Federal Court of Appeal | Cour d'appel fédérale

Date: 20111025

Docket: A-286-10

Citation: 2011 FCA 296

CORAM: **NADON J.A.**
TRUDEL J.A.
MAINVILLE J.A.

BETWEEN:

9056-2059 QUEBEC INC.

Appellant

and

HER MAJESTY THE QUEEN

Respondent

Hearing held at Montréal, Quebec, on September 8, 2011.

Judgment delivered at Ottawa, Ontario, on October 25, 2011.

REASONS FOR JUDGMENT BY: TRUDEL J.A.

CONCURRED IN BY: NADON J.A.
MAINVILLE J.A.

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REASONS FOR JUDGMENT

TRUDEL J.A.

Introduction

[1] This appeal concerns a judgment of the Tax Court of Canada (2010 TCC 358, Justice Tardif [the judge]), by which the appeal of the assessment of 9056-2059 Québec Inc. (9056 or the appellant) in relation to the Goods and Services Tax for the period from February 1, 2002, to December 31, 2005, was dismissed except as regards the penalty resulting from the failure to

collect and remit this net tax. The judge therefore found that the appellant had not demolished any of the Minister's 11 assumptions of fact on which the impugned assessment was founded. I disagree.

[2] I conclude that the appellant has shown that the legislative provision relied on by the Minister in making the assessment at issue does not apply in this case. As a result, I would allow the appeal for the reasons that follow.

[3] The *Excise Tax Act,* R.S.C. 1985, c. E-15 (the ETA), under which the federal government collects tax on products and services, sets out, among other things, which of those products and services are zero-rated supplies, as opposed to taxable supplies. In this case, under section 138 of the ETA, 9056 was deemed to be offering, for a single consideration, multiple (or mixed) supplies, of which the principal supply was taxable. As a result, the other supply was merely incidental to and presumed to be part of the first; it then became taxable although it is non-taxable on its own. The dispute in this appeal pertains essentially to the characterization of the services offered by the appellant and to the application, if appropriate, of the rule set out at section 138 of the ETA to the facts of the case.

[4] To ensure that the facts relevant to this dispute are understood, I reproduce that section below:

138. For the purposes of this Part, where (*a*) a particular property or service is supplied together with any other property or service for a single consideration, and (*b*) it may reasonably be regarded that the provision of the other property or service is incidental to the provision of the particular property or service, the other property or service shall be deemed to form part of the particular property or service so supplied.	**138.** Pour l'application de la présente partie, le bien ou le service dont la livraison ou la prestation peut raisonnablement être considérée comme accessoire à la livraison ou à la prestation d'un autre bien ou service est réputé faire partie de cet autre bien ou service s'ils ont été fournis ensemble pour une contrepartie unique.

Relevant facts

[5] Registered in 1997, 9056 is an agri-tourism business interested in beekeeping. To promote sales of their cottage-industry products, the appellant, and its shareholders Jean-Pierre Binette and Madeleine Courchesne before it, developed on their land a network of intersecting trails in the form of a labyrinth, better known to its users as the "labyrinthe du domaine de la forêt perdue", or labyrinth of the lost forest estate (the labyrinth). These trails provide a setting for engaging in various outdoor activities all year long, including hiking; in-line skating or ice skating; watching deer, moose, elk and other wildlife; etc. (see promotional pamphlet, appeal record, volume II, tab 38). This use was approved, although not without great difficulty, by the

Commission de la protection du territoire agricole du Québec, or Quebec agricultural land protection board (CPTAQ). Indeed, after three previous refusals, the CPTAQ made a decision on April 25, 1997, authorizing non-agricultural use of the land required for 9056's activities, given that this would not cause major harm to the agricultural surroundings and that this project, on the whole, would contribute to agri-tourism development in the region beyond the summer peak season (*ibid*., tab 22, page 195).

[6] There is no doubt that 9056 achieved its aim. Particularly during the winter season, the labyrinth receives a high volume of visitors, which the appellant relies on to sell its honey and honey-based products (the honey or its honey). The appellant also offers other independently sourced, locally produced products.

[7] The marketing strategy is that the user must purchase a farm product to gain access to the trails. The transaction is carried out through the purchase of tickets. The first ticket is sold at $12 for an adult and $10 for a child. In practice, an adult who pays $12 obtains a first farm product, priced at one ticket (assessed at $1.50), and need do nothing more to be able to use the trails that day for as many hours as desired. According to the the appellant's pricing sheet, one ticket can be used to obtain one of the following products: 50 g of honey or maple syrup, a bag of 8 candies, a maple lollipop or a 454-g bag of buckwheat flour. By comparison, a 500-g jar of churned liquid honey, assessed at $6, is priced at 4 tickets, whereas the 1-kg jar, assessed at $9, is priced at 6 tickets. Exceptions aside, additional tickets cost $1.50 each. Those are just a few

examples of the pricing scheme established by 9056 (list of prices of products sold, *ibid*., tab 25, page 211).

[8] By the appellant's own admission, customers thus pay a considerable price for the first ticket and acquire only one farm product of small value. However, customers pay a lower price to purchase subsequent products (appellant's memorandum, paragraph 12). The appellant thus counts on the customers who use the labyrinth to take the opportunity to purchase additional tickets and obtain larger quantities of its honey than the amount available upon purchase of the initial entry ticket.

[9] This is the context in which section 138 of the ETA was raised. The Minister of National Revenue took the position that the sale of honey and the access to the labyrinth were mixed supplies. The honey and other locally produced products offered by 9056 are zero-rated (Schedule VI, Part III, section 1 of the Schedule referred to in subsection 123(1) of the ETA), whereas access to the labyrinth, as the appellant concedes, constitutes admission to a place of amusement, that is, a taxable supply made in the course of a commercial activity (within the meaning of subsection 123(1) of the ETA) (appellant's memorandum, paragraphs 32ff). The Minister of Revenue, of the opinion that the labyrinth was the principal supply and the honey, the incidental supply, took 9056's total sales into account and issued an assessment for net tax in the amount of $36,992.08 with $2,020.87 in interest and a penalty of $4,211.04. Except for the penalty, the judge confirmed the Minister's position.

Standard of review

[10] Section 138 of the ETA requires the application of a legal standard to a set of facts, which is a question of mixed fact and law reviewable by this Court in the event of a palpable and overriding error (*Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235 [*Housen*]).

[11] Furthermore, the statement of this legal standard is a question of law subject to the correctness standard (*Housen* above, paragraph 27; *Camp Mini-Yo-We Inc. v. Canada*, 2006 FCA 413, paragraph 17 [*Camp Mini*]).

Judgment of the Tax Court of Canada

[12] On appeal in the Tax Court of Canada, 9056 took the following alternative legal positions:

> [TRANSLATION]
>
> 7. The appellant's position is unequivocal: the sale of honey and the access to the trail are one and the same supply for the purposes of the ETA.
> 8. This single supply is the sale of honey by the appellant, a zero-rated supply within the meaning of the ETA.
> 9. However, and only in the alternative, the appellant submits that if the sale of honey and the access to the trail are multiple supplies, which it strongly denies, then the access to the trail is incidental to the sale of the honey, under section 138 of the ETA.
> 10. If the Court accepts neither of the appellant's two positions, then the appellant submits, last, that the supply of the honey is not incidental to access to

> the trail and that, therefore, section 138 of the ETA does not apply (additional documents in the appellant's record, volume III, tab 46, page 433).

[13] The judge dismissed the single supply argument. On appeal before this Court, the appelant abandoned that position, and rightly so, in my view. Single supply is generally characterized by the fact that one element of the transaction is so dominated by another element that it loses all identity for tax purposes. *Camp Mini*, above, is a good example of single supply. In that case, the evidence established that it was not possible to charge one amount for the religious services offered to the children who went to Camp Mini-Yo-We and another amount for the recreational and athletic services. This was the context in which section 138 was found to be inapplicable, since there was a single supply having multiple components. The facts in this appeal do not point in that direction at all.

[14] Having made that decision, the judge then analyzed the facts and their application in the context of multiple supplies so as to determine which of the services offered had the features of a principal supply. The appellant asked the judge to find that the honey was the principal supply, thus creating the presumption that the labyrinth was a zero-rated supply having the corresponding tax characteristics.

[15] In support of its theory, the appellant emphasized the CPTAQ's favourable decision authorizing its trail project. The CPTAQ had noted that, in 9056's application, [TRANSLATION] "all [9056] is asking is that existing trails that are also necessary for pick-your-own activities be

used on a need-by-need basis for purposes other than agricultural, either during the summer months for educational and sightseeing purposes, or during the winter months to allow for ice fishing, as with the use of farm land or back-country trails for the installation of snowmobile trails or cross-country skiing" (appeal record, volume II, tab 22, page 195). The CPTAQ stated that it could not [TRANSLATION] "ignore the fact that an authorization of the request would promote the sale of part of the applicant's farm production, which would in turn be beneficial to the development of this agricultural sector's farming activities" (*ibid*.). However, the CPTAQ also stated that it could not [TRANSLATION] "permit the placement of a commercial use not related to agriculture in that area" (*ibid*.).

[16] The appellant asked the judge to make the same finding. Understandably, 9056 was seeking a decision from the Tax Court of Canada that would harmonize with the CPTAQ's decision which was instrumental in making its project a reality.

[17] The judge correctly noted that he had no need to comment on the CPTAQ's decision, as it had no bearing on the tax dispute he had to decide. That decision by the judge was not appealed by 9056 in this Court. CPTAQ's decision will not take precedence over the decision forthcoming in this appeal. The *Act respecting the preservation of agricultural land and agricultural activities*, R.S.Q., c. P-41.1 and the ETA each have very different purposes. The CPTAQ's concern, in the appellant's file, was to ensure that 9056 did not limit the exercise of agricultural activities on the surrounding parcels of land. The Minister of Revenue's concern,

under the ETA, is to ensure that 9056 fulfills its tax responsibilities regarding the Goods and Services Tax.

[18] In that vein, the judge defined the issue as follows:

> [27] The real issue is whether the ticket price served as consideration for the purchase of the very small quantity of honey or other product or admission to the trails. In other words, was the price or amount paid to purchase the ticket a scheme to water down, if not conceal, the actual consideration for admission to the trails?

[19] As stated above, the judge concluded that section 138 of the ETA applied and that 9056 was mainly providing a recreational and tourism service, that is, access to the labyrinth. The sale of honey was merely incidental, within the meaning of the above-stated provision. In reaching that conclusion, the judge took into account the following factors: the disproportion between the price of the first ticket and the real value of the farm product obtained; 9056's advertising campaigns that highlighted the recreational activities; the large visitor turnout during the winter; and the infrastructure put in place to operate the trail system, including the parking lot with a capacity for several hundred vehicles and the Zamboni resurfacer used to maintain the ice (Reasons for Judgment, paragraphs 95, 22, 29 and 64).

[20] The appellant took issue with the fact that the judge did not find the honey to be the principal supply, with the labyrinth being an incidental service. I can find no error here. Given

the evidence in the record, if section 138 applied, I would have made the same finding. I will therefore give no further consideration to this ground of appeal.

[21] We are left with the appellant's argument that section 138 does not apply in this case. The judge wrote the following at paragraph 90 of his reasons:

> On this basis alone [the appellant is doing indirectly what the *Act respecting the preservation of agricultural land and agricultural activities* prevents it from doing directly], I cannot but conclude that the element of multiple supply other than access to the labyrinth should not be included or form part of the taxable supply which is the value of the admission itself. [Emphasis added.]

[22] A careful reading of this paragraph leads the reader to think that the judge accepted 9056's argument. In point of fact, if the judge concluded that the supply of the honey must not be included or must not be presumed to be a taxable supply, and that the taxable supply is to be limited to the value of access to the labyrinth, then no multiple supplies are made within the meaning of the above provision, and this provision cannot resolve the dispute. This Court has already established that section 138 of the ETA applies only in the event of multiple supplies [*Camp Mini*]. However, the judge reaches a different conclusion entirely.

[23] With respect, the only explanation I can find for this inconsistency in the judge's reasons is that he failed to correctly set out the applicable legal standard in this case and apply it to the facts adduced in evidence and accepted by him.

[24] I will therefore begin my analysis with a discussion of section 138 of the ETA and then set forth my reasons for determining that it cannot apply in the case at bar.

Analysis

[25] For convenience, I am reproducing below the language of this section:

138. For the purposes of this Part, where (*a*) a particular property or service is supplied together with any other property or service for a single consideration, and (*b*) it may reasonably be regarded that the provision of the other property or service is incidental to the provision of the particular property or service, the other property or service shall be deemed to form part of the particular property or service so supplied.	**138.** Pour l'application de la présente partie, le bien ou le service dont la livraison ou la prestation peut raisonnablement être considérée comme accessoire à la livraison ou à la prestation d'un autre bien ou service est réputé faire partie de cet autre bien ou service s'ils ont été fournis ensemble pour une contrepartie unique.
[Emphasis added.]	[Je souligne.]

[26] The wording makes it clear that two conditions must be met to establish multiple supplies: (1) two or more supplies must be supplied for a single consideration; and (2) the provision of one of the supplies must be reasonably regarded as being incidental to the provision of the other.

A. Multiple or mixed supplies made for a single consideration

[27] To determine whether the first condition is met, it is useful to recall the rule set out in *O.A. Brown Ltd. v. Canada*, [1995] T.C.J. No. 678, referenced by Justice Sharlow in *Hidden Valley Golf Resort Association v. Canada*, [2000] F.C.J. No. 869, 257 N.R. 164 (FCA) and referenced again at paragraph 28 of *Camp Mini* (above):

> In each case it is useful to consider whether it would be possible to purchase each of the various elements separately and still end up with a useful article or service. For if it is not possible then it is a necessary conclusion that the supply is a compound supply which cannot be split up for tax purposes.

[28] In theory, although 9056's commercial practice, guided by the decision of the CPTAQ, was another matter entirely, the honey and the labyrinth could easily have been the subject of separate transactions. The purchase of the honey and the use of the labyrinth are not interdependent and together do not constitute a single supply with multiple components. The services offered by the appellant are not so closely integrated that they cannot be usefully separated, as was the case in *Camp Mini* (*ibid*.). The evidence also showed that users who

purchase a season's pass to access the labyrinth do not have to purchase a local food product on each visit. 9056 explained that these persons paid more for the first ticket, then sold at a price of $50 (examination of Thérèse Deslauriers, trial transcript, page 166, lines 1 to 10). This first ticket allowed them to purchase one of the products listed at paragraph [7], with additional tickets, if desired, available for $1 apiece.

[29] On this basis, I conclude that the first condition of section 138 has been met. I will now consider the second condition.

B. Multiple supplies: the principal supply and the incidental supply

[30] Since there are multiple supplies, which one—the labyrinth or the honey—is incidental to the other? Or, to quote the judge, "[was] access to the rink designed in the form of a labyrinth . . . , for the period covered by the assessment, an exempt supply or rather a taxable supply?" (Reasons for Judgment, paragraph 19).

[31] As stated above, the judge concluded that the honey was incidental to the labyrinth. The judge provided the following explanation of his reasoning in support of that conclusion:

> [58] Generally speaking, those inseparable things or components are often intangible. Nevertheless, when dealing with, as in the case bar [*sic*], individual goods that have absolutely nothing in common, this instantly raises a number of questions for the purposes of identifying what is primary as opposed to incidental.

> [59] Although there are a number of decisions in this area, there is no objective formula or magic recipe with various criteria making it possible to obtain a decisive and reliable result.
>
> [60] I am of the view that the process and analysis must be guided by a basic common sense approach within a context of reasonableness. . . .

[32] It is true that little enough of Canadian case law deals with the provision considered here. Although this Court and the Tax Court of Canada have examined the applicability of section 138 of the ETA on a few occasions, no decision deals with it in detail or sets out a test for assessing the incidental nature of a supply (see *Camp Mini*, above; *Locator of Missing Heirs Inc. v. Canada*, [1997] F.C.J. No. 528 (FCA), paragraph 14; *Sterling Business Academy Inc. v. Canada*, [1998] T.C.J. No. 1106 (TCC), paragraph 22 [*Sterling*] following *Minister of National Revenue v. Estate of Cunnumparathu Abraham Zachariah*, [1970] 70 D.T.C. 6326 (TCC) [*Zachariah*]; *Oxford Frozen Foods Ltd. v. Canada*, [1996] T.C.J. No. 1222 (TCC), paragraphs 29 and 32; *Robertson v. Canada*, [2002] T.C.J. No. 48 (TCC), paragraph 145; *Interior Mediquip Ltd. v. Canada*, [1994] T.C.J. No. 1160 (TCC), paragraphs 8 and 10). In fact, in most of these cases, section 138 was excluded because it was a matter of a single supply having multiple components.

[33] Nevertheless, before analyzing the evidence, the judge had to state the legal standard that was to guide his reasoning. In this case, without identifying the rationale for section 138 of the ETA or the definition of the term “incidental” found therein, the judge simply listed 9056’s activities as they related to beekeeping and the labyrinth and concluded that:

> [t]he evidence strongly suggest [*sic*] that the honey, its by-products, maple syrup and other products, were not the dominant elements; rather, they were secondary, as the dominant, primary and/or determining element was admission to the trails. (Reasons for Judgment, paragraph 93). [Emphasis added.]

[34] However, section 138 refers to a secondary element in the sense of minor or non-essential. To fulfill the second condition, it is not enough for the supply or service to be secondary; this supply or service must also be of small value in relation to the principal activity. This is, furthermore, the meaning conveyed by the policy statement P-159R-1 *Meaning of the Phrase Reasonably Regarded as Incidental*, revised on March 8, 1999, concerning multiple supplies (see also *Sterling* and *Zacharias*, referenced at paragraph [32]).

[35] Although administrative interpretations are not binding on the courts, they are entitled to weight and may even constitute an important factor in the interpretation of statutes: *Silicon Graphics Limited v. Canada*, [2003] 1 F.C. 447 (FCA).

[36] This administrative policy explains, first, that section 138 “is intended to deal with recurring commercial transactions where an allocation of the purchase price between two or more items provided together would be administratively cumbersome for the supplier particularly where the transactions are frequent and the dollar value of the property or services is small” (additional documents in the appellant’s record, volume III, tab 46, pages 449ff).

[37] It has not been established from the evidence that it would be administratively cumbersome for the appellant to allocate the price of the first ticket between its honey and labyrinth services. These two supplies are very dissimilar, and each incurs its own operating costs that the applicant can easily identify, as evidenced by its financial documents (*ibid.*, pages 480 to 484, appellant's memorandum, paragraphs 59 to 62).

[38] This policy statement also suggests two questions for determining whether a supply is incidental: (1) Is the supplier's primary objective to provide a particular property or service, or several properties or services together? and (2) Is the value of consideration charged for these several properties or services the same as, or only marginally different from, what the value of the consideration for the particular property or service would be if it were provided alone?

[39] The first question aims to establish the supplier's objective. In this case, the judge found that the appellant was selling admission to its trails in hopes of earning a return on sales of its honey (Reasons for Judgment, paragraph 91). The judge also concluded that the customers primarily sought admission to the trails (*ibid.*, paragraphs 89, 91, 94 and 95). On the basis of the record as it stands, I see no palpable and overriding error warranting the intervention of this Court.

[40] The second question proposed in the policy statement concerns the value of consideration charged for the principal property or service. Generally, where the value of the consideration for

a particular property or service provided together with several other properties or services is the same as, or only marginally different from, what it would be if the particular property or service were provided alone, the provision of the other properties or services may be regarded as incidental to the provision of the particular property or service (appellant's memorandum, paragraph 54).

[41] In this regard, the judge found that the honey "[was] the equivalent of the surprises found in cereal boxes" (Reasons for Judgment, paragraph 94). He deemed the cost of the first ticket to be disproportionate in comparison to the quantity of honey received ($12 for a 50-g jar of honey). For him, the honey had only symbolic worth in respect of the value of the first ticket sold to a customer.

[42] Like the judge, I note the disproportionate gap between the price of the first ticket and the quantity of honey to which the purchaser was entitled. The comparison between the nature and scope of the activities available upon purchase of a ticket, that is, several hours of outdoor activities as opposed to 50 g of honey or a maple lollipop, suggests that the apiary aspect of the transaction is secondary to the recreational and touristic aspect. But this secondary status does not automatically give the honey an incidental role in relation to the other service offered.

[43] In this regard, author David Sherman (David Sherman, *Canada GST Service*, looseleaf, Carswell, pages 138-102) asserts that, in general, "The *de minimis* test used throughout the

legislation and in Revenue Canada's administrative policy is 10%". Examples that come to mind are the manufacturing and processing profits deductions, which are not granted to corporations whose manufacturing activities generate less than 10 percent of the gross sales of all active businesses carried on in Canada (subsection 125.1(3) of the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) [ITA]; "butterfly" transactions, in which the disposition of property is limited to less than 10 percent of its market value in order to ensure the continuity of shareholder interest (paragraph 55(3)(*b*) of the ITA); or, where a charity offers a benefit in return for a donation, the benefit is only considered to have a nominal value where its fair market value does not exceed the lesser of $50 or 10 percent of the amount of the gift (ITA, sections 110.1 and 118.1; Canada Revenue Agency, Interpretation Bulletin IT-110R3, *Gifts and Official Donation Receipts*, revised July 11, 1997).

[44] For the fiscal year ending on December 31, 2005, the evidence in the record shows that the honey accounts for 51 percent of the appellant's sales, while 50 percent of its maintenance costs are attributable to beekeeping (appellant's memorandum, paragraph 61). As well, production costs make up 89 percent of the honey's selling price, which explains why 9056 cannot sell its cottage-industry product at supermarket prices without suffering financial losses (*ibid.*, paragraph 65).

[45] The production costs for honey and the honey-based products are too significant for them to be considered small in comparison to the price of the first ticket. The above-noted policy

emphasizes that section 138 “is intended to apply in situations where the dollar value of the purported incidental supply is small. It generally will not apply to transactions where its application would have significant tax revenue implications”. That is what would happen here, if it applied.

[46] The appellant has satisfied me that the judge erred in not accepting those factors in his analysis of the applicability of section 138. In light of the appropriate legal standard, these facts were sufficient to rebut the Minister’s assumption that farm products were obtained incidentally to payment of admission fees (Reasons for Judgment, paragraph 3(*h*)). [Emphasis added.]

[47] Since I have answered the second question in the negative, section 138 does not apply in the case at bar. For the period at issue, the appellant had to remit only the net tax resulting from its sales in connection with the labyrinth. That is the basis on which 9056 should have been assessed.

Conclusions

[48] I would therefore allow the appeal with costs in both Courts, set aside the judgment of the Tax Court of Canada and, delivering the judgment which that Court should have made, I would vacate the assessment at issue and refer the file back to the Minister of National Revenue for reconsideration and reassessment, taking into account the fact that section 138 of the ETA does

not apply in this case and that the appellant is required to pay the net tax from its sales in connection with the labyrinth and the interest on those amounts.

"Johanne Trudel"
J.A.

"I agree.
M. Nadon J.A."

"I agree.
Robert M. Mainville J.A."

Certified true translation
Sarah Burns

FEDERAL COURT OF APPEAL

NAMES OF COUNSEL AND SOLICITORS OF RECORD

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