Federal Court  Cour fédérale

Date: 20130320

Docket: T-502-12

Citation: 2013 FC 291

Ottawa, Ontario, March 20, 2013

PRESENT: The Honourable Mr. Justice Russell

BETWEEN:

SOFT-MOC INC.

Applicant

and

THE MINISTER OF NATIONAL REVENUE AS REPRESENTED BY THE ATTORNEY GENERAL OF CANADA

Respondent

REASONS FOR JUDGMENT AND JUDGMENT

INTRODUCTION

[1] This is an application for judicial review pursuant to subsection 18.1 of the *Federal Courts Act*, RSC, 1985, F-7, and subsections 231.6(4) and 231.6(5) of the *Income Tax Act*, RSC, 1985, c 1 (5th Supp) (ITA). The Applicant seeks review in respect of a decision (Decision) of the Assistant Director, Toronto East Tax Services Office, Canada Revenue Agency (Director), dated

21 December 2011, to issue a Foreign-Based Information Requirement (Requirement) requiring the Applicant to obtain and provide to the Canada Revenue Agency (CRA) certain foreign-based information and documents.

BACKGROUND

[2] The Applicant is a Canadian resident corporation that sells footwear. Mr. Bryan Bardocz is the President of the Applicant and owns 10% of the Applicant's common shares. Mr. Bert Krista owns, directly or indirectly, 90% of the Applicant's common shares. In 2004, Mr. Krista took up residence in the Bahamas and incorporated the other four corporations involved in this application: ITPC Inc. (ITPC), Manser Inc. (Manser), MWF Inc. (MWF) and SoftPOS Inc. (SoftPOS). Mr. Krista wholly owns these four corporations.

[3] During the course of its operations, the Applicant received services from ITPC, Manser, MWF and SoftPOS, all of whom have their centers of operation in Nassau, Bahamas. During 2005 and 2006, the Applicant paid substantial amounts to these four corporations for a variety of services, such as merchandising services, information technology consulting services, business development services and software licensing fees.

[4] In April 2009, the Minister undertook an audit of the Applicant (Transfer Pricing Audit or TPA). Part of the TPA included a review of the payments made by the Applicant to ITPC, Manser, MWF and SoftPOS as consideration for the services provided by them to the Applicant. The TPA also aimed to determine whether the services said to be provided by the four companies were provided in the Bahamas or in Canada and, if the services were provided in the Bahamas, how they were provided.

[5] The Minister also sought to determine whether the consideration paid by the Applicant to the four companies benefited the Applicant. This determination was to assist in ascertaining whether the transfer price paid by the Applicant was an "arm's length transfer price."

[6] On 6 October 2009, the Applicant received an audit query from the Minister. The Applicant provided a binder of material in response. The Applicant received a second audit query on 28 January 2010, to which it responded on 26 March 2010. On 21 December 2011, the Minister issued the Requirement to the Applicant for foreign-based information pursuant to subsection 231.6(2) of the ITA.

[7] In addition to the Requirement, the Applicant was served with a request to provide certain domestic information dated 16 January 2012. On 20 March 2012, the Applicant provided the Minister with a binder of material in response to this request.

[8] On 24 January 2012, Mr. Bardocz wrote to Terry North, counsel for Mr. Krista, Manser, ITPC, MWF and SoftPOS in the Bahamas, informing him of the Requirement. On 5 March 2012, Mr. North responded to a portion of the 74 questions issued in the Requirement. MWF, ITPC, SoftPOS and Manser declined to provide some of the requested information on the basis that such information did not exist or was confidential and proprietary, or that the release of such information would detrimentally affect the competitive advantage of each corporation.

[9] The following information was not provided by the Applicant in response to the Requirement:

a. Minute books, personnel charts, information relating to the organizational structure and financial statements of ITPC, Manser, MWF and SoftPOS;

b. The names of independent buyers and purchasing agents with whom ITPC networked and any correspondence exchanged with them;

c. The names of industry experts contacted by ITPC in 2005 and 2006;

d. The names of information technology specialists who were involved in providing services, and documents supporting payments made to these specialists;

e. Documents to support payments to a U.S.-based company from Manser, and correspondence exchanged between it and Manser;

f. Whether Manser and SoftPOS provided services to other arm's length or non-arm's length customers and, if so, the names of those customers and a detailed description of the services provided; and

g. The names of employees or external computer contractors hired by Manser and their telephone numbers.

[10] Mr. Bardocz, on behalf of the Applicant, says that he does not know why the information is confidential or proprietary in nature, or how it would affect the competitive advantage of the four companies. Upon receiving the answers provided by the four companies, the Applicant commenced this judicial review.

DECISION UNDER REVIEW

[11] The Decision under review in this application is the Requirement issued by the Director on 21 December 2011. Pursuant to subsection 231.6(2) of the ITA, the Director lays out 74 questions to which the Applicant's previously provided responses from the audit queries were considered incomplete or lacking in detail.

[12] The questions in the Requirement ask for a variety of detailed information about the four Bahamian companies. Employees' names and phone numbers are requested, as is the personal information of external contractors and specialists. There are also questions about service contracts, how business relationships were built up, details about manufacturers, independent buyers and purchasing agents, merchandising agents, marketing and advertising allowances, new retail stores and their images, new products, and sales and customer programs.

[13] The Requirement requests specific details of some of the services provided by Manser to the Applicant. It also requests expenses incurred by Manser, and the cost and profit allocated to the Applicant by Manser. There are also a variety of questions about tradeshows attended by ITPC.

ISSUES

[14] The Applicant raises forward the following issues:

a) Whether the Requirement should be entirely set aside as being unreasonable on account of the following:

i. It is overly broad in scope;

ii. It requires the production of information and documents that are not relevant to the administration or enforcement of the ITA; and

iii. It requests certain information that cannot be obtained or provided by the Applicant because such information is confidential and proprietary, non-existent, or otherwise unavailable; or

b) Whether the Requirement should be varied so as to delete all questions relating to information that cannot be obtained or provided by the Applicant by virtue of such information being confidential and proprietary, non-existent, or otherwise unavailable.

STANDARD OF REVIEW

[15] The Supreme Court of Canada in *Dunsmuir v New Brunswick*, 2008 SCC 9 held that a standard of review analysis need not be conducted in every instance. Instead, where the standard of review applicable to a particular question before the court is well-settled by past jurisprudence, the reviewing court may adopt that standard of review. Only where this search proves fruitless must the reviewing court undertake a consideration of the four factors comprising the standard of review analysis.

[16] In *Saipem Luxembourg S.A. v Canada (Customs and Revenue Agency)*, 2005 FCA 218 [*Saipem*], the Federal Court of Appeal held that the standard of review applicable to a requirement under subsection 231.6 of the ITA is reasonableness. This was also the finding of the Federal Court in *Fidelity Investments Canada Ltd. v Canada (Revenue Agency)*, 2006 FC 551 [*Fidelity*] at paragraph 27.

[17] The Applicant points out that in the context of subsection 231.6, the Requirement may be found to be unreasonable even if all the requested information is relevant to the administration of the ITA. The Federal Court of Appeal said at paragraph 27 of *Saipem*:

> The element which is present in section 231.6, and which is lacking in section 231.2, is the availability of judicial review of the notice of requirement on the ground of unreasonableness. Such a review lacks any substance if a notice of requirement is reasonable simply because the information requested is, or may be, relevant to the administration and enforcement of the Act. Given that Parliament took the trouble to provide for a review on the basis of reasonableness, I conclude that Parliament intended that a notice of requirement in respect of a foreign-based document must not only relate to a document which is relevant to the administration and enforcement of the Act but that it must also not be unreasonable.

[18] When reviewing a decision on the standard of reasonableness, the analysis will be concerned with "the existence of justification, transparency and intelligibility within the decision-making process [and also with] whether the decision falls within a range of possible, acceptable outcomes which are defensible in respect of the facts and law." See *Dunsmuir*, above, at paragraph 47, and *Canada (Minister of Citizenship and Immigration) v Khosa*, 2009 SCC 12 at paragraph 59. Put another way, the Court should intervene only if the Decision was unreasonable in the sense that it falls outside the "range of possible, acceptable outcomes which are defensible in respect of the facts and law."

STATUTORY PROVISIONS

[19] The following provisions of the ITA are applicable:

Definition of "foreign-based information or document"	**Sens de « renseignement ou document étranger »**
231.6 (1) For the purposes of this section, "foreign-based	**231.6** (1) Pour l'application du présent article, un

information or document" means any information or document that is available or located outside Canada and that may be relevant to the administration or enforcement of this Act, including the collection of any amount payable under this Act by any person.

renseignement ou document étranger s'entend d'un renseignement accessible, ou d'un document situé, à l'étranger, qui peut être pris en compte pour l'application ou l'exécution de la présente loi, y compris la perception d'un montant payable par une personne en vertu de la présente loi.

Requirement to provide foreign-based information

Obligation de fournir des renseignements ou documents étrangers

(2) Notwithstanding any other provision of this Act, the Minister may, by notice served personally or by registered or certified mail, require that a person resident in Canada or a non-resident person carrying on business in Canada provide any foreign-based information or document.

(2) Malgré les autres dispositions de la présente loi, le ministre peut, par avis signifié à personne ou envoyé par courrier recommandé ou certifié, exiger d'une personne résidant au Canada ou d'une personne n'y résidant pas mais y exploitant une entreprise de fournir des renseignements ou documents étrangers.

[…]

[…]

Review of foreign information requirement

Révision par un juge

(4) The person on whom a notice of a requirement is served under subsection 231.6(2) may, within 90 days after the service of the notice, apply to a judge for a review of the requirement.

4) La personne à qui l'avis est signifié ou envoyé peut, dans les 90 jours suivant la date de signification ou d'envoi, contester, par requête à un juge, la mise en demeure du ministre.

Powers on review

Pouvoirs de révision

(5) On hearing an application under subsection 231.6(4) in respect of a requirement, a

(5) À l'audition de la requête, le juge peut :

judge may

(*a*) confirm the requirement;

(*b*) vary the requirement as the judge considers appropriate in the circumstances; or

(*c*) set aside the requirement if the judge is satisfied that the requirement is unreasonable.

Idem

(6) For the purposes of paragraph 231.6(5)(*c*), the requirement to provide the information or document shall not be considered to be unreasonable because the information or document is under the control of or available to a non-resident person that is not controlled by the person served with the notice of the requirement under subsection 231.6(2) if that person is related to the non-resident person.

[…]

Consequence of failure

(8) If a person fails to comply substantially with a notice served under subsection 231.6(2) and if the notice is not set aside by a judge pursuant to subsection 231.6(5), any court having jurisdiction in a civil proceeding relating to the

a) confirmer la mise en demeure;

b) modifier la mise en demeure de la façon qu'il estime indiquée dans les circonstances;

c) déclarer sans effet la mise en demeure s'il est convaincu que celle-ci est déraisonnable.

Précision

(6) Pour l'application de l'alinéa (5)*c*), le fait que des renseignements ou documents étrangers soient accessibles ou situés chez une personne non-résidente qui n'est pas contrôlée par la personne à qui l'avis est signifié ou envoyé, ou soient sous la garde de cette personne non-résidente, ne rend pas déraisonnable la mise en demeure de fournir ces renseignements ou documents, si ces deux personnes sont liées.

[…]

Conséquences du défaut

(8) Si une personne ne fournit pas la totalité, ou presque, des renseignements ou documents étrangers visés par la mise en demeure signifiée conformément au paragraphe (2) et si la mise en demeure n'est pas déclarée sans effet par un juge en application du

administration or enforcement of this Act shall, on motion of the Minister, prohibit the introduction by that person of any foreign-based information or document covered by that notice.	paragraphe (5), tout tribunal saisi d'une affaire civile portant sur l'application ou l'exécution de la présente loi doit, sur requête du ministre, refuser le dépôt en preuve par cette personne de tout renseignement ou document étranger visé par la mise en demeure.

ARGUMENTS

The Applicant

The Requirement is Overly Broad in Scope

[20] The Applicant says that the information relating to MWF, ITPC, SoftPOS and Manser was requested by the CRA in order to assist in determining:

a) Whether the services were provided in the Bahamas or in Canada, and if provided in the Bahamas how they were provided; and

b) What is the most appropriate transfer pricing methodology for consideration paid by the Applicant to the four Bahamian companies, and whether the services were paid for at an "arm's length transfer price."

The Applicant submits that the information requested by the CRA goes well beyond what is necessary to enable the CRA to make determinations on the above issues.

[21] The Requirement requested the following information in questions 1-5, 8, 14, 23, 24, 29, 32 and 52:

a. The names of IT specialists involved in the services provided by Manser and documents supporting the payments made thereto;

b. Extensive details about a United States-based computer company that provided services to Manser, such as copies of emails and other correspondences, the name of the contact person, dates and details of services performed, the applicable service contract and documentation supporting payment for services;

c. Information about services Manser provided to any customers besides the Applicant;

d. Minute books, financial statements and a list of directors and employees for all four companies;

e. The names and telephone numbers of anyone hired by Manser to perform services for the Applicant;

f. A breakdown and details of the costs and profits allocated to the Applicant by Manser;

g. The names of independent buyers and purchasing agents with whom ITPC networked, as well as correspondences with these parties;

h. The names of industry experts contacted by ITPC; and

i. The names of other buyers with whom ITPC networked to discuss upcoming trends.

[22] The Applicant says that it has already provided the CRA with a significant amount of information for purposes of the Requirement. Specifically, it has provided:

a. Details of the processes whereby each of the four companies provided services to the Applicant; and

b. Background documentation such as correspondence, names and contact information supporting the services performed by each of the four companies for the Applicant.

[23] In *Saipem*, above, the requirement at issue sought "information, and production of all invoices, correspondence, agreements, contracts with amendments, financial statements, books and records of account, reports, memoranda, schedules, working papers, minutes of meetings, telexes, faxes or other documents…" The information was sought in order to carry out a general audit of the applicant's affairs with a view to determining its Canadian tax liability. The Federal Court of Appeal described the information sought by the CRA at paragraph 32 of *Saipem* as follows:

> In *Merko* and *Bernick*, the notices of requirement called for the production of records relating to a specific transaction in respect of which the taxpayer was claiming a tax benefit. The link between the documents whose production was sought and the individual's tax liability is obvious and reasonable. In this case, the notice of requirement requires Saipem to produce the whole of its corporate documentation for two fiscal years. The link between the documents to be produced and Saipem's liability for tax is more remote.

[24] The Applicant submits that the Requirement at issue in the present case requests the production of information even more remote than the information requested in *Saipem*. The CRA has essentially requested the whole of the corporate documentation of four separate foreign corporations. In addition, the purpose of the requirement in *Saipem* was to conduct a general audit. The purpose of the Requirement in the present case is not general; it is to determine the location from which ITPC, Manser, MWF and SoftPOS provided services to the Applicant, the manner in

which those services were provided, and the appropriate transfer pricing methodology that should be applied.

[25] In *Maheux c Canada (Procureur général)*, 1999 CarswellQue 1176 [*Maheux*], the requirement was issued in order to allow the CRA to confirm certain deductions for business losses claimed by a group of investors in their Canadian income tax returns. Part of this involved the consideration of certain payments that had been made to the foreign company in exchange for services allegedly provided by the foreign company. The Requirement at issue in the present case demanded the production of information such as minute books, the general ledger, sales records, salary records, bank statements, financial statements, and information relating to the business carried on by that foreign company. The Court in *Maheux* found the requirement to be overly broad, and that it should have been limited to information concerning the deductions. The Court varied the requirement so that the applicant was only ordered to provide confirmation of certain expenses which led to the deductions that were claimed by the group of investors.

[26] The Applicant submits that, as in *Maheux*, the Requirement in the present case was issued for a specific purpose: to allow the CRA to determine the location from which ITPC, Manser, MWF and SoftPOS provided services to the Applicant, the manner in which those services were provided, and the appropriate transfer pricing methodology to be applied. The Applicant submits that the Requirement requests a variety of information that is not relevant to this purpose, and that the Requirement should be limited to information that is relevant to the Minister's stated purpose.

[27] Given the narrow parameters of the Minister's stated purpose in the present case, the Applicant says that the request to provide minute books, names of executive directors, minutes of board meetings, organization charts, personnel charts and financial statements is overly broad and

amounts to a "fishing expedition" by the CRA. In addition, the request to provide highly specific business and trade information possessed by Manser and ITPC is overly broad, not necessary and/or irrelevant, and the Applicant submits it is unreasonable for the CRA to require the Applicant to provide this information.

[28] The Applicant further submits that it has already provided the CRA with detailed and substantive information that is sufficient to reach determinations on the issues identified as the purpose of the TPA. Had the CRA given proper consideration to these materials, the Requirement may not have been necessary, or the questions in the Requirement could have been substantially more focused and concise.

[29] Mr. Nick Yiu, the CRA auditor assigned to this matter, was unable to identify any other audits of retail businesses that he had conducted. The Applicant submits that this indicates that he lacked experience in conducting international audits of retail businesses. Prior to the issuance of the Requirement, Mr. Yiu made no attempt to interview Mr. Krista, who Mr. Yiu states is a substantial shareholder of the Applicant. He briefly interviewed Mr. Bardocz once, as well as Mr. Matthew Wall, who was a short-term advisor to the Applicant.

[30] After Mr. Yiu's initial meeting with Mr. Bardocz, he did not request any additional follow-up meetings. Mr. Yiu admitted in his cross-examination that this was unusual in the context of a TPA. He also said in his testimony that to the date of cross-examination he had not completed a review of even the domestic materials that he received from the Applicant. The Applicant submits that had Mr. Yiu conducted further interviews with Mr. Bardocz, Mr. Krista or other high-level employees, and if he had completed a review of the materials already given, he could have significantly narrowed the scope of the Requirement.

The Requirement Demands the Production of Information and Documents that are not Relevant to the Administration or Enforcement of the ITA

[31] The test for relevance of foreign-based documents was described in *European Marine Contractors Ltd. v Canada (Customs and Revenue Agency)*, 2004 FC 114 [*European Marine*] at paragraph 23 as follows:

> Thus, the test to be applied is not whether the information requested will be relevant in determining the applicant's Canadian tax liability, but rather whether the information is relevant to the administration of the Act.

[32] The Respondent has taken the position that the four Bahamian companies are related to the Applicant, but this does not in itself make the Requirement reasonable. As the Federal Court said in *Fidelity*, above, at paragraph 32:

> …In light of subsection 231.6(6), the fact that the Applicant is related to FMR Co. and FIMMI does not make the requirement to produce information and documents unreasonable. In my opinion, however, the relationship alone does not make the requirements "reasonable". The factor of relevance must also be satisfied. In my view, there must be evidence that the documents requested are relevant for the purposes of the Act.

[33] In *Fidelity*, the only documents in dispute were the financial statements of two related corporations. The applicant in that case had also offered to disclose the documents subject to certain restrictions. Here, the information sought in the Requirement is far more extensive, and the Applicant has made no explicit or implicit concession of the relevance of any of the documents listed.

[34] The Applicant submits that even if all the information requested is relevant to the administration of the ITA, it is still unreasonable. The information requested by the CRA is not

relevant to making determinations on the specific issues identified in the Affidavit of Mr. Yiu. The detailed information requested in the Requirement is entirely irrelevant to the administration of the ITA as it relates to the Applicant, and cannot assist the CRA in determining the location from which services were provided, the manner in which services were provided, or the appropriate transfer pricing methodology.

[35] The Applicant further submits that section 231.6 "pertains only to information as to a particular taxpayer in question." In *eBay Canada Ltd. v Canada (Minister of National Revenue – M.N.R.)*, 2007 FC 930 at paragraph 22 the Court provided as follows:

> The Applicants argue that since section 231.6 makes express provision whereby the Minister can seek information from foreign sources, section 231.2 must be read such that it contemplates only information resident in Canada. Counsel for the Minister argues that section 231.6 is more restrictive than section 231.2 in that section 231.6 pertains only to information as to a particular taxpayer in question whereas section 231.2 pertains to "any information" and to "any person" so long as the purposes are genuinely those contemplated by the *Income Tax Act*.

[36] The Applicant submits that the information about MWF, ITPC, SoftPOS and Manser requested in the Requirement relates only to those corporations, and not to the Applicant. Therefore, such documents are outside the scope of subsection 231.6 of the ITA.

The Requirement Demands Information that Cannot be Obtained or Provided by the Applicant Because Such Information is Confidential and Proprietary, Non-existent, or Otherwise Unavailable

[37] In *Fidelity*, the requirement at issue sought the financial statements of two related foreign companies. The Court was satisfied the financial statements in question were essentially confidential, and held at paragraphs 42-43:

> Section 231.6 does not identify the confidential nature of information as a basis for non-disclosure when a notice is issued pursuant to this provision. There is no evidence to suggest that the Respondent is engaged in a "fishing trip" for the purpose of using the financial statements of FIMMI and FMR Co. other than in the conduct of an audit of the Applicant. In general, the Minister is subject to the obligation of acting in good faith. That obligation has been recognized by the Courts in respect of notices issued pursuant to section 231.2 of the Act; see *M.N.R. v. Sand Exploration Ltd.*, [1995] 3 F.C. 44 (T.D.). I see no reason in principle why the same obligation of good faith would not exist with respect to notices issued pursuant to section 231.6 of the Act.
>
> That being so, I conclude that the Applicant's concerns about the confidential nature of the financial statements in issue do not establish that the request for their production is unreasonable…

[38] The Applicant submits the issue of confidentiality in the present application can be distinguished from *Fidelity* in two respects. First, the information requested in this Requirement is far more extensive than that requested in *Fidelity*. The Requirement here demands the production of a significant amount of corporate information, as well as sensitive details regarding business practices and procedures of four foreign corporations.

[39] Secondly, the issue in *Fidelity* was the disclosure of the financial statements to the CRA. Here, the issue is the disclosure of the information to the Applicant. The four Bahamian corporations do not wish to provide this information to anyone, including the Applicant. In particular, Manser and ITPC do not want to provide the contact information of and correspondence with buyers and purchasing agents, industry experts, IT specialists, other customers, and employees.

[40] The value of the services performed by MWF, ITPC, SoftPOS and Manser derives from their specific industry knowledge. For these corporations to divulge the information requested, including to the Applicant itself, would undermine the value of the services. The CRA's attempt to value these services should not destroy their value in the process.

[41] The Applicant acknowledges that subsection 231.6(6) of the ITA says that a requirement shall not be considered unreasonable because the information requested is under the control of a non-resident person and the Applicant is related to that person. However, as established in *Fidelity*, the fact that the parties are related does not make the Requirement reasonable. The Applicant submits that the extent and nature of the information sought by the CRA is such that the Requirement is unreasonable and should be set aside.

Consequences of Failure to Comply

[42] The Federal Court of Appeal described the potential consequences of a failure to comply with a requirement at paragraph 24 of *Saipem*:

> …the recipient of a notice of requirement is not free to choose which of the documents demanded he will produce, as suggested in the learned judge's reasons. Subsection 231.6(8) is explicit that if the notice of requirement is not "substantially complied with", the court may make an order which "prohibit[s] the introduction by that person of any foreign-based information or document covered by that notice" [emphasis added]. Consequently, even if the taxpayer partially complies with the Requirement, the court can order than none of the material covered by the notice can be tendered, not even those documents which have been produced. Thus, the broader the demand, the more drastic the consequences of non-compliance.

[43] The Applicant says that the risk it faces from the potential application of subsection 231.6(8) is enhanced by the uncertainty of the application of the subsection, which is not definitively determined on a judicial review of a requirement but in the course of a future civil proceeding. As

described in *1144020 Ontario Ltd. v Canada (Minister of National Revenue – M.N.R.)*, 2005 FC 813 at paragraph 78:

> In my view, it is not appropriate that this Court issue such a declaration of substantial compliance, at least in the circumstances of the present case. While the Court has the evidence of the applicant's deponents that the applicant has complied with the foreign-based requirements, there is no independent means of verifying the accuracy of this evidence. The proper time and forum for the determination of substantial compliance is when, in any civil proceeding relating to the administration or enforcement of the Act, the applicant attempts to introduce information or a document that the Minister believes was covered by the foreign-based requirements.

[44] The Applicant submits that it has already provided significant information to the CRA in response to the Requirement, and that the risk of holding that it has failed to substantially comply with the Requirement is unfairly prejudicial to the Applicant, considering its overly broad scope.

Conclusion and Relief Sought

[45] The Applicant reiterates that the Requirement is unreasonable because it is overly broad in scope, it requires production of information that is irrelevant to the administration of the ITA and the stated purpose of the Requirement, and it requires the production of confidential information from third parties which, if disclosed, would destroy the value of the services provided by those third parties. In addition, the broad scope of the Requirement creates a risk the Applicant will lose recourse to information legitimately provided in response to the Requirement. Accordingly, the Applicant submits the Requirement is unreasonable and should be set aside.

[46] In the alternative, the Applicant submits the Requirement should be varied to delete all questions relating to information that cannot be obtained or provided by the Applicant by virtue of such information being confidential and proprietary, non-existent or otherwise unavailable.

Specifically, the Applicant requests the following questions in the Requirement be varied or deleted: 1-5, 8, 14, 15, 23, 24, 29, 32, 52.

The Respondent

[47] The Respondent points out that section 231.6 of the ITA gives the Minister strong, comprehensive and far-reaching powers to secure foreign based information or documents which "may be relevant to the administration or enforcement" of the ITA (*Merko v Canada (Minister of National Revenue – M.N.R.)*, [1991] 1 FC 239 at paragraph 24). The Respondent submits that the Requirement is reasonable as it seeks relevant and necessary information and documents, it is not overly broad, and the material sought is available.

The Material Sought is for a Purpose Related to the Administration and Enforcement of the ITA

[48] Obtaining information and documents relevant to the tax liability of a taxpayer through the issuance of a requirement is a purpose related to the administration and enforcement of the ITA. Subsection 231.6(1) says that foreign-based information includes any information or document "that may be relevant to the administration or enforcement of this Act" [emphasis added].

[49] The Respondent points out that a requirement issued under section 231.2 of the ITA is valid if the requested information may be relevant for the determination of the tax liability of a taxpayer. The case law establishes that the threshold for relevance is low (see *Tower v Canada (Minister of National Revenue – M.N.R.)*, 2003 FCA 307 at paragraph 29; *Fraser Milner Casgrain LLP and Gilbert Schmunk v The Minister of National Revenue*, 2002 DTC 7310 (FCTD) at paragraphs 20-27). The threshold for relevance for a requirement issued under subsection 231.6 is similarly low.

Furthermore, the Minister has no way of knowing whether the material sought is relevant until she has had an opportunity to examine that material (*AGT Ltd. v Canada (Attorney General)*, [1997] 2 FC 878 (FCA) at paragraph 23).

The Material Sought is Relevant and Necessary

[50] The Affidavit of Mr. Yiu clearly sets out why this material is necessary and how it is relevant to the administration and enforcement of the ITA. He maintains that the information is required in order to determine from which location the services of the four Bahamian companies were provided, and to determine the proper transfer-pricing methodology. Mr. Yiu maintained on cross-examination that this information is required for him to properly perform the TPA.

[51] The Requirement seeks specific information and documents from the four companies related to the services they provide to the Applicant, how the services are provided, and who within the company provides the services. This material will enable the Minister to perform a functional analysis and determine where and how the services were provided. The Requirement also seeks corporate and financial materials to enable the Minister to determine the appropriate transfer pricing methodology to apply so that she can determine whether the transfer price paid by the Applicant was an arm's length transfer price.

[52] The Applicant says that the material sought is "entirely irrelevant" to the administration of the ITA as it relates to the Applicant, but the Respondent submits that this is incorrect. On cross-examination, Mr. Yiu said that he conducts interviews with the people who run companies as part of the audit. In order to conduct interviews, the CRA requires the names of executive directors and must have access to organizational and personnel charts.

[53] With respect to the other information, Mr. Yiu was clear that the material was sought in order to verify the answers previously provided by the Applicant. Mr. Yiu explained that he needs to verify that the services provided by the four companies exist, and who performs them (see page 196 of the Respondent's Record). Thus, the Respondent submits the information sought is relevant.

The Requirement is not Overly Broad

[54] Given that the information sought from the Applicant is necessary and relevant to the ongoing TPA, the Respondent submits that the Requirement is not overly broad. The Applicant characterizes the CRA's purpose as having "narrow parameters," and argues that the Requirement amounts to a "fishing expedition." The Respondent submits that this characterization is inaccurate and fails to appreciate the complex nature of a TPA and the type of information that is needed to verify that the transfer price paid by the Applicant to the four companies is an arm's length transfer price.

[55] Guidance as to the nature or type of information and documents to be obtained as part of a TPA is found in the CRA's Information Circular 87-2R as well as the 2010 Organization for Economic Co-operation and Development Transfer Pricing Guidelines for Multinational Enterprises and Administration (the Guidelines). The Guidelines explain the wide variety of documentation that ought to be considered in determining a transfer pricing methodology (page 44 of the Respondent's Record).

[56] Mr. Yiu explained in his affidavit and cross-examination that the first step is to review the function provided by the offshore entity. Function refers to what services are provided by the staff of the off-shore entity and the Canadian company. It is necessary to determine if the functions exist

before the appropriate methodology can be selected. This is determined after a review of documents that would indicate that the services were in fact performed. Mr. Yiu explains in his affidavit that at this stage, the CRA does not have enough information to determine which pricing methodology to use (page 6 of the Respondent's Record).

[57] In *Saipem*, above, the Federal Court of Appeal held it was reasonable for the Minister to require production of the whole of the foreign company's corporate documentation for two fiscal years. The Applicant seeks to distinguish that case on the basis that the Minister's stated purpose was to perform a general audit, whereas here the Minister's purpose is to conduct a narrower TPA. The Respondent submits this is simply not the case. Part of the general audit in *Saipem* was to determine whether the company had a permanent establishment in Canada. To do so, production of the corporate documents was required. Here, the Minister seeks information to determine whether the services were performed in the Bahamas or in Canada, and if performed in the Bahamas how they were provided, in order to determine the appropriate transfer pricing methodology. The information sought from the Applicant is necessary to make those determinations.

[58] The Applicant also relies on the decision in *Maheux*. The evidence given by the principal of the foreign company in that case was that the requirement sought information that included business dealings of the foreign company that did not involve the Canadian taxpayers. The Court limited the requirement to the information in the possession of the foreign company that related to the Canadian taxpayers (*Maheux* at paragraphs 34-35).

[59] The Respondent submits that, unlike in *Maheux*, the Requirement in this case does not inadvertently capture the four companies' other business dealings. There is no evidence that these

companies had any business dealings with any persons other than the Applicant at the material time. In fact, the evidence is that the Applicant is MWF, SoftPOS and ITPC's only client.

[60] The Applicant proposes that the scope of the Requirement can be narrowed and that Mr. Yiu should interview certain people. The Federal Court of Appeal made clear in *Saipem* that it is not up to the Applicant to say how the CRA should conduct its audit. The Federal Court of Appeal said at paragraph 36 of *Saipem* that "It is the Agency's prerogative as to whether it will conduct an audit, and what form that audit will take."

[61] The Applicant also suggests that the information and documents provided to date provide a response to the Requirement. The Respondent submits that there is no evidence before this Court to support this suggestion.

[62] Although the material sought is part of the records of the four companies, it is still relevant and necessary to determine the Applicant's tax liability, and whether the transfer price paid to the four companies for the services provided was at an arm's length transfer price. The Requirement is not overly broad in scope and should not be set aside in whole or in part as it seeks relevant and necessary information that is required in order to properly conduct the TPA of the Applicant's 2005 and 2006 taxation years.

The Information is not Confidential or Proprietary

[63] There is no evidence that the information sought is confidential and/or proprietary. The only evidence before the Court is the affidavit of Mr. Bardocz. In cross-examination, he could not provide an explanation as to why the documents requested were confidential and/or proprietary, and he admitted he never asked any of the four companies for an explanation. He admitted on cross-examination that he never followed up with any of the companies as to why this information would be considered confidential or proprietary.

[64] In any event, the Respondent submits it is not unreasonable to require production of information pursuant to subsection 231.6 even if the information is confidential or proprietary. In *Fidelity*, above, it was found at paragraphs 42-43 that the confidential nature of information is not a basis for non-disclosure pursuant to a requirement issued under subsection 231.6 of the ITA.

[65] The Applicant suggests that the four Bahamian companies do not wish to disclose this information to anyone, including the Applicant, because disclosing the information could "destroy" the very value of the services the four companies provide. The Respondent submits that there is no evidence that disclosure would have any impact on the value of the services provided by the four companies. As previously stated, Mr. Bardocz was unable to explain why this information is confidential and/or proprietary, and there is no other evidence as to how disclosure would impact the value of the services provided by the four companies.

[66] The Applicant and the four companies are related. Mr. Krista owns 90% of the Applicant and 100% of the foreign companies. It is Mr. Krista who empowers Mr. Bardocz to run the Applicant in Canada. The Applicant is MWF, SoftPOS and ITPC's only client. The Respondent states that it is disingenuous to argue that, as owner of the four foreign companies, Mr. Krista refuses to disclose the information to the Applicant.

[67] The Respondent also questions whether the Applicant could or would use the information in any way to the detriment of the four companies. Given that the Applicant is MWF, SoftPOS and ITPC's only client, the only way the information could affect the services they provide would be if the Applicant chose to alter their arrangement.

[68] The ITA specifically prohibits this type of attempt to shelter information at subsection 231.6(6):

(6) For the purposes of paragraph 231.6(5)(*c*), the requirement to provide the information or document shall not be considered to be unreasonable because the information or document is under the control of or available to a non-resident person that is not controlled by the person served with the notice of the requirement under subsection 231.6(2) if that person is related to the non-resident person.	(6) Pour l'application de l'alinéa (5)*c*), le fait que des renseignements ou documents étrangers soient accessibles ou situés chez une personne non-résidente qui n'est pas contrôlée par la personne à qui l'avis est signifié ou envoyé, ou soient sous la garde de cette personne non-résidente, ne rend pas déraisonnable la mise en demeure de fournir ces renseignements ou documents, si ces deux personnes sont liées.

[69] The Respondent submits it is not open to the Applicant to argue that the Requirement is unreasonable because the information being sought is in the hands of the four companies, which are related to the Applicant.

[70] To the extent that the Applicant has concerns with disclosing the information to the Minister, the Court in *Fidelity* noted at paragraph 42 that the Minister is subject to an obligation to act in good faith. As established in that case, concerns with providing information to the CRA do not establish that production is unreasonable.

[71] The Respondent submits there is no evidence that disclosing the information will impact the value of the services the four companies provide. Therefore, the confidential and/or proprietary nature of the information is no basis for limiting the information sought under the Requirement.

Consequences of the Failure to Comply

[72] Where the information sought by the Minister is both necessary and relevant to the TPA, subsection 231.6(8) operates as it should to prevent abuse. The Respondent submits that if individuals were permitted to pick and chose what information to provide, and then later during a civil proceeding they are permitted to rely on only what they choose to provide, there is potential for them to create a completely inaccurate representation of their tax affairs.

[73] The Respondent takes the position that the information in this case is both necessary and relevant to the TPA issues, and the potential consequences for failing to disclose are no basis for narrowing or setting aside the Requirement.

ANALYSIS

Broadness and the Relevance of the Information Requested in the Requirement

[74] The Applicant's position is that the information and documents requested by CRA go well beyond what is necessary to enable CRA to make determinations on the issues of concern under the TPA. Relying upon *Saipem*, above, the Applicant says that not only was the information and documentation requested not relevant to the administration and enforcement of the ITA, it amounted to a far-reaching fishing expedition.

[75] In the present case, it is true that the Requirement was issued for specific purposes:

a. To allow CRA to see or determine the location from which ITPC, Manser, MWF and SoftPOS provided services to the Applicant;

b. To allow CRA to determine the manner in which the services were provided; and

c. To allow CRA to determine the appropriate transfer pricing methodology.

[76] The Applicant's complaint is that, given these objectives, the requirement to produce minute books, organization charts, personnel charts, and financial statements for each of the four Bahamian companies is overly broad, and the requirement to produce information related to the highly specific business and trade information of the four companies is overly broad, unnecessary, irrelevant, and unreasonable. Due consideration to the materials provided to date, or an interview with Mr. Krista would have provided sufficient information for the specific purposes or would have significantly narrowed the scope of the Requirement.

[77] In his affidavit and on cross-examination, Mr. Yiu explains the analysis that is required to determine an appropriate transfer pricing methodology. As part of this process, it is necessary to document whether the services were in fact performed at the material time. It is also necessary to ascertain and confirm what functions were provided by the four Bahamian companies and the Applicant. However, before the appropriate transfer pricing methodology is selected CRA has to ascertain if the functions of all these companies exist and were performed. As Mr. Yiu explains in his affidavit, all of the documentation requested was needed to assess the arms-length issue because CRA needs to know the who, what, where and how of how the services were provided to the Applicant in a situation where the Applicant and the four Bahamian companies were owned and controlled by Mr. Krista. Any information already provided by the Applicant needs to be verified.

Under this kind of TPA the quality of information provided cannot be ascertained without verification.

[78] In my view, the Applicant has not convincingly challenged Mr. Yiu's evidence that this was the best evidence for CRA to seek for the purposes of the TPA.

[79] In this case, CRA is conducting a TPA of the Applicant. In connection with that TPA, the Minister is reviewing the payments made by the Applicant to the four Bahamian companies for the services. The Minister seeks specific information related to those payments to determine whether the services were performed in the Bahamas or Canada and, if in the Bahamas, how the services were provided, and to determine the appropriate transfer pricing methodology to be applied so that the Minister can ascertain whether the transfer price paid was an arms-length transfer. In my view, the information sought from the Applicant is necessary to make these determinations and to verify information that has already been provided.

[80] Also, in my view, the link between the information and documentation requested and the purposes of the TPA is both obvious and reasonable. As in *Saipem*, at paragraph 36:

> It is the Agency's prerogative as to whether it will conduct an audit, and what form that audit will take. Given that the records in question are, by definition, maintained outside Canada, the Agency can do little more to gain access to the records than issue the notice of requirement which it issued here. If the result is an audit which does not meet the Agency's usual standards, it is nonetheless the best audit the Agency can conduct in the circumstances. As a result, I conclude that the Agency's determination to conduct an audit supports the scope of the notice of requirement served upon Saipem by the Minister.

[81] Subsection 231.6 of ITA makes it clear that "foreign-based information or document" means any information or document that is available, or located outside of Canada and that "may be

relevant" to the administration or enforcement of the Act, including the collection of any amount payable under the act by any person.

[82] The documents requested in the Requirement need to be both relevant and reasonable, but the cases say that the threshold is low and the powers of the Minister are wide-ranging. See *Tower*, above, at paragraph 29. As the Respondent points out, *Saipem*, above, also makes it clear that it is not for the Applicant to say what will suffice. See paragraph 35.

[83] Further, as the Respondent points out, unlike in *Maheux*, the Requirement issued to the Applicant is this case does not inadvertently capture irrelevant business dealings of the four Bahamian companies. This is because there is no evidence to indicate that these companies do business with anyone else except the Applicant. The Applicant is the only client of three of the companies. This justifies the scope of the documentation and information requested. Mr. Krista owns, either directly or indirectly, 90% of the Applicant's common shares. He ceased doing business in Canada in 2004 and took up residency in the Bahamas, whereupon he incorporated the four companies to provide services to the Applicant. Mr. Krista owns 100% of the common shares of the Bahamian companies. During 2005 and 2006, the Applicant paid substantial amounts of money to the four Bahamian companies as consideration for a variety of services to be provided to the Applicant.

[84] Given these arrangements, it is obvious that the information which the CRA seeks may well be part of the corporate and other documents requested in the Requirement, and it is not for the Applicant to say that such information could be ascertained by other means. See *Saipem*, above, at paragraph 36. Even an interview with Mr. Krista would not have provided the CRA with the objective confirmation it requires to complete the TPA. In my view, then, the Requirement is not

overly broad in scope because it seeks relevant and necessary information to properly conduct the TPA for the 2005 and 2006 taxation years and assess the Applicant's tax liability and whether the transfer price paid by the Applicant to the four Bahamian companies for the services was an arms-length transfer price. Documentation and information requested in the Requirement are both relevant and reasonable.

Information in Confidential and Proprietary, Non-existent, or Otherwise Unavailable

[85] The Applicant seeks to distinguish the present situation from that in *Fidelity*, above, in several ways. The Applicant says that, in *Fidelity*, the Court was only dealing with allegedly confidential financial statements for two related companies. In the present case, the Requirement seeks the production of significant corporate documentation, as well as sensitive details regarding business practices and procedures of the four Bahamian companies.

[86] The Applicant provides little in the way of evidence to establish that the corporate documentation and business practices and procedures in question are confidential or proprietary or sensitive. There is no reason to distinguish the present situation from the guidance given in *Fidelity* on point:

> In *Fidelity* the Applicant argued that the requirement at issue was unreasonable, in part because the documents sought by the CRA, being financial statements of two related foreign corporations, were confidential. The Court was satisfied that the financial statements in question were essentially confidential, but held:
>
> > Section 231.6 does not identify the confidential nature of information as a basis for non-disclosure when the notice is issued pursuant to this provision. There is no evidence to suggest that the Respondent is engaged in a "fishing trip" for the purpose of using the financial statements of FIMMI and FM Co. other than in the conduct of an audit of the Applicant. In

> general, the Minister is subject to the obligation of acting in good faith. That obligation has been recognized by the Courts in respect of notices issued pursuant to section 231.2 of the Act; see *Minister of National Revenue v. Sand Exploration Ltd.*, [1995] 3 F.C. 44 (Fed. T.D.). I see no reason in principle why the same obligation of good faith would not exist with respect to notices issued pursuant to section 231.6 of the Act.
>
> That being so, I conclude that the Applicant's concerns about the confidential nature of the financial statements in issue did not establish that the request for their production is unreasonable.
>
> […]

[87] The Applicant also says that the four Bahamian companies are, unlike in *Fidelity*, not refusing to disclose information to CRA; they are refusing to disclose the documentation and information to anyone, including the Applicant.

[88] Given the corporate relationship between the Applicant and the four Bahamian companies, and the control that resides in Mr. Krista, this is equivalent to saying that Mr. Krista refuses to divulge information to the Applicant — a company he controls — from four companies he also controls. In any event, the proprietary or sensitive character of information is not a reason for finding a notice of requirement unreasonable. See *Fidelity*, above, at paragraph 43.

[89] The rationale offered by the Applicant is that the value of the services performed by MWF, ITPC, SoftPOS and Manser derives from the specific industry knowledge, contact information, and other confidential business information possessed by those corporations. It is alleged that for any of these corporations to divulge such information to any person or corporation, including the Applicant itself, would undermine the value of the services to which such information relates.

[90] The Applicant argues that to the extent that the CRA seeks to determine the value of the services performed by MWF, ITPC, SoftPOS and Manser, it would be entirely antithetical to such determination to destroy the value of such services by indirectly forcing MWF, ITPC, SoftPOS and Manser to divulge the very business strategies and practices that allow them to provide such value to the Applicant in the first place.

[91] There is no evidence to support these assertions.

[92] In my view, the relevance and reasonableness of the Requirement have nothing to do with the compellability of either the four Bahamian companies or Mr. Krista. As in *Saipem*, given that the documentation and information are maintained outside of Canada, CRA could do little more to gain access to the records than issue the Requirement. Subsection 231.6(6) of the Act provides as follows:

(6) For the purposes of paragraph 231.6(5)(*c*), the requirement to provide the information or document shall not be considered to be unreasonable because the information or document is under the control of or available to a non-resident person that is not controlled by the person served with the notice of the requirement under subsection 231.6(2) if that person is related to the non-resident person.	(6) Pour l'application de l'alinéa (5)*c*), le fait que des renseignements ou documents étrangers soient accessibles ou situés chez une personne non-résidente qui n'est pas contrôlée par la personne à qui l'avis est signifié ou envoyé, ou soient sous la garde de cette personne non-résidente, ne rend pas déraisonnable la mise en demeure de fournir ces renseignements ou documents, si ces deux personnes sont liées.

There is no evidence before me that it would require an extensive effort to provide the information requested or that providing it would destroy its value as alleged by the Applicant.

[93] The Minister's obligation to act in good faith under the ITA and the protection that this provides has not been challenged before me. There is no basis upon which to set aside this Requirement.

[94] Finally, the consequences of not providing the documentation and information requested as outlined in subsection 231.6(8) of the Act cannot, in my view, have anything to do with the relevance or reasonableness of the Requirement. Mr. Krista and the four Bahamian companies he controls are not compellable, but they have to realize that the Applicant's inability to substantially comply with the Requirement at this stage could lead to future negative consequences for the Applicant. This is, in essence, the purpose behind the issuance of a requirement under the ITA, and the consequences seem wholly appropriate in this case.

JUDGMENT

THIS COURT'S JUDGMENT is that

1. The application is dismissed with costs to the Respondent.

"James Russell"
Judge

FEDERAL COURT

NAME OF COUNSEL AND SOLICITORS OF RECORD

DOCKET:	T-502-12
STYLE OF CAUSE:	**SOFT-MOC INC.**
	- and -
	THE MINISTER OF NATIONAL REVENUE AS REPRESENTED BY THE ATTORNEY GENERAL OF CANADA
PLACE OF HEARING:	Toronto, Ontario
DATE OF HEARING:	February 12, 2013
REASONS FOR JUDGMENT AND JUDGMENT:	HON. MR. JUSTICE RUSSELL
DATED:	March 20, 2013

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