Federal Court of Appeal  Cour d'appel fédérale

Date: 20151216

Docket: A-511-14

Citation: 2015 FCA 288

CORAM: **GAUTHIER J.A.**
WEBB J.A.
NEAR J.A.

BETWEEN:

AGRACITY LTD

Appellant

and

HER MAJESTY THE QUEEN

Respondent

Heard at Toronto, Ontario, on September 30, 2015.

Judgment delivered at Ottawa, Ontario, on December 16, 2015.

REASONS FOR JUDGMENT BY: WEBB J.A.

CONCURRED IN BY: GAUTHIER J.A.
NEAR J.A.

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REASONS FOR JUDGMENT

WEBB J.A.

[1] The main issue in this appeal is whether the Crown can have inconsistent pleadings in relation to appeals filed in the Tax Court of Canada by different taxpayers. Justice C. Miller of the Tax Court of Canada partially allowed the motion of AgraCity Ltd. (AgraCity) to strike parts of the reply filed by the Crown (Docket 2014-1537 (IT)G). AgraCity is appealing the decision to not strike the other parts of the reply that AgraCity was seeking to have struck on the basis that

such parts are inconsistent with another reply that has been filed by the Crown in response to an appeal of another taxpayer. AgraCity is also appealing the Order that it serve and file a list of documents in accordance with Rule 82 of the *Tax Court of Canada Rules (General Procedure)* (the *Rules*).

[2] The Crown is cross-appealing the order to strike or rewrite parts of its reply. The main issue in the cross-appeal is whether the references to paragraphs 247(2)(*a*) and (*c*) of the *Income Tax Act*, R.S.C. 1985, c.1 (5th Supp.) (the *Act*) should have been struck.

[3] For the reasons that follow, I would dismiss the appeal of AgraCity and allow, in part, the cross-appeal of the Crown.

Background

[4] This matter is at the pleadings stage before the Tax Court of Canada. The actual facts of the case are not clear and are in dispute. It appears that there is no dispute that farmers in Canada wanted to buy a particular herbicide, ClearOut, which was to be imported into Canada. What is not clear is who was selling ClearOut.

[5] There are three companies that are relevant in this matter:

- AgraCity, which is wholly owned by Jason Mann;
- 101072498 Saskatchewan Ltd. (SaskCo), which is indirectly owned by Jason Mann and his brother, James Mann; and

- NewAgco-Barbados, a company incorporated under the laws of Barbados, which is wholly owned by SaskCo.

[6] During the taxation years under appeal, NewAgco-Barbados reported significant profits from the sale of ClearOut and claimed that it had paid significant amounts to AgraCity as a service fee in relation to the sale of ClearOut.

[7] In the reply filed by the Crown in relation to AgraCity's appeal to the Tax Court of Canada, the Crown pled that NewAgco-Barbados did not sell any ClearOut and therefore should not have been entitled to any profit from the sale of ClearOut. The Crown determined, under section 247 of the *Act*, that the fair market value of the services provided by AgraCity was equal to the amount that had been paid by NewAgco-Barbados plus the net profit that had been reported by NewAgco-Barbados from the sale of ClearOut, thus effectively reallocating all of the profit reported by NewAgco-Barbados from the sale of ClearOut to AgraCity.

[8] In the reply filed by the Crown in relation to SaskCo's appeal to the Tax Court of Canada, the Crown pled that NewAgco-Barbados bought ClearOut and sold it to AgraCity. As noted by the Tax Court Judge, the pleadings of the Crown in relation to the appeals of AgraCity and SaskCo are irreconcilable.

[9] The only reply that is the subject of this appeal, is the reply related to AgraCity's appeal to the Tax Court of Canada.

Decision of the Tax Court

[10] The Tax Court Judge held that the Crown could have a reply in relation to an appeal of one taxpayer that is inconsistent with the reply filed in relation to the appeal of another taxpayer. As a result, he did not grant AgraCity's motion to strike all of the parts of the reply that would be inconsistent with the reply filed by the Crown in relation to the appeal of SaskCo.

[11] The Tax Court Judge did, however, strike certain paragraphs related to transfer pricing. In the reply, the Minister relied on both paragraphs 247(2)(*a*) and 247(2)(*b*) of the Act to adjust the amount that would be included in the income of AgraCity under paragraph 247(2)(*c*) (if only paragraph 247(2)(*a*) was applicable) or under paragraph 247(2)(*d*) (if paragraph 247(2)(*b*) was applicable). The Tax Court Judge concluded that since the Minister had assumed that no product was sold by NewAgco-Barbados, the provisions of paragraphs 247(2)(*a*) and (*c*) of the *Act* could not be applicable and he struck those paragraphs of the reply that referred to these paragraphs.

[12] The Tax Court Judge also struck certain parts that he identified as conclusions of law and ordered the Crown to file an amended reply in which paragraph 14(d) would be moved to another location in the reply and to clarify the facts upon which it was basing its assessment of the penalty under subsection 163(2) of the *Act*.

[13] The Tax Court Judge also ordered the parties to serve and file a list of documents under *Rule* 82.

[14] While the Tax Court Judge also ordered the parties to submit a timeline for the completion of various steps and that the appeal of AgraCity would be heard on common evidence with the appeal of SaskCo, neither party appealed these orders.

[15] As noted above, AgraCity has appealed and the Crown has cross-appealed to this court.

Standards of Review

[16] The standards of review are those standards as set out in *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235 (*Decor Grates Inc. v. Imperial Manufacturing Group Inc.*, 2015 FCA 100, [2015] F.C.J. No. 503). In *Housen v. Nikolaisen*, the Supreme Court of Canada confirmed that the standard of review for appeals from decisions of the lower courts for questions of law is correctness. Findings of fact (including inferences of fact) will stand unless it is established that the Tax Court Judge made a palpable and overriding error. For questions of mixed fact and law, the standard of correctness will apply to any extricable question of law and otherwise the standard of palpable and overriding error will apply. An error is palpable if it is readily apparent and it is overriding if it changes the result.

Issues

[17] The issues arising as a result of the appeal and the cross-appeal are whether the Tax Court Judge erred in:

(a) not striking all of the parts of the reply that are inconsistent with the position of the Crown in the reply filed in relation to the appeal of SaskCo;

(b) ordering each party to serve and file a list of documents under *Rule* 82;

(c) striking the paragraphs from the reply that relate to paragraphs 247(2)(*a*) and (*c*) of the *Act*;

(d) striking or ordering the Crown to move paragraphs of the reply that the Tax Court Judge determined to be statements of law; and

(e) ordering the Crown to redraft its reply in relation to the assessment of penalties under subsection 163(2) of the *Act*.

Inconsistent Positions

[18] AgraCity argues that the Crown, in its reply, cannot plead any facts that are inconsistent with the facts as pled by the Crown in the reply filed in relation to the appeal of SaskCo. I do not agree with the position of AgraCity.

[19] AgraCity and SaskCo, although they are related persons for the purposes of the *Act*, are two separate persons. The Minister of National Revenue (the Minister) is to assess (or reassess) each taxpayer under section 152 of the Act. Because each taxpayer is assessed (or reassessed) separately, this can result in inconsistent assessments (*Peterson v. The Queen*, 2005 FCA 263, [2005] F.C.J. No. 1269, at paragraph 4). If the Minister has issued inconsistent assessments, this will lead to inconsistent pleadings, if the taxpayers appeal to the Tax Court of Canada. In this case the Crown acknowledges that the assessments and hence the pleadings are inconsistent and that the Crown does not seek to have both assessments upheld.

[20] Even though the Crown made certain admissions of fact in the reply filed in relation to the appeal of SaskCo, those admissions would only relate to that appeal, not to the appeal of AgraCity (Lederman, Bryant and Fuerst, *The Law of Evidence in Canada*, 4th ed. (Canada: LexisNexis Canada Inc., 2014) at para. 19.6). Since these appeals will be heard on common evidence, how any admission of facts will affect the outcome of the appeals is a matter best left to the trial judge who will be hearing all of the evidence and who will determine what facts have been established.

[21] I would dismiss AgraCity's appeal in relation to this issue.

Full Disclosure – Rule 82

[22] There are two rules related to the disclosure of documents in a proceeding before the Tax Court of Canada: *Rule* 81 (Partial Disclosure) and *Rule* 82 (Full Disclosure). *Rule* 81 provides that each party is to file and serve a list of documents that might be used to support any allegation of fact made by that party or to rebut any allegation of fact made by the opposing party. Therefore, a list of documents filed under *Rule* 81 by a particular party may omit a relevant document that such party does not intend to introduce at the hearing before the Tax Court of Canada.

[23] If the parties agree or if the Tax Court of Canada so orders, each party will be required to provide a list of all relevant documents as provided in *Rule* 82. In this case, the Crown brought a motion for an order for full disclosure under *Rule* 82 and the motion was granted.

[24] AgraCity's main argument in appealing the order for full disclosure is that the Crown had inconsistent pleadings in the reply filed in relation to AgraCity's appeal and the reply filed in relation to SaskCo's appeal. AgraCity also argued that ordering full disclosure was premature.

[25] As noted above, the Crown can have inconsistent pleadings in relation to two different taxpayers. It must be remembered that the transactions in question are transactions completed by AgraCity, SaskCo and other related companies – they are not transactions completed by the Minister. The Minister's knowledge of the transactions can only be gleaned from what is discovered when the companies are audited. Since the Crown has inconsistent pleadings this would indicate that what actually transpired between or among the various companies is far from clear. Disclosing all relevant documents may well assist in clarifying what actually happened. Therefore, I do not accept AgraCity's argument that inconsistent pleadings should be a basis for overturning the Tax Court Judge's decision to grant the order for full disclosure under *Rule* 82.

[26] AgraCity also submits that the order should not have been granted because the pleadings have not closed and because no list of documents has been provided under *Rule* 81. AgraCity refers to the decision of Justice Campbell in *Long v. The Queen*, 2010 TCC 197, 2010 D.T.C. 1146. Justice Campbell denied an appellant's request for an order under *Rule* 82. She stated that:

> **30** The most compelling argument against full disclosure at this time is the timing of the Motion. The Appellant brought this Motion at the close of the pleadings but prior to the commencement of any other steps in the litigation process. Although there is no limitation on the timing of a Rule 82 application, one of the considerations to be taken into account is the stage of the proceedings, particularly when none of the preliminary steps have been initiated. In fact, some of the very documents which the Appellant requests under Rule 82 may be produced under the production of a partial list of documents pursuant to Rule 81.

[27] This decision was affirmed on appeal (2011 FCA 85, [2011] 3 C.T.C. 160).

[28] As noted by Justice Campbell, "there is no limitation on the timing of a Rule 82 application". However, she considered the stage of the proceedings to be a relevant consideration in that case. In this case, the Tax Court Judge also considered my comments in *Imperial Tobacco Canada Ltd. v. The Queen*, 2012 TCC 135, [2012] 5 C.T.C. 2005, at paragraph 25, that the interests of justice is also an important consideration.

[29] In my view, the Tax Court Judge did not commit any error in weighing the interests of justice against the timing of the application. As the Tax Court Judge noted, there is a history of delays in providing information by AgraCity or persons related to AgraCity and he was "not convinced that a wait and see approach is an expeditious way of proceeding in this matter".

[30] By requiring a full disclosure of all documents by AgraCity at this stage of the proceedings it may well assist in determining, before discovery, what transpired between or among the various companies during the years in question and may shorten the discovery examinations and reduce the number of undertakings that would have to be provided at discovery.

[31] As a result, I would dismiss AgraCity's appeal in relation to this issue:

Paragraphs 247(2)(a) and (c) of the Act

[32] Subsection 247(2) of the *Act* is as follows:

247 (2) Where a taxpayer or a partnership and a non-resident person with whom the taxpayer or the partnership, or a member of the partnership, does not deal at arm's length (or a partnership of which the non-resident person is a member) are participants in a transaction or a series of transactions and

247(2) Lorsqu'un contribuable ou une société de personnes et une personne non-résidente avec laquelle le contribuable ou la société de personnes, ou un associé de cette dernière, a un lien de dépendance, ou une société de personnes dont la personne non-résidente est un associé, prennent part à une opération ou à une série d'opérations et que, selon le cas :

(a) the terms or conditions made or imposed, in respect of the transaction or series, between any of the participants in the transaction or series differ from those that would have been made between persons dealing at arm's length, or

a) les modalités conclues ou imposées, relativement à l'opération ou à la série, entre des participants à l'opération ou à la série diffèrent de celles qui auraient été conclues entre personnes sans lien de dépendance,

(b) the transaction or series

b) les faits suivants se vérifient relativement à l'opération ou à la série

(i) would not have been entered into between persons dealing at arm's length, and

(i) elle n'aurait pas été conclue entre personnes sans lien de dépendance,

(ii) can reasonably be considered not to have been entered into primarily for bona fide purposes other than to obtain a tax benefit,

(ii) il est raisonnable de considérer qu'elle n'a pas été principalement conclue pour des objets véritables, si ce n'est l'obtention d'un avantage fiscal,

any amounts that, but for this section and section 245, would be determined for the purposes of this Act in respect of the taxpayer or the partnership for a taxation year or fiscal period shall be adjusted (in this section referred to as an "adjustment") to the quantum or nature of the amounts that would have been determined if,

les montants qui, si ce n'était le présent article et l'article 245, seraient déterminés pour l'application de la présente loi quant au contribuable ou la société de personnes pour une année d'imposition ou un exercice font l'objet d'un redressement de façon qu'ils correspondent à la valeur ou à la nature des montants qui auraient été déterminés si :

(c) where only paragraph (a) applies, the terms and conditions made or imposed, in respect of the transaction or series, between the participants in

c) dans le cas où seul l'alinéa a) s'applique, les modalités conclues ou imposées, relativement à l'opération ou à la série, entre les participants

the transaction or series had been those that would have been made between persons dealing at arm's length, or	avaient été celles qui auraient été conclues entre personnes sans lien de dépendance;
	d) dans le cas où l'alinéa b) s'applique, l'opération ou la série conclue entre les participants avait été celle qui aurait été conclue entre personnes sans lien de dépendance, selon des modalités qui auraient été conclues entre de telles personnes.

[33] It is implicit in the reasons of the Tax Court Judge that he found that, since the Crown assumed that no product had been sold by NewAgco-Barbados, paragraph 247(2)(a) of the *Act* could not apply because no arm's length person would have entered into an agreement to provide services to NewAgco-Barbados in relation to the sale of a product that was not going to be sold by NewAgco-Barbados. As noted above, the Crown's position in the reply related to AgraCity's appeal is that AgraCity is entitled to all of the profit from the sale of ClearOut.

[34] However, this case was decided before this Court released its decision in *Cameco Corp. v. The Queen*, 2015 FCA 143, [2015] F.C.J. No. 774. In that case, the Crown was alleging that the non-resident corporation did not perform any services and therefore the amount that the resident corporation should have paid for services was nil. In confirming the Tax Court Judge's decision to not strike the references to paragraph 247(2)(*a*) and (*c*) in that case, this court stated that:

> **51** No court has determined where paragraphs 247(2)(*a*) and (*c*) end and where 247(2)(*b*) and (*d*) begin and I agree with the Crown that it would be inappropriate to attempt to resolve this issue on a motion to strike (Hunt at paras. 18, 28 and 43). The question whether a nil price can give rise to the application of paragraphs 247(2)(*a*) and (*c*) -- in addition to paragraphs 247(2)(*b*) and (*d*) -- is best left to be decided by the trial judge in the fullness of the evidence (Reasons at para. 27).

[35] In *Cameco*, the allegation of the Crown was that all of the services were provided by the company resident in Canada and therefore no amount should have been paid by that company to the non-resident corporation. The net effect was that the non-resident corporation, in the Crown's view, was not entitled to any profit in relation to the transactions in issue.

[36] Although in *Cameco* the issue was whether the company resident in Canada should have paid nothing while the issue in this case is whether the company resident in Canada should have received all of the amount related to the sale of ClearOut, in both cases the net effect is that all of the profit would be reallocated to the company resident in Canada. In both cases the Crown is arguing that paragraphs 247(2)(*a*) and (*c*) of the Act could effectively allocate all of the profit to the company resident in Canada. Just as in *Cameco*, it seems to me that at this stage of the proceedings the paragraphs of the reply related to paragraphs 247(2)(*a*) and (*c*) of the *Act* should not have been struck and the Tax Court Judge committed an error in doing so.

[37] As a result I would allow the appeal of the Crown in relation to the part of the order striking paragraphs 15(a) and 17 of the reply.

Statements of Law

[38] The Tax Court Judge struck paragraph 14(c) and the first sentence of paragraph (h) from the reply on the basis that this paragraph and this sentence stated conclusions of law.

[39] Paragraph 14(c) and the first sentence of paragraph (h) of the reply are as follows:

> 14. The Deputy Attorney General of Canada further states the following additional facts in support of the reassessments under appeal:
>
> …
>
> c) the series of transactions would not have been entered into between persons dealing at arm's length since no arm's length party would accept the risks of the said series of transactions and yet forego the benefits of the series of transactions given NewAgco-Barbados limited functions, lack of assets and having no employees;
>
> …
>
> h) the series of transactions entered into by AgraCity amounts to a sham or window dressing designed to deceive the Minister into concluding that NewAgco-Barbados, not AgraCity, was undertaking a business and incurring real risks. […]

[40] It seems to me that both of these provisions are questions of mixed fact and law. Paragraph c) would require the judge to determine what persons dealing at arm's length would do in this particular situation. This would require a determination of the applicable standard to be used and then the application of that standard to the facts. As well, whether the facts would lead to the conclusion that the series of transactions is a sham is also a question of mixed fact and law. These statements should not be stated to be facts.

[41] In *Anchor Pointe Energy Ltd. v. Canada*, 2003 FCA 294, [2004] 5 C.T.C. 98 and *Canadian Imperial Bank of Commerce v. The Queen*, 2013 FCA 122, [2013] 4 C.T.C. 218, this Court emphasized the requirement that assumptions of fact must be restricted to only the facts and are not to include statements of mixed fact and law. The facts are to be extricated from such statements. Although paragraph 14 of the reply in this case does not state the facts that were assumed by the Minister in reassessing, it is still indicating that what is included in this

paragraph are facts. The characterization of statements as statements of fact or mixed fact and law does not change simply because these are stated to be additional facts and not stated to be assumed facts. The Crown should not be excused from misidentifying statements of mixed fact and law as statements of fact just because it has included these statements as additional facts.

[42] In any event, the conclusion that arm's length persons would not enter into these transactions is also repeated in paragraphs 15 b) and 18 of the reply, although the basis upon which the Crown is relying to reach this conclusion is missing from these paragraphs. The conclusion that the series of transactions amounts to a sham is also repeated in paragraphs 15 c) and 19 of the reply.

[43] I would dismiss the appeal of the Crown from the Order striking paragraph 14 c) and the first sentence of paragraph 14 h) from the reply.

[44] The Tax Court Judge also ordered that paragraph 14 d) of the reply is to be incorporated into paragraph 15 b). Since this paragraph will still be in the reply, albeit in a different location, and since the Crown has not shown how it would be prejudiced by relocating this paragraph, I would not interfere with this part of the order of the Tax Court Judge.

Penalties

[45] The Tax Court Judge, in paragraph 31 of his reasons, stated that:

> [31] I am not prepared to strike these provisions but am going to allow the Respondent time (two weeks) to straighten them out and clarify whether the penalty is due to knowingly underreporting or underreporting under

> circumstances amounting to gross negligence or, if both, plead in the alternative. If gross negligence is at issue, then the pleadings should be clear what the circumstances are, and if indeed that is why the Respondent made the assumptions in paragraphs 13(b) and (c), though interestingly those assumptions postdate the alleged false statement.

[46] In *The Queen v. O'Dwyer*, 2013 FCA 200, 449 N.R. 285, I stated as follows:

> **31** In setting out the basis upon which the penalty was assessed, the Minister should clearly identify the role that Thomas O'Dwyer is alleged to have played and not simply reiterate every possible permutation or combination that could satisfy the statutory conditions to impose the penalty. Any taxpayer who has been assessed a penalty should know why the penalty was assessed. Simply reiterating the multiple combinations of possibilities that could result in the imposition of the penalty does not tell a taxpayer what specific act (that would result in the imposition of the penalty) he or she is alleged to have committed.

[47] I agree with the Tax Court Judge that these comments from *O'Dwyer* are applicable here and I would dismiss the Crown's appeal from this determination by the Tax Court Judge.

Conclusion

[48] As a result, I would:

(a) dismiss the appeal of AgraCity, with costs, and

(b) allow the cross-appeal of the Crown in part and without costs, and I would amend the Order of the Tax Court of Canada dated November 14, 2014 by deleting the reference to paragraph 15(a) and paragraph 17 from paragraph 1 of this Order. I would allow the Crown thirty days to file and serve an amended reply.

"Wyman W. Webb"

J.A.

“I agree.
Johanne Gauthier J.A.”

“I agree.
D.G. Near J.A.”

FEDERAL COURT OF APPEAL

NAMES OF COUNSEL AND SOLICITORS OF RECORD

APPEAL FROM AN ORDER OF THE HONOURABLE JUSTICE CAMPBELL J. MILLER OF THE TAX COURT OF CANADA DATED OCTOBER 21, 2014, DOCKET NUMBER 2014-1537(IT)G.

DOCKET:	A-511-14
STYLE OF CAUSE:	AGRACITY LTD v. HER MAJESTY THE QUEEN
PLACE OF HEARING:	TORONTO, ONTARIO
DATE OF HEARING:	SEPTEMBER 30, 2015
REASONS FOR JUDGMENT BY:	WEBB J.A.
CONCURRED IN BY:	GAUTHIER J.A. NEAR J.A.
DATED:	DECEMBER 16, 2015

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