# "EQUITY HAS NO PLACE HERE":[1] SHOULD EQUITABLE REMEDIES BE AVAILABLE TO REVERSE FAILED TAX PLANNING?

Adam Hofri-Winogradow[2]

*I discuss an odd use of equity: the granting of equitable remedies to assist authors of tax minimization plans where their plans result in unexpected tax liabilities. Canadian law has in the current century first taken a strikingly liberal approach to granting rescission and rectification to reverse the tax results of failed, mistake-based tax planning, and later switched to an approach far more restrictive than those under UK and US law. I believe the current Canadian approach to be both too permissive and not permissive enough: given the importance of the tax-and-transfer system for providing equalizing redistribution, and the regressive redistributive effects of tax planning, state-funded courts should in general not grant equitable remedies to authors of tax minimization schemes that have met with unexpected tax burdens as a result of tax mistakes. I recognize, however, that tax mistakes can lead to devastating results for taxpayers, and that such mistakes are to be expected given the complexity of our tax law and our acceptance of tax law changes operating retroactively. I therefore suggest that courts retain a power to grant rescission or rectification, as necessary, to eliminate mistake-based tax planning that will reduce a human taxpayer to insolvency if not eliminated, where such elimination is not realistically available in other ways.*

*L'auteur propose une réflexion sur une pratique peu courante en equity : l'octroi d'un recours visant à aider les auteurs de plans de réduction fiscale qui engendrent des obligations fiscales inattendues. Depuis le début du siècle, le droit canadien a d'abord adopté une approche fortement libérale quant à l'octroi d'annulations et de rectifications visant à corriger les effets de plans fiscaux fondés sur des erreurs et qui ont échoué, avant de se tourner vers une approche beaucoup plus restrictive que ce qu'on voit en droit britannique ou américain. Le droit canadien actuel apparait aujourd'hui*

1 *Canada (Attorney General) v Collins Family Trust*, 2022 SCC 26 at para 7 [*Collins* SCC].

2 Professor, Peter A Allard School of Law, University of British Columbia. I thank David Duff, Dennis Pavlich, Camden Hutchison, Bruce MacDougall, Lionel Smith, Sam Beswick and Jakub Adamski for their comments on an earlier draft of this paper; attendees at a lecture organized by the Centre for Business Law at the Allard School of Law; participants at the Canadian Law of Obligations conference held at the Université de Montréal in October 2024; Yu-Sen (Sam) Zhai for excellent research assistance; the Allard School of Law for generous funding; and the editors and referees for the *Canadian Bar Review*.

*à la fois trop permissif et trop restrictif. Compte tenu du rôle central du système de transferts fiscaux pour assurer une redistribution équitable, et des effets de redistribution rétroactive inhérents à la planification fiscale, les tribunaux financés par l'État devraient généralement se garder d'accorder des recours propres à l'equity aux auteurs de plans de réduction fiscale ayant généré des charges fiscales imprévues à cause d'erreurs fiscales. Il demeure toutefois indéniable que ces erreurs peuvent entraîner des conséquences catastrophiques pour les contribuables, erreurs d'autant plus probables que les lois fiscales sont d'une grande complexité et que les modifications législatives à effet rétroactif sont couramment admises. Par conséquent, il serait approprié que les tribunaux conservent le pouvoir d'accorder une annulation ou une rectification, selon les besoins, pour éliminer les plans fiscaux fondés sur des erreurs pouvant réduire un particulier à l'insolvabilité si rien n'est fait et dans les cas où cette élimination n'est réalisable que par cette voie.*

## Contents



## Introduction

Aristotle said that "[t]he nature of the equitable [is] a rectification of law where law is defective because of its universality."[3] Irit Samet, a more recent scholar, wrote that the characteristic function of the part of the law called equity is promoting correspondence between legal liability and moral duty.[4] Equitable intervention has long been described as a response

[3] Aristotle, *Nicomachean Ethics*, translated by H Rackham (Cambridge, MA: Harvard University Press, 1926) at 317.

[4] Irit Samet, *Equity: Conscience Goes to Market* (Oxford: Oxford University Press, 2018) at 2.

to injustice or unconscionability.[5] As the Supreme Court of Canada noted, "[e]quity, which is concerned with fairness and justice, provides remedies in particular cases where the rigidity of the common law would lead to unconscionable results."[6] Yet equitable remedies are sometimes available in circumstances that may have little to do with correcting injustice. Both in Canada and the UK, rescission and rectification in equity have been used to retroactively eliminate the disappointing results of tax planning gone awry, leaving planners and their clients free to try again to minimize the latter's tax burden.[7] While such use of equity supports the realization of taxpayers' intention to save tax, it undermines the tax-and-transfer system and its redistributive goals. Breaking with this status quo, the Supreme Court of Canada has in *Canada (Attorney General) v Collins Family Trust* largely eliminated such use of equity in Canada, except for rectification of documentation errors.[8] In this essay I ask whether the Supreme Court of Canada was right to so narrow the ambit of Canadian equity. I conclude that rescission and rectification should be available to avoid or amend failed tax plans only where a human taxpayer would be rendered insolvent should those remedies not be granted.

Part one describes the law governing the use of rescission and rectification to retroactively avoid or modify tax planning that was based on an erroneous understanding of applicable tax law, where the tax results of this planning have proven disappointing. Focusing on Canadian law, I include a comparison with UK and US law. Part two provides my view regarding the circumstances under which equitable remedies should be available to avoid or modify such failed tax planning.

## Part I. Using Equitable Remedies to Reverse Failed Tax Planning: the Law

Many Canadian and UK taxpayers have asked the courts to extract them, by way of granting an equitable remedy, from disappointing tax results

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5 See e.g. *Ewing v Orr Ewing* (1883), 9 AC 34 (House of Lords) at 40; James Penner, "Equity, Justice and Conscience: Suitors Behaving Badly?" in Dennis Klimchuk, Irit Samet & Henry E Smith, eds, *Philosophical Foundations of the Law of Equity* (Oxford: Oxford University Press, 2020) 52 at 52.

6 *Jean Coutu Group (PJC) Inc v Canada (Attorney General)*, 2016 SCC 55 at para 46 [*Jean Coutu*].

7 See e.g., in Canada, *Re Pallen Trust*, 2014 BCSC 305, aff'd 2015 BCCA 222 [*Pallen*] (rescission); *Attorney General of Canada v Juliar*, 2000 CanLII 16883 (ONCA) [*Juliar*] (rectification); in England, *Pitt v Holt*, [2013] UKSC 26, [2013] AC 108 (rescission); *Lobler v HMRC*, [2015] UKUT 0152 (TCC) (rectification).

8 *Collins* SCC, *supra* note 1.

they have not expected.[9] Looking at the accumulated corpus of relevant decisions makes clear the courts have fairly often obliged.[10] The key equitable remedies recently awarded to achieve the desired extraction are rescission and rectification. Rescission erases the transactions or arrangements having the regretted tax result; rectification replaces them with alternative transactions or arrangements having a better tax result.

## A) Rectification

Between 2000–2016, Canadian courts have made available a strikingly extended version of this remedy where rectification was sought to revise a transaction having tax results that taxpayers found disappointing. Prior to this extension, rectification could, under *771225 Ontario Inc v Bramco Holdings Co Ltd*, be available to fix the disappointing results of a tax mistake where a taxpayer had a common and continuing intention to achieve or avoid a specific fiscal result, which was not properly expressed in the documents executed.[11] In other words, rectification in the tax planning context operated like it operates in other contexts: to conform documents to parties' intentions, where the documents do not express these intentions correctly.[12] Even this state of the law is strikingly taxpayer- and tax planning-friendly: the courts lend their services, paid for by taxpayers, to relieve taxpayers from the results of errors in the execution of their planning. The planning-friendly motivation behind the courts' use of rectification in this context was made plain in *Re Slocock's Will Trust*, an English decision on which Canadian courts have repeatedly drawn: "[p]arties are entitled to … arrange their affairs to avoid payment of tax if they legitimately can … If a mistake is made in a document legitimately

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9 For examples, additional to those in *supra* note 7, see, in Canada, *Crean v Canada (Attorney General)*, 2019 BCSC 146 [*Crean*]; *5551928 Manitoba Ltd v Canada (Attorney General)*, 2019 BCCA 376 [*5551928 Manitoba*]; *TechnoComm Solutions Inc v Canada (Attorney General)*, 2019 ONSC 924; *Kraft Heinz Canada ULC v Canada (Attorney General)*, 2022 BCSC 796. In England, see *Kennedy v Kennedy*, [2014] EWHC 4129 (Ch); *Van der Merwe v Goldman*, [2016] EWHC 790 (Ch) [*Van der Merwe*]; *Barker v Confiànce Ltd*, [2018] EWHC 2965 (Ch) rev'd on another point; *Glover v Barker*, [2020] EWCA Civ 1112; *Hartogs v Sequent (Schweiz) AG*, [2019] EWHC 1915 (Ch) [*Hartogs*]; *Bhaur v Equity First Trustees (Nevis) Ltd*, [2023] EWCA Civ 534.

10 See e.g. cases cited in *supra* note 7.

11 21 OR (3d) 739, 1995 CanLII 745 (ONCA) [*Bramco*].

12 For the rules governing the availability of rectification outside the tax planning context see *Shafron v KRG Insurance Brokers (Western) Inc*, 2009 SCC 6 and *Performance Industries Ltd v Sylvan Lake Golf & Tennis Club Ltd*, 2002 SCC 19; and see discussion in Jeffrey Berryman, *The Law of Equitable Remedies*, 3rd ed (Toronto: Irwin Law, 2023) at 681–91; Rami Pandher & Channing Brown, "Practitioners Beware: Equitable Remedies Are Limited (but the Door Has Not Closed)" (2019–2020) 39 Est Tr & Pensions J 165 at 171.

designed to avoid the payment of tax, there is no reason why it should not be corrected."[13]

Between 2000–2016 many Canadian courts radicalized rectification's pro-planning bias. Starting in *Attorney General of Canada v Juliar*, they made rectification available even where a tax plan was executed correctly and was perfectly reflected in documents executed, but as a result of a planning mistake had tax results that disappointed taxpayers. *Juliar* and the later cases applying it made rectification in the tax planning context more generous than rectification in other contexts. Non-tax rectification adjusts documents to reflect the parties' agreement, while in the tax planning context, rectification came, in the *Juliar* line of cases, to re-do transactions to conform to parties' tax-efficient intentions or expectations, even where documents executed reflected taxpayers' agreement or tax minimization plan correctly.[14]

Justice Russell Brown has played a leading role in bringing the *Juliar* line of cases to an end. Brown first pointed out the unorthodoxy of *Juliar* and its progeny as a judge of the Court of Queen's Bench of Alberta. In *Graymar Equipment (2008) Inc v Canada (Attorney General)*, he pointed out that the question rectification applicants need to answer is "'what did the parties originally intend to do?'," not "'what would they have done had they known about this unanticipated tax outcome?'," which would always be answered "'…"something else"'."[15] Brown further explained that "rectification is available to avoid a tax disadvantage for a transaction only where it is established on sufficient evidence that avoiding that tax disadvantage was the original motivation for the transaction."[16] Following Brown's elevation to the Supreme Court of Canada, he held in *Canada (Attorney General) v Fairmont Hotels Inc* that:

> [w]here, therefore, an instrument recording an agreed-upon course of action is sought to be rectified, the party seeking rectification must identify terms which were omitted or recorded incorrectly and which, correctly recorded, are sufficiently precise to constitute the terms of an enforceable agreement.[17]

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13 [1979] 1 All ER 358 (Ch D), relied on by the ONCA in *Juliar*, *supra* note 7.

14 Catherine Brown and Arthur J Cockfield, "Rectification of Tax Mistakes Versus Retroactive Tax Laws: Reconciling Competing Visions of the Rule of Law" (2013) 61 Can Tax J 563 at 575–78. Brown and Cockfield discuss developments to 2013; the *Juliar* line of cases continued until 2016.

15 2014 ABQB 154 at para 71.

16 *Ibid* at para 76.

17 2016 SCC 56 at para 32.

*Fairmont Hotels* rejected the special rectification regime *Juliar* created for tax mistakes, conforming Canadian law governing rectification of tax mistakes to Canadian law governing rectification in other contexts.[18]

The *Fairmont* test can be seen as narrower than the tests in *Bramco* and *Graymar*, which hold that applicants for rectification must show an original, continuing intention to avoid tax in a specific way, not correctly recorded as a result of an error. *Fairmont* requires identifying specific terms which were agreed but omitted or recorded incorrectly. Yet following *Fairmont*, courts continued, and continue, to award rectification in cases where the terms that were agreed are unspecific, and could fairly be characterized as intentions rather than terms. In one case, company directors intended to pay a dividend in the maximum amount that could be paid without tax becoming payable. Their accountants calculated that amount incorrectly based on a tax mistake. It was the amount so calculated that appeared in the directors' resolution. The BC courts rectified it to show the amount the directors would have calculated absent the tax mistake.[19]

## B) Rescission

Between 2015–2022, rescission in equity was available in Canada as an alternative remedial route for eliminating the regretted results of tax mistakes. Rescission became available in Canada in this context by way of the UK Supreme Court decision in *Pitt v Holt* being applied by some Canadian courts. *Pitt* provided that dispositions could be set aside in equity where there was a causative mistake, basic to the transaction, of sufficient gravity to make it unconscionable on the part of the recipient to retain the property.[20] The gravity with which *Pitt* was concerned is of the injustice created by the disposition. Courts have found some tax mistakes to be of sufficient gravity to justify rescission. In *Pitt* itself, Mr. Pitt received compensation for injuries sustained in a traffic accident. Mrs. Pitt settled the sum received on a discretionary trust. Neither she nor her advisors realized that this structuring choice would produce an inheritance tax liability. That liability could have been avoided had the trust been structured as a disabled person's trust, an alternative trust form expressly provided for by statute.

The *Pitt* rule was first applied in Canada in *Re Pallen Trust*, a very different case than *Pitt*. *Pallen* involved a complex series of contrived

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[18] See discussion in Bruce MacDougall, *Mistake in Contracting* (Toronto: LexisNexis, 2018) at 428–29. See also discussion of *Bramco*, *Juliar* and *Fairmont Hotels* in Berryman, *supra* note 12 at 691–98.

[19] *5551928 Manitoba Ltd (Re)*, 2018 BCSC 1482; aff'd *5551928 Manitoba*, *supra* note 9. Rectification was also granted in *Crean*, *supra* note 9.

[20] *Pitt v Holt*, *supra* note 7 at para 122.

transactions intended to avoid tax payable on a corporate dividend.[21] Here follows a partial description of the transactions involved, omitting many of the steps undertaken. A holding company settled a trust, then sold shares of an operating company to the trustee of that trust. The trust was settlor-interested: the holding company reserved the right to call for the shares to be returned. The operating company then distributed dividends to the trustee. Because the trust was settlor-interested, the dividends were attributed to the holding company for income tax purposes under the attribution rules in subsection 75(2) of the Income Tax Act (ITA).[22] These rules require the attribution of income accrued in settlor-interested trusts to their settlors. The attribution made the dividends inter-corporate dividends, paid by one corporation to another. Inter-corporate dividends are effectively tax-free, as corporations may claim a deduction for dividends received under ITA subsection 112(1).[23]

The series of transactions in *Pallen* was not a mistake in 2008, when made; it was a highly artificial tax minimization plan that was long a matter of common practice among Canadian tax planning experts. It reflected a widely accepted understanding of the law. As noted above, one element of the plan was attribution of trust income to the trust settlor under the anti-avoidance rule in section 75(2) of the ITA. Like some other anti-avoidance rules, this rule has long been exploited as an instrument of tax minimization. While the Canadian Revenue Agency (CRA) has earlier made statements that could be read to mean that the plan, or components thereof, would work to avoid tax,[24] in 2006, it determined the plan to be abusive and so to permit application of the general anti avoidance rule (GAAR) in section 245(2) of the ITA.[25]

In 2011, the Tax Court of Canada decided in *Sommerer v Canada* that attribution under section 75(2) of the ITA does not occur where the property, gains on which were sought to be attributed, was sold, rather than gifted, to the trust, a view upheld by the Federal Court of Appeal in 2012.[26] In 2014, the CRA reassessed Pallen's trust for 2008, noting that shares of Pallen's operating company were sold, not gifted, to the trust. Given *Sommerer*, the CRA determined the commonplace tax plan Pallen used to produce a large, and hitherto unsuspected, tax liability: as section

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21 *Pallen*, *supra* note 7.

22 RSC 1985, c 1 (5th Supp) [*ITA*].

23 *Ibid*.

24 Canada Revenue Agency, Interpretation Bulletin IT-369R, "Attribution of trust Income to Settlor" (12 March 1990); Canada Revenue Agency, CRA Views 2001-0116045.

25 Canada Revenue Agency, Conference, CRA Views 2006-0196231C6 (6 October 2006). The Tax Court of Canada and Federal Court of Appeal adopted this view in *Fiducie Financière Satoma v The Queen*, 2017 TCC 84; aff'd 2018 FCA 74.

26 2011 TCC 212, aff'd 2012 FCA 207 [*Sommerer*].

75(2) of the ITA did not apply, the dividends the operating company paid to the trustee were not attributed to the holding company that settled the trust, and were therefore not eligible for the inter-corporate dividend deduction in subsection 112(1) of the ITA. The dividends were instead taxed in the hands of the trust, which as an *inter vivos* trust was subject to the top marginal tax rate under subsection 122(1) of the ITA. The BC courts granted rescission of the tax plan, because not only was Pallen's plan not aggressive, said the British Columbia Court of Appeal, it relied on the CRA's own longstanding understanding of the law.[27]

## C) Canada v Collins Family Trust

When two tax plans, nearly identical to each other and to Pallen's plan, came before the Supreme Court of British Columbia in 2019 in *Collins Family Trust v Canada (Attorney General)*, that court applied the British Columbia Court of Appeal's decision in *Pallen*, by which it was bound.[28] The Supreme Court of British Columbia also noted, however, that *Fairmont* and its Quebec civil law analogue, *Jean Coutu Group v Canada*, laid down a general principle that tax should be assessed on what taxpayers did, not on what they intended to do, and, consequently, that *Pallen* should be reconsidered.[29] The British Columbia Court of Appeal dismissed the Attorney General's appeal in *Collins*, noting that *Fairmont* and *Jean Coutu* were limited to rectification, while rescission was to be awarded according to the rule in *Pitt*, and that both remedies should be awarded when the conditions for granting each are met, even when their granting leads to a tax advantage.[30] On appeal to the Supreme Court of Canada, Justice Brown extended *Fairmont*'s restrictive approach from rectification to rescission, noting that *Pitt* contradicts Canadian law in holding that equity can relieve against a tax mistake.[31] Justice Brown said that:

> [e]quity has no place here, there being nothing unconscionable or otherwise unfair about the operation of a tax statute on transactions freely undertaken. It follows that the prohibition against retroactive tax planning, as stated in *Fairmont*

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27 *Re Pallen Trust*, 2015 BCCA 222 at paras 54–56. Justice Mary Newbury of the British Columbia Court of Appeal has been notably generous in awarding equitable remedies allowing erasure of disappointing tax results: see her decisions in *Pallen*, *supra* note 7, and in *5551928 Manitoba*, *supra* note 9. I thank David Duff for improving, in his comments on an earlier draft of this paper, my description of *Pallen*: the description in the text is partly his.

28 2019 BCSC 1030.

29 *Ibid* at paras 93–100.

30 *Collins Family Trust v Canada (Attorney General)*, 2020 BCCA 196 at paras 54–56 [*Collins* BCCA].

31 *Collins* SCC, *supra* note 1 at para 24.

> *Hotels* and *Jean Coutu*, should be understood broadly, precluding any equitable remedy by which it might be achieved, including rescission.[32]

Notably, lower courts have continued to award rectification in the tax planning context since the Supreme Court of Canada decision in *Collins*, reading Justice Brown's prohibition on retroactive tax planning as not extending to rectification of clerical mistakes.[33] Rectification is now awarded to implement tax planning and other transactions as originally structured and intended, correcting documentation errors; it is no longer awarded to erase or replace failed tax plans where tax mistakes were inherent to the plan as structured.

Justice Brown's position in *Collins* has the merit of clarity: while tax planning for tax minimization purposes is allowed, subject to the GAAR, to specific anti-avoidance rules and to judicial anti-avoidance doctrines, such as the sham doctrine, the courts will not extract taxpayers whose plans led to disappointing tax results from their predicament by way of equitable remedies. His decisions in *Fairmont* and *Collins* stand out for their decisive, cut and dried character. They have made Canadian law governing the availability of equitable remedies to retroactively erase or amend mistake-based tax planning far more restrictive than English and US law on the topic. In England, while the law governing rectification in tax mistake cases is similar to *Fairmont*,[34] rescission in such cases is available under *Pitt*, and is quite frequently granted.[35] Glister and Lee note that:

> factors which have so far been taken into account in assessing unconscionability under *Pitt* include the availability of an alternative remedy, the size of any unintended tax liability, the centrality to the decision [sought to be rescinded] of any incorrect professional advice obtained, the effect on the claimant if the disposition were not set aside, and the effect on any other parties or obligations.[36]

In the US, the federal courts have just once rescinded a transaction based on a tax mistake.[37] The paucity of rescinding decisions is likely explained

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[32] *Collins* SCC, *supra* note 1 at para 7. See discussion in Berryman, *supra* note 12 at 698–99.

[33] *Sleep Country Canada Holdings Inc v Canada (Attorney General)*, 2022 ONSC 6103; *Slightham v AGC*, 2023 ONSC 6193.

[34] Jamie Glister & James Lee, *Hanbury & Martin: Modern Equity*, 22nd ed (London: Thomson Reuters 2021) at para 29-020.

[35] See e.g. *Bainbridge v Bainbridge*, [2016] EWHC 898 (Ch); *Freedman v Freedman*, [2015] EWHC 1457 (Ch); *Kennedy v Kennedy*, *supra* note 9; *Van der Merwe*, *supra* note 9; *Hartogs*, *supra* note 9.

[36] Glister & Lee, *supra* note 34 at para 29-003.

[37] *Neal v United States of America*, 1998 US Dist LEXIS 12048 (Pa Dist Ct).

by the Internal Revenue Service allowing parties to transactions that have been discovered to have bad tax results to themselves rescind the transactions, absent court involvement, if rescission is carried out within one year of the original transaction.[38] US state law provides an extended rectification doctrine applicable to trust instruments alone: the Uniform Trust Code, versions of which have been enacted into law in 35 states and the District of Columbia, provides that:

> [t]he court may reform the terms of a trust, even if unambiguous, to conform the terms to the settlor's intention if it is proved by clear and convincing evidence what the settlor's intention was and that the terms of the trust were affected by a mistake of fact or law, whether in expression or inducement.[39]

The comment to this section provides that "a mistake in the inducement occurs when the terms of the trust accurately reflect what the settlor intended to be included or excluded but this intention was based on a mistake of fact or law".[40] 35 US states therefore have a rectification doctrine similar to that in *Juliar*, but applicable to trust instruments alone.

## Part II. Should Equitable Remedies be Available to Reverse Failed Tax Planning?

This Part provides a policy discussion of whether equitable remedies should be available to reverse failed tax planning schemes. I will approach this question in two stages. First, I will lay out the arguments pro and con. Then I will lay out, and seek to justify, my view.

### A) Reasons pro and con

I see two fundamental reasons for allowing equitable remedies to reverse failed tax planning. First, our law sees tax planning, also known as tax minimization, as legitimate. This is obvious in the case law, which continues to celebrate the so-called "Duke of Westminster principle … that

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38 Stanley C Ruchelman & Neha Rastogi, "Rescission - Undoing a Transaction that Seemed Like a Good Idea at the Time" (2021) 8:6 Insights 40; New York State Bar Association Tax Section, *Report on the Rescission Doctrine* (New York: 2010); Allen Sparkman, "The Rescission Doctrine: Everything Old is New Again" (2015) 4:2 Am U Bus L Rev 183.

39 Uniform Trust Code § 415 (2010).

40 *Ibid*. The North Dakota Supreme Court remanded a case, instructing the district court to reform two trusts under the North Dakota equivalent of this Uniform Trust Code section, despite the trust instruments reflecting the settlors' intentions, because the settlors formulated those intentions under a mistake of law: *In re Matthew Larson Trust Agreement*, 2013 ND 85 (N Dak Sup Ct).

taxpayers have the right to order their affairs to minimize tax payable[.]"[41] The majority of the Supreme Court of Canada stated in *Canada v Alta Energy Luxembourg SARL* that "[t]axpayers are allowed to minimize their tax liability to the full extent of the law and to engage in 'creative' tax avoidance planning, insofar as it is not abusive within the meaning of the GAAR[.]"[42] Legislation sets out acceptable tax minimization plans for taxpayers to follow: see, for example, section 85(1) of the Income Tax Act, which "permits the 'rollover' or sale [of shares] on a tax deferred basis if the consideration for the vendor's shares includes shares of the purchaser".[43] Even the recently amended GAAR provides that its application should "not [prevent] taxpayers from obtaining tax benefits contemplated by Parliament[.]"[44] Since much tax planning is seen as legal and legitimate, there may be little cause to prevent private law doctrines enabling reversal of mistake-based contracts and dispositions from being applied in a tax planning context.

Another reason to allow the reversal or amendment of tax plans that have failed pursuant to a tax mistake is that given the extreme complexity of tax legislation, the likelihood of such mistakes is significant. Most cases where taxpayers applied to have their tax planning rescinded or rectified originated in planning mistakes by well-known, well-compensated tax advice professionals, who ignored the impact of well-known tax rules on the planning they sold.[45] The risk of tax mistakes is further aggravated by the Canadian rule that tax law changes may operate retroactively.[46] Further, the results of tax mistakes can be truly devastating for the individuals involved. An illustrative example of such results is found in the UK case of *Lobler v HMRC*.[47] Mr. Lobler, a Dutch national, moved to England for work, taking his wife and two young children along. Soon

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41 *Jean Coutu*, *supra* note 6 at para 41.

42 2021 SCC 49 at para 48 [*Alta Energy*]. The recent case of *Deans Knight Income Corp v Canada*, 2023 SCC 16 [*Deans Knight*] takes a less pro-planning direction. This one case, however, should not be seen as bringing the SCC's treatment of tax planning as legitimate to an end. The SCC has given planning-critical decisions in the past, only for them to be followed by planning-friendly decisions: see text accompanying notes 67–68 below.

43 *Juliar v Canada (Attorney General)*, 1999 CanLII 15097 (ONSC) at para 46.

44 *ITA*, *supra* note 22, s 245(0.1)(a).

45 See e.g. *Sommerer*, *supra* note 26, and *McPeake v Canada (Attorney General),* 2012 BCSC 132, which both resulted from tax professionals overlooking the impact of the income attribution rule in the ITA at s 75(2); as well as *Juliar*, *supra* note 7, and *Stone's Jewellery Ltd v Arora*, 2009 ABQB 656, which both resulted from such professionals misapplying the above-mentioned s 85(1) of the ITA.

46 Retroactive application of *Sommerer*, *supra* note 26, where the Federal Court of Appeal interpreted the ITA s 75(2) differently to how it was interpreted until then, brought about the downfall of the tax planning in *Pallen*, *supra* note 7, and *Collins* SCC, *supra* note 1.

47 *Lobler v HMRC*, *supra* note 7.

thereafter he sold the family home in the Netherlands, the value of which represented his entire life's savings. Lobler invested the price received for his home in insurance policies, then withdrew money from those policies, by way of partial surrender, to pay for an English home he bought for his family. Lobler believed this to be a withdrawal of capital and thus non-taxable. Unfortunately, he fell foul of a statutory provision, of which he was unaware, holding nearly the entirety of the withdrawn amount to be taxable income. Paying the assessment issued to Lobler would have exhausted his life savings and potentially bankrupted him.[48] Fortunately for him, the Upper Tax Tribunal granted rectification.[49] Notably, had Mr. Lobler's case been subject to Canadian law, he would have won rectification under *Juliar*, but not under current law. His mistake was in being unaware of the statutory provision deeming the sum he withdrew from his policies to be taxable income, not in mis-documenting his intentions. Given rescission is currently unavailable in Canada in the tax mistake context, a Canadian Lobler may well have had to declare bankruptcy. Mr. Lobler's case was one of tax ignorance rather than of tax planning. I will return to this distinction below. Given, however, Canadian law's acceptance of tax planning, and the significant likelihood and potentially devastating consequences of planning mistakes, giving failed tax planners access to rescission and rectification may appear to make sense.

Some would list a third reason for allowing rescission and rectification to reverse failed tax planning: that equity, being a part of private law, should be allowed to run its course before tax, a part of public law, is applied to the results. On this view, that taxpayers seek rescission or rectification in order to improve their tax situation is irrelevant to these equitable remedies' operation. Where mistakes such as private law sees to suffice have been made, equitable remedies should follow, regardless of their effect on plaintiffs' tax position, or of the role of that effect in driving plaintiffs to sue.[50] I am not convinced by this approach. In my view, the law does not, and should not, maintain a tight separation between private and public (specifically tax) law, with private law being applied to transactions and dispositions in disregard of the tax results of equitable remedies being or not being granted. Equity does not disregard the public policy results of its application. As Nair and Samet make clear, equity has long taken public policy into account. This is evident in its preferring bona fide purchasers of property despite the harm this preference does to assets' erstwhile owners, in order to bolster commercial certainty, a public

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48 *Ibid* at paras 9–13.

49 *Ibid* at paras 74, 142. While *Lobler* was followed in *Cooke v HMRC*, [2024] UKFTT 00272 (TC), it is contrary to the main trend of English law regarding rectification of decisions due to tax mistakes, for which see Glister & Lee, *supra* note 34 at para 29-020.

50 I owe this point to correspondence with Lionel Smith.

policy.[51] Another example of equity giving weight to public policy dates from the eighteenth century, when English Chancellors relieved against contracts entered into by expectant heirs to large family fortunes, who alienated or charged their interests in the family property to support their indebtedness. Equity relieved such high-class debtors not because of their convincing private law cases, but to "prevent the ruin of families."[52] As Macmillan noted, "[e]quity sought to set aside the bargain with the heir in order to implement an underlying principle of public policy, namely, the prevention of damage to the heir's family and, indeed, to great families generally."[53] In other words, eighteenth century equity acted to maintain the concentration of wealth in the then ruling class. Preserving this concentration was then public policy. One could hardly claim, therefore, that taking public policy into account is somehow foreign to equity. As a result, the claim that equitable remedies are applicable whatever the tax results because such results are a public law matter and equity does not take such matters into account cannot pass muster.

There are also reasons, mostly of distributive justice, against granting equitable remedies to reverse failed tax planning. As Gillis noted, "[t]ax avoidance … has at least two distributive effects: 1) it reduces government revenues, which are often used for redistributive expenditures; and 2) it disproportionately reduces the tax liability of high-income individuals."[54] In other words, tax planning creates inequality in disrupting the operation of the tax-and-transfer system, society's chief instrument of redistribution. The granting of judicial assistance to tax planning clients faced with disappointing results aggravates this inequality. Given the cost of litigating all the way to rescission or rectification, access to such judicial assistance may itself be unequally distributed. One is also minded to ask whether the judicial system, funded with taxpayer money, should spend that money on helping the better-off reduce the tax yield. Further, the availability of equitable remedies in cases of failed planning makes planning less risky, and so incentivizes taxpayers to plan, increasing the amount of planning and probably decreasing the tax yield. Admittedly, granting an equitable remedy to reverse the tax result of an individual's tax planning errors is likely to have a smaller adverse impact on the public fisc than granting restitution of all tax paid under a tax statute

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[51] Aruna Nair & Irit Samet, "What Can 'Equity's Darling' Tell Us About Equity?' in Klimchuk, Samet & Smith, *supra* note 5 at 264–90.

[52] *Earl of Chesterfield v Janssen* (1751), 2 Ves Sen 125, 28 ER 82, at 101, 158, quoted in Catharine Macmillan, "Earl of Aylesford v Morris (1873)", in Charles Mitchell & Paul Mitchell, eds, *Landmark Cases in Equity* (Oxford: Hart Publishing, 2012) 329 at 329, 332.

[53] Macmillan, *supra* note 52 at 345.

[54] Rory Gillis, "The Limits of Legal Substance: Tax Avoidance and Equitable Remedies after *Collins Family Trust*" (2022) 66 Can Bus LJ 323 at 332.

later deemed unconstitutional.[55] A judicial approach like that in *Juliar*, making equitable tax planning reversals and amendments relatively easily accessible, is likely, however, to result in such remedies being granted to many taxpayers, increasing the adverse impact on the fisc.

Another reason against granting equitable remedies to reverse failed tax planning is that, in granting them, equity is duplicating and extending the existing judicial avenues for interfering with CRA assessments. Courts impeding government policy and decisions, including in the tax field, are nothing new: public and human rights law lets courts impede government policies and decisions. Judge-made and court-administered law is seen as a normative anchor for protecting individuals from the brunt of those policies and decisions. Taxation can certainly be seen as infringing persons' and entities' property rights, and as noted above, such infringement can be so grave as to make the right-holder destitute. Application of equitable remedies in tax planning mistake cases can be understood as an analogue to judicial review of administrative decisions. As Fox-Decent noted, "[e]quity has the form of public law," providing a bulwark against domination and abuse between private parties that is analogous to public law's bulwark against abuse of state power.[56] Such formal similarity does not imply, however, that equity should take on public law's role of protecting individuals from state-caused harm. Appeals from CRA assessments take place by way of the tax court, while judicial review of abuses of process by the CRA is handled by the Federal Court of Canada. These courts do not strike down CRA assessments due to taxpayers having made planning mistakes. The pre-*Collins* use of equitable remedies to reverse the tax results of failed planning can be seen as an attempt to extend judicial review of or appeals from CRA assessments. Current law does not allow such extension: as the Supreme Court of Canada said in *Quebec (Agence du revenu) v Services Environnementaux AES inc*, "the specific avenues established by Parliament for tax appeals cannot be circumvented[.]"[57]

## B) My view

Whether and to what extent equity should prefer the purposes of the tax-and-transfer system or those of individuals resisting it is a value question. One could say that answers to this question are to be determined according to the values—the public policy—of each nation, to the extent

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55 See discussion of courts' taking into account the adverse impact of such restitution on the public fisc in Mitchell McInnes, *The Canadian Law of Unjust Enrichment and Restitution*, 2nd ed (Toronto: LexisNexis Canada, 2022) at para 24.02[2].

56 Evan Fox-Decent, "The Constitution of Equity", in Klimchuk, Samet & Smith, *supra* note 5 at 116–43. The quote is at 118.

57 2013 SCC 65 at para 43, paraphrasing *Canada v Addison & Leyen Ltd*, 2007 SCC 33 at para 11.

each has a pertinent national view. The different current views of English and Canadian law regarding the desirable extent of equitable reversal of mistake-based tax planning—English law allows rescission in the presence of "causative mistakes of sufficient gravity",[58] while Canadian law does not—parallel the status each system accords to property rights generally. The UK provides some quasi-constitutional protection of property rights in its Human Rights Act, which entrenches in UK law the "rights and freedoms guaranteed under the European Convention on Human Rights," including the "protection of property".[59] Canada, on the other hand, chose not to entrench protection of property rights in its Charter. Still, it would be naïve to assume that the law of each nation allows the extent of equitable reversal of mistake-based tax planning that expresses each nation's values, so that law reform is nowhere necessary. After all, Canadian law on topic has changed dramatically within the last decade, as did English law on topic in 2013.[60] There is therefore reason to try and outline the extent of such reversal that fits Canadian law.

Canadian law accepts both redistribution by way of government tax-and-transfer systems and tax planning. A balance must be struck, taking into account the reasons pro and con canvassed above. Given that allowing equitable erasure of mistake-based tax planning is likely to increase the amount of planning and reduce taxes payable, I believe rescission and rectification should be granted in the tax planning context only where an individual taxpayer (meaning a natural, not a legal, person) would be reduced to insolvency should they not be so granted. Tax should not beggar anyone. It is a mechanism of social equalization and improvement, not a trap. Where equity eliminates taxpayer-beggaring tax burdens, the state's loss is less than the total tax burden eliminated: should the burden be allowed to stand, the state is quite likely to have to provide the newly poor taxpayer with welfare benefits. Cancellation of the burden therefore costs the state less than is apparent. While cases where taxpayer-beggaring tax burdens resulted from taxpayers' ignorance, such as *Lobler*, seem more deserving of burden-erasing assistance than cases where similarly crushing burdens result from tax planning gone wrong, even the latter should be afforded assistance where the burden is so crushing as to lead to insolvency of a human taxpayer, given our law's fundamental acceptance of tax planning.

My proposal is more generous on rescission than current law, which makes it unavailable in all tax mistake cases. On rectification, it is less

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58 *Pitt v Holt*, *supra* note 7 at para 122.

59 *Human Rights Act 1998* (UK), 1998 Introduction. The "protection of property" is provided for in Schedule 1, Part II, art 1.

60 *Pitt v Holt*, *supra* note 7.

generous than current law, which grants rectification where a specific tax minimization plan has been inaccurately recorded. Under *Fairmont*, rectification is available to taxpayers who put in place a detailed scheme of artificial tax avoidance, only to have it misrecorded, but would not have been available to the hapless Mr. Lobler. Our law thus incentivizes taxpayers to construct detailed, specific tax minimization plans: surely an inappropriate incentive. If current law imposes too much tax, the burden needs to be lessened, either by cutting rates or by reforming tax bracket schedules so that higher rates only apply to higher incomes than at present. Current tax burdens should not be indirectly cut by providing judicial assistance to taxpayers whose tax minimization plans have gone wrong due to mistake. As the UK Supreme Court said, "artificial tax avoidance is a social evil which puts an unfair burden on the shoulders of those who do not adopt such measures."[61] Which is to say: it has regressive distributive effects, consonant with the public policy of the eighteenth century, but not with that of the present. While our law accepts such avoidance, it should not provide judicial assistance to disappointed planners at taxpayer expense, except in cases where planning gone wrong will render flesh-and-blood taxpayers insolvent if not erased by the court. Such judicial assistance should never be available to corporations: as they are often, by design, leveraged close to the line of (in)solvency, an unexpected tax liability could easily tip them over that line.[62]

As the CRA has repeatedly pointed out in litigating rescission and rectification cases in the tax context, taxpayers faced with a ruinous tax burden following error-ridden planning have remedies at their disposal other than equitable remedies. They can appeal their tax assessment to the Tax Court of Canada; sue their professional advisors for negligence; and apply to the Minister of Finance for an order-in-council for remission of tax where its collection is "unreasonable or unjust" or where it is "otherwise in the public interest to remit the tax[.]"[63] Each of these alternatives differs from equitable remedies. The Tax Court of Canada has no power to award rectification or set aside transactions as between the parties; it may, however, recognize that a transaction is ineffective under provincial law and treat it, for tax purposes, as set aside.[64] A negligence suit against professional advisors responsible for a tax mistake is only possible where the advisor's liability for negligence has not been ousted in some applicable document. It is also an "expensive, slow and uncertain" process.[65]

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61 *Ibid* at para 135.

62 A point made by one of the referees for the *Canadian Bar Review*.

63 *Financial Administration Act*, RSC 1985, c F-11, s 23. This federal provision has provincial analogues. See e.g. *Ontario Land Transfer Tax Act*, RSO 1990, c L.6, s 20.

64 *McLaughlan v Canada*, 2007 TCC 209 at paras 15–25; *Kufsky v Canada*, 2019 TCC 254 at para 26.

65 *5551928 Manitoba Ltd (Re)*, *supra* note 19 at para 47.

Applications for remission, finally, are "'uncertain, complex and slow',"[66] with the minister likely to guide him or herself by the CRA's view.[67] Some have seen the very existence of these alternative avenues of recourse to suffice for excluding equitable remedies.[68] Joel Nikitman, counsel for the taxpayers in both *Pallen* and *Collins*, wrote, on the other hand, that "the test is not whether there exists a *possible* alternative remedy, but whether that remedy is a *practical*, *realistic* remedy. Only in a rare case would suing one's advisers or seeking remission meet that test."[69] My view is that, given the cost of judicial proceedings, taxpayer-beggaring tax burdens produced by planning mistakes are better removed by way of administrative recourse. But where such recourse is not realistically available, or is not cheaper to provide than a judicial proceeding, equitable remedies should be available to erase mistake-based tax planning where absent such erasure the tax burden produced would render the taxpayer insolvent. Recourse is realistically available where the taxpayer has a means, other than applying for equitable remedies, of having the devastating results of their error-ridden tax planning eliminated. Such elimination could take place other than by eliminating the transactions or dispositions undertaken or the consequent tax assessment, as by the taxpayer's advisors compensating the taxpayer for the results of their negligence. A putative recourse that is not practically available, as where negligent advisors are protected by a liability exemption clause, or where tax remission is never, or very rarely, in practice granted, would not suffice to exclude equitable remedies in the devastating cases where I suggest they be made available.

One alternative to the view delineated above is allowing rescission or rectification, depending on the type of mistake involved, where the tax plan in question was such as Canadian law sees as legitimate, and refusing equitable relief where the tax plan was abusive. While some prefer a rule focused on the substance of the plan to one focused on the results of its failure, the line between legitimate and abusive tax plans is, to a significant extent, in the eye of the beholder, rendering this alternative rule uncertain. This uncertainty has been demonstrated regarding the very plan in *Pallen*: while the British Columbia Court of Appeal saw it as non-aggressive,[70] renowned tax expert David Duff sees it as very aggressive.[71] While Duff believes jurisprudence applying the GAAR has been successful in clarifying

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66 *5551928 Manitoba*, *supra* note 9 at para 28.

67 *Collins* BCCA, *supra* note 30 at para 87.

68 *Canada Life Insurance Company of Canada v Canada (Attorney General)*, 2018 ONCA 562 at para 92.

69 Joel Nitikman, "Equitable Rescission of Contracts for Mistake in Canada After Great Peace: Whither Solle v. Butcher?" (2021) 69:4 Can Tax J 1027 at 1075.

70 *Re Pallen Trust*, 2015 BCCA 222 at paras 54–56.

71 Original correspondence with author.

what planning is legitimate and what is abusive,[72] Duff himself described the winding, uncertain course of that jurisprudence, now restricting the GAAR's ambit,[73] now expanding it.[74] There being little reason to believe the Supreme Court of Canada's latest GAAR decision, the pro-revenue decision in *Deans Knight Income Corp v Canada*, to be the end of that winding course,[75] I believe that the ever-shifting line drawn by GAAR jurisprudence between legitimate and abusive tax plans is not clear and stable enough to provide a limit for the application of equitable remedies in tax mistake cases. While recent amendments to the GAAR appear to make it more of a constraint on tax planning than it had hitherto been, they do not make the line between legitimate and abusive planning any clearer than it was.[76] Insolvency, on the other hand, is more easily identifiable: taxpayers applying for rescission or rectification in the tax context should be required to show the court that absent the remedy applied for, they will be reduced to insolvency. Where a tax plan involves several persons, only one or some of whom are rendered insolvent by its tax consequences, relief should be available where those taxpayers not rendered insolvent cannot be expected to help those so rendered: whenever, that is, the former are not the immediate relatives of the latter.

Another alternative rule is refusing relief in all cases of tax mistakes, directing disappointed taxpayers to sue the tax advisors that put in place the ill-advised tax plan or supplied the error-ridden document. While the government is better placed to absorb and spread loss than even the largest corporate tax advisor, advisors are best placed to prevent the loss, by taking more care in advising. [77] Imposing the loss on advisors, however, would require disallowing the duty waivers and liability exemptions advisors use. Should waivers and exemptions be disallowed, however, tax advice would either become more expensive or far less easily available, or both. Given the complexity of much tax law, I believe tax advice should stay available to individuals, at as affordable a price as possible. Corporations, on the other hand, often have more power to negotiate with their advisors *ex ante*

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72 Original correspondence with author.

73 See e.g. *Canada Trustco Mortgage Co v Canada*, 2005 SCC 54; *Alta Energy*, *supra* note 42.

74 See e.g. *Lipson v Canada*, 2009 SCC 1; *Deans Knight, supra* note 42. See discussion of the jurisprudence in David G Duff, "Amendments to the Canadian General Anti-Avoidance Rule" (2023) no 5 Brit Tax Rev 666 at 672–80 [Duff, Amendments].

75 See Duff's analysis of this decision in David G Duff, "Corporate Tax Attribute Trading and the General Anti-Avoidance Rule: Deans Knight Income Corp. v. Canada" (2024) 69:1 Can Bus LJ 69.

76 *Fall Economic Statement Implementation Act, 2023*, SC 2024, c 15, s 66, amending s 245 of the *ITA*, *supra* note 22, and discussed in Duff, Amendments, *supra* note 74 at 680–93.

77 These two alternative rules were suggested by David Duff.

concerning the latter's liability where they make a tax mistake. For these reasons I believe my view above to be preferable to both current law and the two alternative solutions I discussed.

## Conclusion

I discussed one of the oddest uses of equity: the granting of equitable remedies to assist users of tax minimization plans where their plans result in unexpected tax liabilities. Such use of equity is far from its classical uses to remedy injustices between private, non-state parties, that have otherwise been left intact and unremedied by the law. It is analogous to public law in its protection of private taxpayers from the state. Modern law governing this use of rescission and rectification is complex and ever changing, differing both between jurisdictions and across time. This complexity and instability result from modern law's approval of both the state tax-and-transfer system and tax minimization planning, despite the latter being adverse to the former. Canadian law has in the current century first taken a strikingly liberal approach to granting rescission and rectification to reverse the tax results of failed, mistake-based tax planning, and later switched to an approach far more restrictive than those under UK and US law. In my view, state-funded courts should in general not grant equitable remedies to taxpayers whose tax minimization schemes have met with unexpected tax burdens as a result of tax mistakes being made in designing or implementing those schemes. I recognize, however, that tax mistakes can lead to truly devastating results for taxpayers, and that such mistakes are quite frequent and are only to be expected given the complexity of our tax law and our acceptance of changes to that law operating retroactively. I therefore suggest that courts retain a power to grant rescission or rectification, as necessary, to eliminate or amend mistake-based tax planning that will, if left intact, render a human taxpayer insolvent, where that result is not realistically preventable in other ways.