allocate those resources toward administering and monitoring higher risk taxpayers. This is the essence of the “enhanced relationship” approach.

The OECD’s recommendations amount to a proposal that revenue bodies work to achieve nothing short of a complete paradigm shift in their relationship with taxpayers. That said, the enhanced relationship approach is not intended to replace the basic relationship but to operate as

\textsuperscript{103} Ibid at 40-43.
\textsuperscript{104} Ibid at 33.
\textsuperscript{105} Ibid.
\textsuperscript{106} Ibid.
\textsuperscript{107} Ibid at 40.
\textsuperscript{108} Ibid at 42.
an overlay to it.\textsuperscript{109} The success of the enhanced relationship approach depends upon a robust basic relationship because it “... is built upon fundamental taxpayer rights such as access to an independent judiciary through appeal processes.”\textsuperscript{110}

The theory of the enhanced relationship is yet to be borne out in practice and early signs suggest that not all taxpayers will respond immediately or in kind to revenue bodies’ initiatives toward adopting the enhanced relationship paradigm.\textsuperscript{111} Nevertheless, many revenue bodies, including peers of the Agency, have made the commitment to test the theory and to take the steps recommended by the OECD to develop enhanced relationship approaches to their administration and enforcement strategies and agendas.\textsuperscript{112} Brought on perhaps by necessity, the commitment alone represents nothing short of a paradigm shift in tax administration.

\textbf{From a Basic to Enhanced Relationship in Canada}

The nature of the general relationship between the Agency and Canadian taxpayers is consistent with the OECD’s description of the “basic relationship” paradigm. Using words reminiscent of those of the OECD, Chris Jaglowitz writes, “The relationship between [Canadian] taxpayers and the [Agency] in general has been, historically and by nature, confrontational.”\textsuperscript{113} It was arguably in recognition of this that, even prior to the release of the OECD’s recommendations, the Agency through the Appeals Renewal Initiative “publically

\textsuperscript{109} Ibid at 40.
\textsuperscript{110} Ibid.
acknowledged” that “… improving relations with Canadian taxpayers” was one of its goals.\textsuperscript{114} Now, in light of the work of the OECD to make explicit the connection between open communication and information exchange and effective and effective tax administration and enforcement, the Agency is among the world’s revenue bodies that have publically acknowledged a commitment develop an “enhanced relationship” approach to its administration and enforcement of tax laws.\textsuperscript{115}

The Agency’s challenge, therefore, to establish a more open and communicative dispute resolution process that also facilitates better information exchange is but one aspect of its broader, indeed more fundamental, challenge to establish a generally more open, communicative – “enhanced” – relationship with Canadian taxpayers. In order to achieve the more fundamental goal, taking concrete steps to transform the notice of objection process so that it reflects the characteristics of the enhanced relationship is a strategic place to start. The effect may be synergistic. A more open and communicative notice of objection procedure would not only qualitatively improve the process itself but it may also advantageously contribute to transforming of the relationship paradigm that defines the relationship between the Agency and Canadian taxpayers. In turn, and as noted by the OECD, an overall more enhanced relationship approach to administration and enforcement may result in measurable improvements to the dispute resolution process as well.\textsuperscript{116} In particular, the enhanced relationship approach may facilitate earlier detection and resolution of disputes which is something, as discussed above, from which the Agency could benefit.\textsuperscript{117} In the OECD’s words:

This type of relationship can be very important because … Rather than waiting to have the tax administration come along and

\textsuperscript{114} Supra note 6 at 9.  
\textsuperscript{115} Supra note 112 at 24-29.  See also supra note 100 at 4.  
\textsuperscript{116} Supra note 5 at 24, 41.  
\textsuperscript{117} Ibid.
challenge a particular transaction and how it has been structured many years after the fact, the tax administration and the taxpayers can sit together, review all of the facts on the basis of full disclosure, and make a determination as to whether or not a particular structure works. 118

Thus, if the theory of the enhanced relationship is borne out in practice, achieving a more open and communicative dispute resolution process may represent a win-win-win for the Agency.

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118 Supra note 100 at 4.
CHAPTER 2

Introduction

The first chapter of this paper examined the notice of objection procedure as currently administered by the Agency as well as the dispute resolution strategies employed by the Agency’s appeals branch. It described the challenges, both quantitative and qualitative, that the objections procedure faces. It observed that achieving timeliness in the dispute resolution process as well as open communication and information exchange with taxpayers have historically been and remain significant challenges for the Agency. The importance of an open and communicative dispute resolution procedure is particularly heightened in light of the growing recognition of the role that generally more open communication and information exchanges between taxpayers and revenues bodies plays in achieving efficient and risk-based tax administration and enforcement.

This chapter turns to alternative dispute resolution and mediation. It advances the view that mediation has the potential, when compared to the status quo dispute resolution procedure of the Agency, to better address the Agency’s challenges as outlined in Chapter 1. The chapter begins with an overview of alternative dispute resolution and then focuses specifically on mediation. It reviews the role of mediation in Canadian dispute resolution and surveys the comparative advantages that mediation offers over litigation and purely adjudicative dispute resolution. Finally, this chapter examines mediation of tax disputes among the Agency’s counterparts in the United States, the United Kingdom, and Australia – the Internal Revenue Service (“IRS”), HM Revenue & Customs (“HMRC”) and the Australian Taxation Office (“ATO”), respectively. Following this discussion, this chapter puts forward the thesis that
mediation can provide Canadian tax dispute resolution with comparative benefits that the Agency’s status quo approach either cannot or simply does not provide.

**Alternative Dispute Resolution**

Disputes are commonplace. They are a regular part of social and economic life. The vast majority are insignificant and are resolved or abandoned wholly informally by the disputants themselves. Less common but more serious disputes are also most frequently resolved informally or abandoned by disputants since the investment of time and money associated with litigation ensures that most even serious disputes do not mature into full-blown legal disputes.  

For those disputes that require it, however, there is an alternative. Between resolution or abandonment by the parties and resolution by litigation, “alternative dispute resolution” processes provide an increasingly well-recognized option for resolving otherwise intractable disputes. By demanding a smaller investment of time and money, alternative dispute resolution provides disputants with access to processes designed to facilitate disputants through to achieving non-adjudicated resolutions of otherwise intractable disputes.

Alternative dispute resolution differs fundamentally from litigation and is often defined with reference to it as any dispute resolution process that is not litigation. Black’s Law

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119 Indeed, the investment of time and money has only increased with time creating concerns about an “access to justice” crisis in Canada. See Middle Income Access to Civil Justice Initiative Steering Committee, “Literature Review Background Paper” (Paper delivered at the Middle Income Access to Civil Justice Colloquium at the University of Toronto Faculty of Law, 10 February 2011) [unpublished], online: Access to Justice Initiative <http://www.law.utoronto.ca/about/giving-back-our-communities/access-justice-initiative> at 9; Action Committee on Access to Justice in Civil and Family Matters, “Access to Civil and Family Justice: A Roadmap for Change” (Ottawa: Action Committee on Access to Justice in Civil and Family Matters, 2013), online: Canadian Forum on Civil Justice <http://www.cfcj-fcjc.org/collaborations>; Right Honourable Beverley McLachlin, P.C., Chief Justice of Canada “Remarks to the to the Law Society of British Columbia Public Forum on Access to Justice” (Address delivered at Vancouver, British Columbia, 28 January 2009) [unpublished], online: Canadian Paralegals Institute <http://www.canadianparalegalinstitute.com>.

Dictionary defines alternative dispute resolution as, “A procedure for settling a dispute by means other than litigation…” The ADR Institute of Canada defines alternative dispute resolution as, “... a basket of procedures outside the traditional litigation process, usually entered into voluntarily by parties to a dispute in an attempt to resolve it.”

The broadest notions of alternative dispute resolution that fit the above definitions encompass adversarial and adjudicative processes such as voluntary or mandatory arbitration. For the purposes of this paper, the concept of “alternative dispute resolution” is limited to dispute resolution processes that are voluntary, non-adversarial, and produce only mutually agreed or “consent-based” resolutions, if and when they produce any. It accordingly excludes adversarial and adjudicative processes such as mandatory or voluntary arbitration. Examples of alternative dispute resolution that fit this narrower concept include mediation, negotiation, and conciliation.

Though alternative dispute resolution defines itself by excluding litigation, it enjoys significant support from the legal profession. In Canada, support for alternative dispute resolution from the legal profession began during the late 1980s. In 1989, the Canadian Bar Association (CBA) Task Force on Alternative Dispute Resolution recommended broad professional, academic, and governmental support for all forms of consent-based dispute resolution in Canada. This recommendation was made in order to further the CBA’s earlier resolution, to “support the study and development of alternative forms of dispute resolution” in Canada. A subsequent report issued in 1996 by the CBA Task Force on Systems of Civil Justice recommended that early and continuing “non-binding” dispute resolution processes be

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121 Black’s Law Dictionary, 8th ed sub verbo “alternative dispute resolution”.
122 ADR Institute of Canada, online: <http://www.adrcanada.ca>.
124 Ibid at 73.
125 Ibid.
encouraged in Canada at the earliest stages of litigation. Today the CBA’s national section devoted to alternative dispute resolution operates pursuant to a mandate to “… practice and promot[e] … various forms of alternative dispute resolution including, but not limited to … collaborative law, facilitation and mediation.”

Alternative dispute resolution is efficient, flexible, and cost-effective. There are, however, limits on its appropriate use. Alternative dispute resolution processes do not necessarily lead, as litigious or adversarial processes are intended, to legally normative outcomes. Because their outcomes are voluntary or consent-based, they need not be consistent with outcomes a judicial forum would impose. Because alternative dispute resolution processes are private and confidential, they furthermore lack the transparency that characterizes open judicial dispute resolution processes. Alternative dispute resolution processes have the potential to divert disputes in which there may be a public interest from treatment in a public forum and may lead to outcomes that are inconsistent with or contrary to the public interest.

As a result of these aspects of alternative dispute resolution, the circumstances in which such processes are recommended as appropriate alternatives to litigation are limited. Alternative

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127 Canadian Bar Association, online: National Alternative Dispute Resolution Section <http://www.cba.org/CBA/sections_Adr/main/>.


130 *Ibid*.

131 *Ibid*.

132 *Ibid*.

133 *Ibid*.
dispute resolution is generally not recommended for disputes that implicate the interpretation of legal principles. It is further generally not recommended for disputes that raise novel legal issues or in which there is otherwise a broader public interest. Proponents of alternative dispute resolution emphasize that, as voluntary alternatives to litigation, alternative dispute resolution processes need not and do not exclude or preclude litigation.\(^{134}\) Parties to a dispute may terminate an alternative dispute resolution process at any time and remain free to make resort to available adjudicative processes to resolve their dispute.\(^{135}\)

**Mediation**

Mediation is a prime example of alternative dispute resolution. It is defined in Black’s Law Dictionary as, “A method of non-binding dispute resolution involving a neutral third party who tries to help the disputing parties reach a mutually agreeable solution.”\(^{136}\) Mediation is a voluntary, collaborative and cooperative process to achieve dispute resolution.\(^{137}\) Its key objective is to arrive at dispute resolutions that parties mutually understand and voluntarily accept.\(^{138}\)

The mediator plays a defining role in the mediation process.\(^{139}\) The mediator, a neutral third party, has no power to determine the outcome of disputes, but rather facilitates the parties through the dispute resolution process.\(^{140}\) By this it is meant that, through a combination of facilitative and evaluative strategies, the mediator works to bring the parties to a common

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134 *Supra* note 123 at 62.
136 *Black’s Law Dictionary, 8th ed., sub verbo, “mediation”.*
139 *Ibid.* See also *supra* note 137.
140 *Supra* note 138.
understanding of the facts and issues in order that the parties may reach consensus to form their own resolutions or settlements.\textsuperscript{141}

Mediation may be facilitative, evaluative, or a combination of these.\textsuperscript{142} During facilitative mediation, the role of the mediator is to facilitate successful communication between the parties in order to achieve clarity, define issues, manage conflict and develop mutual understanding and consensus between the parties.\textsuperscript{143} During evaluative mediation, the mediator provides objective yet evaluative feedback to the parties based on his or her informed and educated view of the legal or other merits of the dispute.\textsuperscript{144} Such feedback is intended to assist the disputants to come to an agreement and does not interfere with the neutral, non-adjudicative, role the mediator otherwise plays.\textsuperscript{145} When the mediation process is successful, parties reach their own resolution and litigation is avoided.

Mediation offers both quantitative and qualitative benefits over adversarial processes. It is regularly observed to take less time and to cost less money than litigation.\textsuperscript{146} It is also credited with the potential, when successful, to preserve and even improve relationships between disputants.\textsuperscript{147} As a result of this latter feature, mediation is recommended as a particularly advantageous dispute resolution strategy in contexts where disputants are expected or required to

\begin{small}
\textsuperscript{141} Ibid.
\textsuperscript{142} Supra note 138. See also Cheryl Picard, \textit{The Many Meanings of Mediation: A Sociological Study of Mediation in Canada} (PhD Thesis, Carleton University, 2000) at 45, online: Carleton University <http://www1.carleton.ca/law/people/cheryl-picard>.
\textsuperscript{143} Ibid.
\textsuperscript{144} Ibid.
\textsuperscript{145} Ibid.
\textsuperscript{146} Ibid.
\end{small}
productively continue their interactions post-dispute. Such dispute contexts include family, employment, corporate and commercial, and estate law contexts. 148

Indeed, according to some mediation experts, “relationship transformation” is not only a potential positive by-product of mediation, but it is one of its core objectives. 149 Whether relationship preservation and improvement is a spontaneous by-product or an explicit objective of mediation, the explanatory theory is same. Because it relies for its success upon cooperation, open communication and the development of common ground, mediation naturally has better potential than adversarial processes to preserve and improve relationships between disputants. 150 Mediation further lends itself toward facilitating this outcome by providing disputants with models of communication and dispute resolutions that they may attempt to emulate on their own in the event of future disputes. 151 As a relatively more informal and out-of-court process, mediation also invokes less anxiety and tension for disputants which may assist to deescalate high tensions and emotions that often accompany serious disputes. 152

Mediation is offered as part of the dispute resolution framework in a wide variety of public dispute contexts in Canada. 153 The Government of Canada has studied and evaluated mediation for resolving a variety of disputes. 154 A meta-analysis published by the Department of Justice found that mediation makes a demonstrable improvement in time savings, cost savings, and in disputants’ perceptions of both time and cost savings. 155 Mediation is offered by the Public Service Staffing Tribunal, the Public Service Labour Relations Board and Agriculture and

148 Ibid.
149 Ibid. See Law Commission of Canada at 106; Bush and Folger at 81.
150 Ibid. See also supra note 137 at 21.
151 Supra note 147.
152 Supra note 138; supra note 147.
153 For a detailed review, see Law Commission of Canada, supra note 147 at 95.
155 Ibid at v and 25.
Agri-Food Canada.\textsuperscript{156} The Federal Mediation and Conciliation Service provides grievance mediation services to the federal Labour Program.\textsuperscript{157} Mediation is also available for resolving unjust dismissal disputes arising under Part III of the Canada Labour Code.\textsuperscript{158}

While, as described above, mediation is available and encouraged in Canada as a strategy for resolving a variety of public sector disputes, it has yet to be embraced as a viable alternative or complementary strategy for resolving Canadian tax disputes. Concurrent with the introduction of the Appeals Renewal Initiative, the Agency announced that it would undertake efforts to explore the compatibility of alternative dispute resolution processes with the notice of objection procedure.\textsuperscript{159} However, in 1998, the Auditor General of Canada appeared to attenuate the Agency’s interest in alternative dispute resolution when it recommended that the Agency “proceed slowly”.\textsuperscript{160} It furthermore urged “caution” around the use of alternative dispute resolution and highlighted its potential to “… disturb a relatively well-functioning appeals system.”\textsuperscript{161} In 2004, the Auditor General of Canada observed that, “The Agency has discussed using mediation for several years, but appeals officers and taxpayers have seldom used it.”\textsuperscript{162} Since then, “little support or initiative from the [Agency] or the Federal Department of Finance” in mediation has been forthcoming.\textsuperscript{163}

\textsuperscript{156} Public Service Staffing Tribunal, online: Public Service Staffing Tribunal < http://www.psst-tdfp.gc.ca/article.asp?id=4424>; Public Service Labour Relations Board, online: Public Service Labour Relations Board <http://pslrb-crtfp.gc.ca/mediation/intro_e.asp>; Agriculture and Agri-Food Canada, online: Farm Debt Mediation Service <http://www.agr.gc.ca/eng/?id=1279223072999>.\textsuperscript{157}Preventive Mediation, online: Labour Program <http://www.labour.gc.ca/eng/relations/pubs_rel/preventive.shtml>.\textsuperscript{158} Canada Labour Code, RSC 1985, c L-2. See also Unjust Dismissal – Mediation Process, online: Labour Program: < http://www.labour.gc.ca/eng/standards_equity/st/pubs_st/mediation.shtml>.\textsuperscript{159} Supra note 43.\textsuperscript{160} Supra note 31 at 5.85-5.86.\textsuperscript{161} Ibid.\textsuperscript{162} Supra note 12 at 6.29.\textsuperscript{163} Supra note 53 at 11.
In contrast, mediation of tax disputes has come to be recognized by the Agency’s peers in other jurisdictions as an effective strategy for resolving tax disputes.\textsuperscript{164} The positive results observed with tax mediation in countries that have actively pursued it demonstrate that the benefits of mediation in other dispute contexts are relevant to and efficacious in the context of tax disputes. So too are the features of mediation that are responsible for its potential to preserve and improve working relationships between disputants. The remainder of this chapter advances these claims in more detail. It surveys the experiences of the United States, the United Kingdom, and Australia with mediation of tax disputes. It concludes by advancing the thesis that mediation has a role to play in tax dispute resolution in Canada.

**Mediation of Tax Disputes: The International Experience**

As set out below, mediation of tax disputes is recognized as a worthwhile alternative and complement to the otherwise purely adjudicative tax dispute resolution processes offered by the revenue bodies of the United States (IRS), the United Kingdom (HMRC) and Australia (ATO). Among these, the IRS boasts the most well-established and comprehensive alternative dispute resolution program that includes several now well-established mediation options. HMRC and the ATO have also implemented substantial alternative dispute resolution programs in which mediation plays a significant role. Of the three, the ATO has perhaps most enthusiastically embraced alternative dispute resolution, having committed to effecting a “culture change” in its dispute resolution process which includes exploring the use of consent-based dispute resolution strategies first before turning to other strategies for resolving most taxpayer disputes.

\textsuperscript{164} Supra note 1.
United States of America

In the United States, the IRS has implemented what has been described as one of the “most mature” alternative dispute resolution programs in the world for resolving tax disputes.\(^{165}\) The alternative dispute resolution options available for resolving tax disputes in the United States are comprehensive and include a variety of agreement-based procedures other than mediation.\(^ {166}\) The alternative dispute resolution options administered by the IRS are offered at a variety of points in the lifespan of tax disputes. Alternative dispute resolution is available at the very earliest audit stages and even in cases where disputes have not yet arisen but are merely anticipated.\(^ {167}\) Alternative dispute resolution is also available for the most mature disputes that have made their way through the internal appeal processes of the IRS but for which satisfactory resolution remains elusive.\(^ {168}\)

Among the alternative dispute resolution programs available with the IRS, mediation figures prominently. Mediation of tax disputes with the IRS has been described as “mainstream”, invoking the idea that mediation of tax disputes in the United States might no longer accurately be described as “alternative”.\(^ {169}\) The IRS administers three key mediation programs: the “Fast Track Settlement” (“FTS”) program for large and small business, the “Fast Track Mediation” (“FTM”) program for small business and the “Post Appeals Mediation” (“PAM”) program.\(^ {170}\) The FTS and FTM programs are designed to provide taxpayers with early access to mediation to resolve disputes that arise during the IRS’s audit or review of the taxpayer.\(^ {171}\) In contrast, the PAM program is designed to resolve mature tax disputes that have progressed through the

\(^{165}\) Supra note 1 at 52. See also Melinda Jone and Andrew J Maples, “Mediation as an alternative option in australia’s tax disputes resolution procedures” (2012) 27 ATF 525 at 527.

\(^{166}\) Supra note 1 at 52.

\(^{167}\) Ibid.

\(^{168}\) Ibid.

\(^{169}\) Supra note 53 at 12.


\(^{171}\) Ibid.
internal dispute resolution processes administered by the IRS but that have for some reason failed to resolve.\textsuperscript{172}

The FTS and FTM programs are considered successful by the IRS for what appears to be one key reason: they save time.\textsuperscript{173} The improved efficiency of the FTS program over the \textit{status quo} adjudicative dispute resolution process was quickly noted by internal IRS evaluations of the program. Piloted during the late 1990s and early 2000s, by 2003 the IRS credited the FTS program with materially reducing the average time to resolve a tax dispute from a period of several months to a period of approximately 40 days.\textsuperscript{174} In the same year, the IRS announced that it would make the FTS program permanent.\textsuperscript{175} Today, the FTS and FTM programs continue to be offered by the IRS as dispute resolution options for which the primary benefit to taxpayers is “expedite[d] case resolution.”\textsuperscript{176}

The purpose of the PAM program, in contrast to FTS and FTM, is to address mature tax disputes.\textsuperscript{177} As a facilitative mediation program, PAM involves the appointment of a mediator who leads the IRS and the taxpayer through a facilitative process designed to break the impasse between the two.\textsuperscript{178} The process encompasses classic features of mediation. It is voluntary, non-binding, can be terminated by either party at any time.\textsuperscript{179} Its goal is to bring the IRS and the taxpayer to a mutually agreed resolution of the dispute.\textsuperscript{180} Though the program is available only for mature tax disputes, a key determinant of the program’s success from the perspective of the

\begin{footnotes}
\textsuperscript{172} \textit{Ibid.}
\textsuperscript{173} \textit{Ibid.}
\textsuperscript{174} “Fast-track mediation for small companies,” \textit{The Kiplinger Letter} (3 July 2003) 1.
\textsuperscript{175} \textit{Ibid.}
\textsuperscript{176} \textit{Supra} note 170.
\textsuperscript{177} \textit{Ibid.}
\textsuperscript{179} \textit{Ibid.}
\textsuperscript{180} \textit{Ibid.}
\end{footnotes}
IRS is its ability to reduce the time it takes to achieve resolution of disputes.\textsuperscript{181} In particular, the program is credited with preventing tax disputes from maturing further and allowing the parties to “... avoid [the] long drawn-out litigation” that might otherwise ensue.\textsuperscript{182}

**The United Kingdom**

Until recently, HMRC was reputed to be reluctant to consider mediation of tax disputes.\textsuperscript{183} Thus, it is in contrast to the maturity of the alternative dispute resolution programs made available by the IRS that HMRC has much more recently explored mediation for tax disputes.\textsuperscript{184} Between 2010 and 2013, HMRC piloted alternative dispute resolution programs for both large and complex cases and for individuals and small and medium sized businesses.\textsuperscript{185} In particular, HMRC piloted mediation and facilitation as strategies to resolve tax disputes using neutral third-parties as mediators and facilitators.\textsuperscript{186} As a result of its pilots, HMRC now embraces mediation as a strategy for resolving individuals’ tax disputes as well as those of small and medium sized business.\textsuperscript{187} HMRC somewhat more cautiously supports mediation for large and complex cases.\textsuperscript{188}

Following the completion of its pilot projects, HMRC evaluated the viability of tax mediation and made several key observations.\textsuperscript{189} First, it noted that both pilot programs revealed

\textsuperscript{181} Ibid.
\textsuperscript{182} Ibid at 7.
\textsuperscript{183} Jonathan Fisher, QC and Kate Balmer, “Mediation in Larger Scale Tax Cases” (2011) 1099 Tax J. 8 at 1.
\textsuperscript{185} Ibid.
\textsuperscript{186} Ibid.
\textsuperscript{187} Ibid.
\textsuperscript{188} Ibid.
\textsuperscript{189} Ibid.
mediation to be an effective strategy for bringing to a successful resolution tax disputes in which
an impasse had been reached. 190 HMRC also observed that mediation provides measurable time
and cost savings for tax disputes of individuals and small to medium sized businesses. 191 Indeed,
for individuals and small to medium sized business, HMRC credited mediation with bringing
disputes that, at the time of the pilot, were of an average age between 8 and 23 months, to
resolution in a much shorter 61 days. 192 For large and complex cases, HMRC was more reserved
in its evaluation of the time and cost savings. It noted that “quantification” of the time and costs
savings was “difficult” to calculate, but that, “[q]ualitatively, HMRC are confident that they have
made significant savings in both cost and time in resolving disputes through the alternative
dispute resolution process for both HMRC and the customer.” 193

HMRC also noted several qualitative benefits that mediation brings to the dispute
resolution process. It found that, even when alternative dispute resolution fails to achieve
mutually acceptable resolutions to disputes, it assists with narrowing issues, creating improved
working relationships with taxpayers, and with revealing information gaps and factual
misunderstandings. 194 For these reasons, HMRC credits mediation with adding value to the
dispute resolution process by, at the very least, better preparing the parties for potential future
hearings. 195 For these reasons, HMRC concluded that mediation of tax disputes is a worthwhile
addition to the tax dispute resolution process even when it fails to achieve resolutions. 196

190 Ibid. See Large or Complex at 6-8; SME and Individual at 6-8.
191 SME and Individual supra note 184.
192 Ibid at 6.
193 Large and Complex supra note 184 at 6.
194 Supra note 184.
195 HM Revenue & Customs, “Resolving Tax Disputes: Practical Guidance for HMRC Staff on the Use of
Alternative Dispute Resolution in Large or Complex Cases” online: HM Revenue & Customs
196 Ibid. See also supra note 184.
Following these observations, HMRC has decided to make alternative dispute resolution a permanent part of its dispute resolution process.\textsuperscript{197} Though it has more cautiously evaluated alternative dispute resolution for large and complex cases, stating merely that, for these cases, alternative dispute resolution “... is a useful tool in resolving entrenched disputes,” it has chosen to move forward with alternative dispute resolution for individuals and small and medium enterprises.\textsuperscript{198} It is, accordingly, implementing permanent alternative dispute resolution options alongside its otherwise purely adjudicative dispute resolution process. In the words of HMRC, alternative dispute resolution is the “final piece” in a “dispute resolution jigsaw” that in the United Kingdom, like Canada, otherwise contains purely adjudicative dispute resolution processes.\textsuperscript{199}

**Australia**

Whereas the IRS has embraced mediation for the measurable time and costs savings it provides and HMRC has just begun to explore the direct benefits of mediation, Australia’s ATO has embraced alternative dispute resolution (including -- in addition to mediation – negotiation, case conferencing, conciliation, and neutral evaluation) for the strategic role that it can play in transforming the culture of tax dispute resolution.\textsuperscript{200} In 2010, two years after the release of the OECD’s recommendation to revenue bodies to explore enhanced relationship approaches, Ernst

\textsuperscript{197} Supra note 184.
\textsuperscript{198} Large or Complex, supra note 184 at 8; SME and Individual, supra note 184 at 8.
\textsuperscript{199} SME and Individual, supra note 184 at 3.
& Young published a summary of the “dispute resolution shift” in Australia, characterizing it as nothing less than a “radical change in mindset for the authorities.”

Indeed, following observations that the use of alternative dispute resolution by the ATO was somewhat haphazard and inconsistently used, Australia’s Commission of Taxation requested that the Inspector-General of Taxation (IGT) conduct a comprehensive review to ensure a more consistent approach. The resulting report, released in May 2012 observed that, the ATO aims, at a high level, to implement dispute resolution strategies that will “…drive a cultural shift towards an earlier and better resolution culture.” It acknowledged alternative dispute resolution as a “useful vehicle for narrowing issues in dispute, clarifying evidence, and fostering ongoing relationships,” but also took note of its potential to play a role “… in a much wider context.” The report recommended that in order to fully unlock the benefits of alternative dispute resolution, the ATO should inter alia, “… bring ADR … to the forefront as the primary dispute resolution mechanism, rather than as an alternative.” It recommended that “… the ATO’s starting position should be that it is appropriate to engage in ADR … unless there are clear reasons to the contrary.”

The ATO has taken steps to fulfill these recommendations. Following the release of the IGT’s report, the ATO released Practice Statement PS LA 2013/3, “Alternative Dispute Resolution (ADR) in ATO Disputes,” setting out the guidelines and principles that define its

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201 Supra note 1 at 20.
202 Supra note 165 at 540.
204 Ibid.
205 Ibid.
206 Ibid.
approach to alternative dispute resolution. The practice statement confirms the ATO’s commitment to resolving disputes using strategies that are simple, cost-effective, and that provide early resolution of disputes. It also set out the ATO’s commitment to play a proactive role in identifying tax disputes that make suitable candidates for alternative dispute resolution, to initiate discussions with objecting taxpayers about the use of alternative dispute resolution in such cases, and to explain to objecting taxpayers the available processes so that they may make informed decisions.

Far more so than that of the IRS and HMRC, the ATO’s public website also reflects its deep commitment to bring alternative dispute resolution forward as a primary dispute resolution strategy. Its dispute resolution policy, available online, provides:

[Our policies] reflect our intention to continue the shift away from adversarial processes, such as litigation, to resolve disputes. We prefer to work with you to resolve disputes directly, as early and cooperatively as possible. We believe this approach provides time and cost savings for you, the broader community and the government.

It provides further: “We aim to promote a resolution culture based on all of the following: effective communication, genuine engagement, collaboration, and strategies that are fair and proportionate to the matters in dispute and lead to early resolution at minimal cost.”

The goals of the ATO to bring about a culture change in its approach to dispute resolution and its efforts to make those goals a reality are recent developments. Accordingly, there is little available in the way of reliable or observable results to evaluate the effectiveness of the approach or the means through which the ATO seeks to achieve it. Suffice it to say here that the ATO is at

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208 Ibid.  
209 Ibid.  
211 Ibid.
the cutting edge of tax administration and that all interested eyes are waiting to discover how its experiment with alternative dispute resolution will turn out. Based on all available information as so far discussed in this paper, it in any event appears that there is nothing to lose by trying.

Mediation of Canadian Tax Disputes: Addressing the Agency’s Challenges

Tonya Scherer wrote that the “… success of mediation in other forums foreshadows the success of mediation in the tax arena.” 212 Bearing out the prediction, the experiences with tax mediation in the United States, the United Kingdom and Australia as described above provide reasons to believe that the benefits of mediation observed in non-tax dispute contexts to be relevant to and efficacious in tax dispute contexts. It is therefore advanced here, *a fortiori*, that the success of mediation in other tax forums foreshadows its success in the Canadian tax arena. As advanced in this final section of this chapter, the international experience with tax mediation suggests its potential to ameliorate the specific deficiencies observed in the notice of objection procedure as detailed in Chapter 1 as well as its potential to play a role in the transformation of the relationship paradigm between the Agency and Canadian taxpayers from basic to enhanced.

Improving Timeliness

As detailed in Chapter 1, improving the timeliness of the notice of objection procedure remains a significant challenge for the Agency. The Agency currently administers a dispute resolution process that, by a “large margin,” takes longer to resolve tax disputes than the 90 days

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after which taxpayers become entitled to appeal directly to the Tax Court. As revealed by the discussion in this chapter, mediation demonstrates the specific potential to reduce the time it takes to achieve tax dispute resolution. The experiences of the IRS and HMRC in particular confirm that mediation reduces the time it takes to achieve tax dispute resolution through status quo adjudicative procedures; it has successfully reduced the time to achieve tax dispute resolution from average periods of 9 to 24 months to average periods of less than 3 months. There is no clear reason to be skeptical that mediation cannot achieve the same improvements in timeliness in Canada.

**Improving Communication and Information Exchange**

As described in Chapter 1, achieving high quality communication and information exchange in the dispute resolution process also remains a significant challenge for the Agency. Signs of substandard communication and information exchange are witnessed in the experiences of self-represented litigants in the Tax Court of Canada and in the rates of out-of-court settlement and withdrawal of appeals. As revealed by the discussion in this chapter, mediation of tax disputes demonstrates a specific potential to improve communication and information exchange in a manner that would directly address these manifestations of lower quality communication and transparency.

In particular, the experience of the HMRC confirm the ability of mediation to facilitate openness and communication between revenue bodies and taxpayers. HMRC found that even when mediation fails to achieve dispute resolution, it improves the parties’ comprehension of the factual and legal issues and better prepares them for success in a judicial forum. This feature of mediation in the tax context has the potential to directly address aspects of the difficulties faced

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213 *Supra* note 12 at 6.31-6.33.
by self-represented litigants in the Tax Court of Canada. The experiences of the IRS and HMRC also confirm the ability of mediation to facilitate the conclusion of long standing tax disputes and to prevent disputes from maturing into litigation in a judicial forum. By facilitating resolution of tax disputes before they escalate into judicial forums, this feature of mediation in the tax context has the potential to directly address aspects of the case-flow management issues faced by the Tax Court of Canada. All signs from the IRS and HMRC indicate that mediation is preferable to status quo dispute resolution for achieving greater levels of communication, information exchange and transparency. There is no clear reason to be skeptical that this same improvement cannot be achieved in Canada through mediation of Canadian tax disputes.

Facilitating Relationship Transformation

This chapter is not complete without a discussion of the role mediation can play in the Agency’s broader goal to transform its relationship with Canadian taxpayers by implementing a relationship-based approach to administration and enforcement. As set out in the previous chapter, current theorizing on best-practices for tax administration posit that low quality communication and information exchange has a potentially significant if indirect negative effect on the efficacy and efficiency of tax administration and enforcement. For the Agency, this means that there is an even greater incentive to work toward achieving better quality communication and information exchange during the dispute resolution process. Because the Agency and Canadian taxpayers become most entangled with each other during the dispute resolution process, it is here where achieving better quality communication and information exchange may provide the most bang for buck when it comes to implementing strategies to achieve the broader goal of creating an enhanced relationship between the Agency and Canadian taxpayers.
Mediation, as a form of dispute resolution that relies for its success specifically upon facilitating open communication and information exchange demonstrates potential superior to the Agency’s status quo dispute resolution process to play a strategic role achieving this relationship transformation.

As discussed in Chapter 1, in non-tax dispute contexts, mediation is credited with facilitating improved relationships, sometimes described as relationship transformation, as a result of its reliance upon facilitating communication, open dialogue, mutual understanding, and information exchange. For this reason, mediation is recommended as a particularly suitable form of dispute resolution in circumstances where disputants are expected or required to remain in a positive working relationship, as certainly revenue bodies and taxpayers are required to do. It stands to reason that mediation of tax disputes may achieve similar results in the tax arena, thus valuably contributing not only to the project of creating a more communicative and transparent dispute resolution process for its own sake but also to the broader project of transforming the relationship paradigm between revenue bodies and taxpayers.

While this idea is timely given recent focus on the quality of the relationship between revenue bodies and taxpayers, this idea is not new, not even in Canada. For example, in his discussion of tax mediation in Canada, Chris Jaglowitz opined that:

… the qualities of mediation are such that perhaps both taxpayer and assessment officer alike may undergo something of a transformation, as described by Bush and Folger. Specifically, the experience may allow each party to better relate to the other, which may help break down the stereotypes each holds of the other, and to make transactions between them more personalized than the age-old "taxpayer versus tax collector" and vice versa. Though perhaps overly idealistic in the case of income tax disputes, the transformative view of mediation is an attractive one.\(^{214}\)

\(^{214}\) Supra note 113 at 9.
The OECD has additionally recognized the potentially strategic role that mediation and other forms of alternative dispute resolution can play in achieving a paradigm shift in the relationship between revenue bodies and taxpayers. It writes:

Litigation is often a hostile and adversarial process which, by its very nature, can only have one ‘winner’. It can involve conflicts of evidence and processes of examination that, while not intended to do so, can undermine any trust and goodwill that exists between the parties. Consent-based ADR, by contrast, is a form of dispute resolution that is based fundamentally on consensus, which, in turn, often provides a better basis upon which the parties can continue their relationship.215

Mediation, therefore, may not only improve communication and information exchange for its own sake, but it may assist to facilitate the transformation of the relationship between the revenue body, the Agency, and Canadian taxpayers from basic to enhanced. There is no clear reason in any event to suggest that the thesis is not worth testing. In this regard, it is advanced here that the Agency consider following the ATO’s bold lead and consider mediation not only for its direct benefits but for its capacity to set the stage for achieving the desired shift in the relationship paradigm between the Agency and Canadian taxpayers.

215 Supra note 5 at 74.
CHAPTER 3

Introduction

This paper has set out to evaluate mediation as a potential alternative strategy for resolving Canadian tax disputes with the Agency using the ACUS framework applied by Deen Olsen in her earlier evaluation of the same. Chapter 1 examined the existing notice of objection procedure for resolving Canadian tax disputes and the Agency’s current approach to administering the dispute resolution process. It surveyed the causes and consequences of two key problem areas: its lack of timeliness and its failure to achieve high quality communication and information exchange. Chapter 2 examined mediation as a dispute resolution process suitable to address these challenges. It surveyed the advantages of mediation and, based upon the real-world experience with tax mediation in the United States, United Kingdom, and Australia, argued that mediation has the potential to address the specific challenges facing the Agency’s dispute resolution process. In connection with this discussion, this paper also discussed the strategic role that mediation can play in the Agency’s mission to achieve a more efficient, relationship-based, approach to administration and enforcement by facilitating the transformation of the relationship between the Agency’s and Canadian taxpayers from basic to enhanced.

This final chapter examines the two remaining ACUS factors for evaluating the viability of alternative dispute resolution programs in the public sector: (i) the legal constraints under which the Minister and the Agency operate that may limit the availability of mediation; and (ii) the tax disputes that mediation is, as a result, both well- and ill-suited to resolve. This chapter argues that notwithstanding legal constraints that limit the range of acceptable tax dispute resolutions the Minister and the Agency may entertain and accept, there remains plenty of scope in the Canadian context for mediation as a viable alternative dispute resolution strategy. Indeed,
the legal constraints under which the Minister and the Agency operate may assist to prevent use of tax mediation in circumstances where mediation would, in any event, not be ideally recommended. Finally, within these constraints, several common types of Canadian tax disputes are well-suited to resolution by mediation. The next section concludes.

**The Constraints**

The key constraint under which the Minister and the Agency operate relevant to evaluating the viability of mediation of Canadian tax disputes results from the legal principle that the Minister, and the Agency as its proxy, is permitted to assess tax only in accordance with the facts and laws as they are understood.\(^{216}\) This rule limits the type of dispute resolutions the Minister may accept.\(^ {217}\) However, it is does not prohibit the use of mediation as a dispute resolution strategy or process.\(^ {218}\) Ample scope remains for mediation as a process to resolve several common types of Canadian tax disputes.

**Assessment in Accordance with Facts and Law**

The Minister may not arbitrarily assess tax.\(^ {219}\) This principle is reflected and quite firmly entrenched in the Canadian common law of taxation.\(^ {220}\) Tax jurisprudence observes that Minister “has a statutory duty to assess the amount of tax payable on the facts as he finds them in accordance with the law as he understands it.”\(^ {221}\) It follows that, when resolving taxpayers’ objections, the Minister is permitted to resolve tax disputes only by applying the law as he

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\(^{216}\) *Supra* note 23.

\(^{217}\) *Ibid.*

\(^{218}\) *Supra* note 5 at 5-7, 15-19.

\(^{219}\) *Supra* note 23.

\(^{220}\) *Ibid.*

\(^{221}\) *Galway, supra* note 23.
understands it to the facts as he understands him while taking into account no other considerations, neither those of his own nor those of taxpayers.222

This rule limits the kinds of out-of-court tax dispute outcomes the Minister may accept.223 Specifically, this rule implies that the Minister may not settle tax debts on a compromise basis but may only settle tax disputes where the settlements comply with the Minister’s duty to assess in accordance with the known facts and applicable laws.224 This rule was recently considered and applied by the Federal Court of Appeal in CIBC World Markets Inc. v. Canada.225 In this case, the primary issue was the extent of the Minister’s ability to settle tax disputes out of court.226 The issue arose from the appellant’s motion for enhanced or substantial indemnity costs following the Minister’s earlier rejection of its offer to settle its appeal.227 Earlier in the litigation process, the taxpayer had offered to the Minister that the appeal be settled without judicial intervention in favour of the taxpayer based upon a 90-10 split of the taxes in dispute.228 The Minister rejected the offer and the matter proceeded to adjudication in the Tax Court of Canada and the Federal Court of Appeal.229 In the result, the taxpayer was made whole and the disputed assessment was vacated in its entirety.230

Although the taxpayer obtained a more favourable adjudicated outcome than the outcome it would have enjoyed had the Minister accepted the terms of the settlement offer, the Federal Court of Appeal denied the taxpayer’s motion for substantial indemnity costs.231 It came to this conclusion on the basis of its finding that the Minister could not have accepted the taxpayer’s

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222 Supra note 23 at 5-7, 15-19.
223 Supra note 113 at 4-6.
224 Ibid. Supra note 6 at 5-7, 15-19.
225 CIBC World Markets Inc, supra note 23.
226 Ibid.
227 Ibid.
228 Ibid.
229 Ibid.
230 Ibid. See also CIBC World Markets Inc. v Canada, 2011 FCA 270, 2011 FCA 270 (Canlii).
231 Ibid.
offer. In particular, it found that the appeal raised issues of statutory interpretation that could only have been resolved on a binary all-or-nothing basis. The Federal Court of Appeal accordingly found that the taxpayer’s offer reflected, not a principled settlement, but an arbitrary compromise of the taxes in dispute. In other words, there was no basis in fact or law to support it. Because the offer provided no factual or legal basis upon which the Minister could assess, the Minister simply could not accept the offer for, accepting it would have violated the principle that the Minister may not arbitrarily assess tax. In the words of the Federal Court of Appeal, the Minister was subject to a “legal disability” to accept the offer. It furthermore held that any "... agreement whereby the Minister would agree to assess ... tax otherwise [than] in accordance with the law would [...] be an illegal agreement.”

The decision of the Federal Court of Appeal in CIBC World Markets provides recent judicial confirmation that the Minister’s inability to assess tax except in accordance with the facts and law means that the Minister may not, for the purpose of resolving tax disputes either out-of-court or during the notice of objection phase, purely negotiate or split-the-difference with objecting taxpayers. However, the Minister’s participation in mediation as a dispute resolution strategy is not thereby also put beyond the scope of the Minister’s or Agency’s legal capabilities. The rule that the Minister may only assess tax in accordance with the facts and laws as they are understood is not equivalent to a limit on the Minister’s ability to participate in mediation. As discussed in Chapter 2, the universe of outcomes that may be obtained through mediation is the universe of consent-based resolutions voluntarily and mutually by the parties. It is otherwise limitless and includes principled settlements as well as purely negotiated or

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232 Ibid.
233 Ibid.
234 Ibid at 37.
235 Supra note 113 at 4-6. Supra note 6 at 5-9, 15-19.
236 Ibid.
otherwise arbitrary settlements. Other than the requirement that mediation result in consent-based outcomes (or no outcomes at all), mediation is indifferent to the nature of the outcomes achieved and is thus compatible with the constraints that limit the Minister to principled settlements.

In fact, for the purpose of proposing mediation as a viable alternative strategy for resolving Canadian tax disputes, the limit on the Minister with respect to principled settlements assists to address some of the more general concerns about alternative dispute resolution discussed in Chapter 2. The private nature of alternative dispute resolution gives rise to concerns that it is not ideally suited for disputes that turn on the interpretation of legal principles or that raise novel legal questions. However, when it comes to resolving Canadian tax disputes, in the event that underlying issues turn on genuine disputes about the legal principles or how they apply to given circumstances, the rule that the Minister may only accept principled settlements or resolutions at the notice of objection stage impairs the Minister from privately settling such disputes in any event (unless disputing taxpayers abandon the matter.) The private nature of alternative dispute resolution also gives rise to concerns that alternative dispute resolution processes do not necessarily lead, as judicial or adjudicative processes are intended, to legally normative outcomes. Again, the rule that the Minister may only accept principled out-of-court settlements or resolutions at the notice of objection phase assists to address this concern. Although the rule provides no guarantee that the Minister and objecting taxpayers will, after engaging in mediation, consistently or even ever arrive at dispute resolutions that reflect what otherwise would or might have been judicially determined by the Tax Court of Canada, the rule nonetheless makes it less likely than it might otherwise be that mediated tax dispute outcomes will fall out of bounds of a range of reasonably possible judicial outcomes. At the very least, this
rule ensures that there is no greater likelihood that mediated tax dispute outcomes will fall outside a reasonable range of such outcomes any more than those outcomes determined through the Agency’s current notice of objection process. Finally, the private nature of alternative dispute resolution gives rise to concerns about its transparency the consistency of the outcomes achieves with public interest. The rule prohibiting the Minister from assessing otherwise than in accordance with the facts and law as they are understood ensures that by participating in mediation there is no greater likelihood than there already is in the current dispute resolution process that dispute outcomes will fail to be consistent with public interest concerns.

**Tax Disputes Ill-Suited to Mediation**

Tax disputes ill-suited to mediation include those that would require the Minister to settle on any basis other than a principled basis and those disputes that are in any event not ideal candidates for alternative dispute resolution as discussed above and in Chapter 2. Olsen enumerates some examples. She writes:

… cases may necessitate proceeding to a hearing in the courts where resolution of the issue is required for precedential value, the matter involves significant questions of government policy, there is a need for consistent treatment among taxpayers, or a full record of the proceeding is important from a public policy perspective.\textsuperscript{237}

Guidelines published by the ATO pick up on similar themes in setting out principles for distinguishing tax disputes that are candidates for alternative dispute resolution from those that are not. The ATO considers alternative dispute resolution may not be appropriate where

(i) parties are in agreement as to the facts and the dispute turns on genuine and fundamental issues of law;

(ii) there is a clearly identified public benefit in having the matter judicially determined; or

\textsuperscript{237} Supra note 6 at 19.
there is a genuinely held concern that it is not appropriate to engage in dispute resolution such as in cases of serious criminal fraud or evasion.\textsuperscript{238}

Richard Fayle has also identified features of tax disputes that may indicate lack of suitability for mediation.\textsuperscript{239} The features identified by Fayle focus on disputes in which there really is no dispute.\textsuperscript{240} Tax disputes identified by Fayle as ill-suited to mediation include disputes in which:

\begin{itemize}
  \item The applicable statutory provisions are unambiguous;
  \item The facts are not disputed;
  \item There exists a direct precedent where the facts are on foot;
  \item There does not exist any conflicting decisions or judgments; and,
  \item The outcome of the dispute is clear.\textsuperscript{241}
\end{itemize}

Guidelines such as these are instructive for delineating the appropriate limits for tax mediation in Canada.

\section*{Tax Disputes Well-Suited to Mediation}

While there are specific types of disputes for which mediation will not be appropriate in the Canadian setting, there is nonetheless a variety of Canadian tax disputes for which mediation will be apt.\textsuperscript{242} As a general observation, mediation will be an appropriate and viable strategy to resolve any dispute the nature of which is factual.\textsuperscript{243} For disputes where a discordant understanding of the facts is the root, there is ample scope for a process facilitated by a mediator

\textsuperscript{238} Supra note 203 at 50.
\textsuperscript{240} Ibid at 100.
\textsuperscript{241} Ibid.
\textsuperscript{242} Supra note 6 at 10.
\textsuperscript{243} Ibid.
the purpose of which is to assist the parties toward developing a unified understanding of the facts.

The Income Tax Act contains a number of provisions the application of which are heavily fact dependent and may be expected to give rise to factual disputes. Following are a few examples. Section 67 provides that “no deduction shall be made in respect of an outlay or expense ... except to the extent that the outlay or expense was reasonable in the circumstances.” Section 68 provides for a deemed reallocation of consideration received by a taxpayer where an amount “... can reasonably be regarded as being in part the consideration for the disposition of a particular property ..., for the provision of particular services ... or for a restrictive covenant.” Provisions such as these lend themselves to dispute of a factual nature to the extent that reasonable people can disagree about what is or is not reasonable. Any dispute turning on determinations of reasonableness are disputes in which mediation may be expected to assist to bring the parties to consensus.

Tax disputes that turn on fair market valuations or pricings of assets and services are also fact dependent. Moreover, they tend to turn on facts about which reasonable people may disagree. Indeed, the Tax Court of Canada noted in Petric v. Her Majesty the Queen that, “Although fair market value is ultimately a question of fact to be resolved by the trier of fact, it is mostly a question of opinion.” Such tax disputes may arise in the context of deemed dispositions. They may also arise in the context of transfer pricing determinations where parties are required to price non arm’s-length transfers of goods and services at comparable

244 *ITA supra* note 9.
245 *Ibid* s 67.
246 *Ibid* s 68.
247 For detailed discussion of the suitability of valuation disputes to resolution by mediation, see IGT *supra* note 203 at 64-66.
248 2006 TCC 306, 60 DTC 3082 at 40.
249 *ITA supra* note 9. See for example ss 70(5), 104(4).
arm’s length prices.\textsuperscript{250} In this regard, valuation disputes represent a category of disputes in which mediation may be expected to assist to bring the parties to a consensus.

The Minister also issues net worth assessments.\textsuperscript{251} Net worth assessments are performed by the Minister when taxpayers fail to maintain adequate books and records or maintain inadequate books and records making it otherwise impossible for the Minister to determine tax liability.\textsuperscript{252} In such circumstances, the Minister will determine tax liability through the net worth assessment method which involves performing a series of estimates and net worth comparisons.\textsuperscript{253} The estimates and other determinations that inform the net worth assessment are based upon a review of the taxpayers’ assets and liabilities, banking records, and other available financial information.\textsuperscript{254} The imprecise nature of the net worth assessment method has been noted by the Tax Court of Canada and, though the method is considered to constitute a method of last resort, it is nonetheless recognized by the Tax Court as an acceptable method of assessment when books and records of the taxpayer are unavailable, non-existent, or otherwise inadequate.\textsuperscript{255}

Mediation may be particularly useful for resolving or narrowing the scope of disagreement generated by net worth assessments.\textsuperscript{256} The internal documentation kept by the Agency to support net worth assessments can be voluminous and unwieldy to review, digest and to dispute.\textsuperscript{257} Consequently, it can be a very inefficient and time consuming exercise for taxpayers to dispute net worth assessments and appeals branch personnel to review and such

\textsuperscript{250} ITA supra note 9 s 247.
\textsuperscript{251} ITA supra note 9 s 152(7).
\textsuperscript{252} Ibid. See also McCarthy v The Queen, 55 DTC 841; [2001] 4 CTC 2480 (TCC); Golden v Her Majesty the Queen, 2009 TCC 396, 2009 TCC 396 (CanLii); 2007 DTC 1647, [2008] 2 CTC 2364 (TCC) (for discussion of net worth assessment method by Tax Court of Canada).
\textsuperscript{253} Ibid.
\textsuperscript{254} Ibid.
\textsuperscript{255} Golden supra note 252 at 17.
\textsuperscript{256} The following observations are made based on the author’s own experience.
\textsuperscript{257} Ibid. Supra note 252.
assessments. Mediation may be especially useful in this context to the extent that it may assist to narrow the scope of the issues while facilitating the taxpayer and the Agency toward arriving at a shared understanding of the facts and issues and toward arriving at a consensus around the outcome. It may also valuably contribute toward providing the Agency with a positive forum in which to educate taxpayers about the requirements for proper book and record keeping.

Finally, mediation may be suitable for tax disputes where objecting taxpayers bear grudges against the Agency’s auditors or reviewers responsible for disputed assessments. For some taxpayers, disputes that arise subsequent to audit and reassessment will not just be about the money. For some taxpayers there will be an emotional element in tax disputes. In recognition of this, Fayle writes:

Another case in point is where the aggrieved taxpayer believes they have been dealt with unfairly, rudely, accused of wrongdoing or the subject of abuse. Such taxpayers are prone to negative attitudes toward the administration, lose faith in the integrity of the taxation system or harbour feelings of anger or distrust. Mediation ought to reveal such attitudes and pave the way to heal the rift once the bridges of understanding have established the basis of misunderstandings and unintended results. While the outcome may have no impact on the revenue it might affect reputations.

In particular, assessments based upon auditors’ determinations of business versus personal amounts, underreported revenues or over-reported expenses may b, rightly or wrongly, perceived by objecting taxpayers to call into question the credibility or trustworthiness of taxpayers’ own determinations. For some taxpayers, this implication may give rise to a dispute that may not truly be resolved in taxpayers’ eyes until any perceived affront is rectified. Mediation presents as an ideal option in such circumstances as it promises to provide a positive forum in which the non-tax aspects of tax disputes can be addressed.

258 Ibid.
259 Supra note 239.
260 Ibid at 100.
CONCLUSION

This paper set out to evaluate mediation as a potential alternative strategy for resolving Canadian tax disputes with the Canada Revenue Agency. The most recent previous consideration of tax mediation in a Canadian context was conducted by Deen Olsen in 1997. While her evaluation found, as this one has, that mediation is compatible with the Minister’s and Agency’s mandates, she nonetheless advised caution against introducing mediation as a measure simply for the sake of change. In contrast, this paper has evaluated tax mediation from the perspective that, in the interim, the tax dispute resolution and administration landscapes in Canada have changed.

In 1997, the Agency introduced with optimism the Appeals Renewal Initiative. This initiative was intended to produce reforms that would measurably and qualitatively improve the dispute resolution process of the Agency, including making it more timely and more apt to produce high quality communication and information exchange. Today, those reforms have proven not to be as effective as once hoped. The Agency continues to struggle to improve its timeliness and to achieve high quality communication in its dispute resolution procedures. Furthermore, in 1997, the Agency did not have the benefit of OECD’s work on the impact that adequate communication and information exchange has on the overall efficiency and efficacy of tax administration and enforcement. The OECD’s work also sheds light on the value of communication and information exchange in a tax administration environment now more than ever characterized by globalization, taxpayer mobility, and taxpayers’ creative and, in some cases, exploitive tax minimization strategies.

It is against this background that this paper highlighted the benefits of mediation and its potential make good on the promise made in other dispute contexts to provide quicker, less expensive, and more communicative tax dispute resolution. Drawing upon the experiences of
the United States, United Kingdom, and Australia with tax mediation, the discussions in this paper have highlighted the potential for mediation to bring its advantages to the Canadian tax dispute resolution process. On the basis of the discussions and arguments above, it is advanced that introducing mediation for resolution of tax disputes constitutes a rational response to the changing tax administration landscape in Canada. It is suggested therefore that mediation be considered once more by the Agency. Only a comprehensive pilot program can test the arguments put forward here.
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