Docket: 2014-1537(IT)G

BETWEEN:

AGRACITY LTD.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on December 3, 4, 5, 6, 10, 11, 12 and 13, 2018 January 28, 29, 30, 31, February 1, 2019, July 15, 16 and 17, 2019 at Toronto, Ontario and September 18, 19 and 20, 2019 at Montreal, Quebec

Before: The Honourable Justice Patrick Boyle

Appearances:

Counsel for the Appellant:	Justin Kutyan Martin Gentile Kristen Duerhammer
Counsel for the Respondent:	Pascal Tétrault Vincent Bourgeois John Krowina

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JUDGMENT

The appeal from the reassessments made under the *Income Tax Act* for the 2007 and 2008 taxation years is allowed, with costs, in accordance with the attached reasons for judgment.

Signed at Montreal, Quebec, this 27th day of August 2020.

"Patrick Boyle"

Boyle J

Docket: 2014-1526(IT)G

BETWEEN:

101072498 SASKATCHEWAN LTD.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on December 3, 4, 5, 6, 10, 11, 12 and 13, January 28, 29, 30, 31, February 1, 2019, July 15, 16 and 17, 2019 at Toronto, Ontario and September 18, 19 and 20, 2019 at Montreal, Quebec

Before: The Honourable Justice Patrick Boyle

Appearances:

Counsel for the Appellant:	Justin Kutyan Martin Gentile Kristen Duerhammer
Counsel for the Respondent:	Pascal Tétrault Vincent Bourgeois John Krowina

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JUDGMENT

The appeal from the reassessments made under the *Income Tax Act* for the 2006 and 2007 taxation years is allowed, with costs, in accordance with the attached reasons for judgment.

Signed at Montreal, Quebec, this 27th day of August 2020.

"Patrick Boyle"

Boyle J.

Citation: 2020 TCC 91
Date: 20200827
Dockets: 2014-1537(IT)G
2014-1526(IT)G

BETWEEN:

AGRACITY LTD.,
101072498 SASKATCHEWAN LTD.,

Appellants,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Boyle J.

[1] These two related appeals are by AgraCity Ltd. ("AgraCity") and 101072498 Saskatchewan Ltd. ("SaskCo"), two related corporations. Both corporations are part of the Farmers of North America group of companies (the "FNA Group"). The FNA Group companies are ultimately controlled by James Mann and/or his brother Jason Mann. AgraCity is wholly owned by Jason Mann; SaskCo is equally owned by James Mann and Jason Mann indirectly through their respective holding companies.

[2] AgraCity had entered into a Services Agreement with NewAgco Inc., a non-arm's length Barbados international business corporation ("NewAgco Barbados") in the years in question in connection with the sale by NewAgco Barbados directly to Canadian farmer-users of a glyphosate-based herbicide ("ClearOut") (being a generic version of Bayer-Monsanto's RoundUp).

[3] In reassessing AgraCity for its 2007 and 2008 taxation years[1] the Canada Revenue Agency ("CRA") relied upon the transfer pricing rules in paragraphs 247(2)(*a*) and (*c*) of the *Income Tax Act* (the "*Act*") and re-allocated an amount equal to all of NewAgco Barbados' profits from these sales activities to the income of AgraCity.

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[1] FYE March 31st.

[4] In its Amended Reply in this Court the Respondent's position is that:

> 1. The paragraph 247(2)(*a)* and (*c*) transfer pricing provisions justify the reassessments including all of the sales profits in AgraCity's income;
>
> 2. The paragraph 247(2)(*b*) and (*d*) transfer pricing provisions permit the recharacterisation of the transactions because arm's length parties, unlike AgraCity, would not have allowed NewAgco Barbados to be part of the transactions or to make any of the profits; and
>
> 3. The transactions in question amount to a sham or window dressing designed to deceive the CRA into concluding that NewAgco Barbados, not AgraCity, was undertaking the sales business and incurring real risks.

[5] At the opening of trial, the Respondent indicated that sham would be its primary position.

[6] After the evidence was in, the Respondent indicated in its written submissions that its first alternative would be paragraph 247(2)(*b*) and (*d*) recharacterisation and that the paragraph 247(2)(*a*) and (*c*) pricing adjustment would be its second alternative argument.

[7] These effectively reversed the ordering of these three bases of supporting the AgraCity reassessments:

> 1. The Respondent's primary position is now that the transactions were a sham or window dressing;
>
> 2. In the alternative, paragraphs 247(2)(*b*) and (*d*) apply to recharacterise the transactions; and
>
> 3. In the further alternative, paragraphs 247(2)(*a*) and (*c*) result in a transfer pricing adjustment.

[8] AgraCity was reassessed transfer pricing penalties under subsection 247(3) in respect of the transfer pricing adjustments. AgraCity concedes that it can not raise the due diligence defence in that provision since it did not satisfy the

contemporaneous documentation prerequisite to being able to make such an argument.

[9] In addition, AgraCity was assessed a so-called gross negligence penalty under subsection 163(2) in respect of the same income adjustment on the basis that it knowingly understated its income.

[10] SaskCo was reassessed for its 2006 and 2007 taxation years[2] on the basis that the profits of its subsidiary and controlled foreign affiliate NewAgco Barbados constituted foreign accrual property income or fapi. SaskCo was also assessed a late filing penalty under subsection 162(1). The reassessment of SaskCo was a protective assessment issued by the Respondent as an alternative assessment to be relied upon if AgraCity prevailed in its appeals. The Respondent was clear that it did not seek to prevail against both AgraCity and SaskCo.[3]

[11] In the Respondent's written submissions filed following the conclusion of the evidence and days in advance of oral argument, it indicated to the Court and the Appellants that it was conceding the SaskCo appeal. The reason given for this was that there was no evidence that could support a finding that NewAgco Barbados did not deal at arm's length with its Canadian farmer-customers or that NewAgco Barbados sold ClearOut to AgraCity who in turn sold it to farmer-users. Accordingly, the appeal of SaskCo is allowed with costs.[4]

[12] Hereafter in these reasons any reference to the Appellant is a reference to AgraCity.

[13] No other Canadian company in the FNA Group was reassessed to include in its income any of the ClearOut sales profits or any other amount in respect of the transactions involving NewAgco Barbados under the transfer pricing rules in section 247, or by virtue of the sham alleged by the Respondent, or in respect of the conferral or receipt of any benefit, or otherwise.

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2 FYE December 31st.

3 This aspect of the reassessments of both taxpayers was the subject of previous procedural litigation in this Court and in the Federal Court of Appeal (2015 FCA 288).

4 While the Respondent concedes the Saskco appeal, it purports to do so without costs. The control of costs awards is not within the Respondent's unilateral control.

[14] The Respondent has not relied upon the general anti-avoidance rule GAAR set out in section 245 of the *Act*, although paragraphs 247(2)(*b*) and (*d*) set out a specific anti-avoidance rule that in part uses somewhat similar concepts.

[15] The dispute in this Court has been defined by the parties, initially by the Respondent's reassessments, and thereafter by both parties' pleadings. It is not open to this Court to make it about something or someone else.

[16] The Appellant's position was to focus on demolishing the Respondent's key assumptions, which are primarily those dealing with (i) the purchase and sale of the ClearOut by NewAgco Barbados, (ii) the legitimacy of the Services Agreement, (iii) the risks taken or borne by NewAgco Barbados in the transactions eg. inventory, foreign currency etc., and (iv) NewAgco Barbados being a key party participating in the transactions that brought real value eg: sourcing of ClearOut etc.[5]

The Tax Law Principles and Provisions Engaged

(1) Sham or Window Dressing

[17] The issue of whether the sale structure was a sham requires the Court to consider whether AgraCity entered into agreements and transactions that were intended to deceive and mislead others, primarily the Respondent, into believing that the rights and obligations between the Appellant and related parties were different than what they truly were. The deceit can be evident from looking at both how the transactions were constructed and how they were conducted: *Continental Bank Leasing Corp. v. HMQ* [1998] 2 SCR 298 at paragraph 20.

[18] The classic definition of a sham is set out in *Snook v. London & West Riding Investments Ltd*., [1967] 1 All ER. 518. The concept of a sham has most recently been set out by this Court in *Cameco Corporation v. The Queen*, 2018 TCC 195 and in *Paletta v. The Queen*, 2019 TCC 205.[6] The Respondent's unsuccessful appeal of *Cameco* to the Federal Court of Appeal[7] did not challenge Justice Owen's decision in this Court that the transactions in question were not a sham.

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5 I am ignoring assumptions in the Amended Reply that are assumptions of law, not fact, or that are conclusions of fact, in identifying those considered key.

6 There is an appeal pending before the Federal Court of Appeal.

7 2020 FCA 112.

[19] In *Paletta* Justice Hogan wrote as follows on the acceptance and interpretation by the Federal Court of Appeal and Supreme Court of Canada of the *Snook* definition of sham for Canada tax law purposes:

> [121] There appears to be no dispute between the parties as to the meaning of sham. They both referred to the case of J. *Snook v. London & West Riding Investments, Ltd*.[57] In *Snook*, Diplock L.J. stated that "sham":
>
> . . . means acts done or documents executed by the parties to the "sham" which are intended by them to give to third parties or to the court the appearance of creating between the parties legal rights and obligations different from the actual legal rights and obligations (if any) which the parties intend to create. One thing I think, however, is clear in legal principle, morality and the authorities . . . that for acts or documents to be a "sham", with whatever legal consequences follow from this, all the parties thereto must have a common intention that the acts or documents are not to create the legal rights and obligations which they give the appearance of creating. No unexpressed intentions of a "shammer" affect the rights of a party whom he deceived. . . [58]
>
> [122] Canadian courts adopted the *Snook* definition of sham in 1972. [59] The Supreme Court of Canada reaffirmed and followed this definition of sham in *Stubart Investments Ltd. V. The Queen*. [60] In *Stubart*, Justice Estey defined sham as:
>
> > . . . a transaction conducted with an element of deceit so as to create an illusion calculated to lead the tax collector away from the taxpayer or the true nature of the transaction; or, simple deception whereby the taxpayer creates a facade of reality quite different from the disguised reality. . . [61]
>
> [123] Two more recent decisions of Justice Noël of the Federal Court of Appeal discuss sham. In *Antle v. The Queen*, he said, in obiter:
>
> > . . . The required intent or state of mind is not equivalent to *mens rea* and need not go so far as to give rise to what is known at common law as the tort of deceit . . . . It suffices that parties to a Transaction present it as being different from what they know it to be . . . [62]
>
> [124] In *2529-1915 Québec Inc. v. The Queen*, he said:
>
> > [59] It follows from the above definitions that the existence of a sham under Canadian law requires an element of deceit which generally manifests itself by a misrepresentation by the parties of the actual transaction taking place between them. When confronted

> with this situation, courts will consider the real transaction and disregard the one that was represented as being the real one.[63]

[125] In a tax context, a Court will arrive at a finding of sham when the evidence shows that the parties misrepresented their arrangements in a bid to achieve a tax benefit that would be denied if the nature of their arrangements was properly disclosed. In tax matters, the party that is deceived by the sham is the Canada Revenue Agency ("CRA").

[126] In considering sham, the Court must examine the objective reality surrounding the arrangements to discern whether the transaction documents truly reflect the parties' intent. Direct evidence of sham is rare where a case proceeds to court; in the absence of an admission, the court is left to weigh circumstantial evidence.

[127] […]The factors that inform the objective reality of the arrangements include:

> i) the circumstances surrounding the development of the transaction structure;
>
> ii) the Appellants' due diligence, involvement and oversight, or lack thereof, in evaluating and participating in the transactions;
>
> iii) the ordinary business and investment practices of the Appellants;
>
> iv) the parties' stated goals and reasons for entering into the transactions; and
>
> v) the legal rights and obligations as defined in the transaction documents.

[128] This list is non-exhaustive. Taken together, these factors inform a court's analysis of whether the legal rights and obligations described in the transaction documents are consistent with the parties' avowed intent.

[129] I stress that searching for the objective reality of a transaction does not conflate sham (i.e.,misrepresentation and deceit) and the notions of "economic substance" or "business purpose". It is well established that a transaction is not a sham because it is devoid of economic substance, lacks a business purpose or serves a tax avoidance purpose. I shall look instead at whether the parties misrepresented the nature of their arrangements to the CRA.

[130] One final point is that sham must be distinguished from abuse. Sham is not an overall scheme that is abusive; it is a matter of the parties having

> misrepresented the legal effect of a transaction. Accordingly, I must point to certain transactions that are misrepresented. The structure in these appeals is complex and comprises many different transactions, and it is important not to combine all the transactions and steps into one, to paint every step as a sham – that would be to misconstrue what sham is. […]

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[57] [1967] 1 All ER 518 [*Snook*]
[58] *Snook*, at page 528
[59] *M.N.R. v. Cameron*, [1974] S.C.R. 1062
[60] [1984] 1 S.C.R. 536 [*Stubart*]
[61] *Stubart*, at pages 545 and 546
[62] 2010 FCA 280 at para 20
[63] 2008 FCA 398 at para 59

[20] Sham is a serious allegation requiring convincing evidence to conclude that a Canadian taxpayer was deceitful on a balance of probabilities. Often this may involve circumstantial evidence. This can be expected to require more then the Respondent's suspicions.

(2) Recharacterisation Pursuant to Paragraphs 247(2)(*b*) and (*d*)

[21] The relevant provisions are set out in Appendix 1. So-called recharacterisation transfer pricing adjustments under these provisions require the Court to consider:

> (i) whether the parties' transactions would not have been entered into between notional arm's length parties;
>
> (ii) whether the transactions can reasonably be considered to have been entered into primarily for *bona fide* purposes other than to obtain a tax benefit; and
>
> (iii) what transactions would have been entered into between notional arm's length parties and on what terms and conditions.

If paragraphs (*b*) and (*d*) apply, the quantum and nature of income amounts are redetermined on the basis of substituted notional arm's length transactions and not the transactions entered into by the parties.

These provisions were most recently considered by the Federal Court of Appeal in *Cameco* wherein Justice Webb wrote:

> *C. Conclusion with Respect to Paragraphs 247(2)(b) and (d) of the Act*
>
> 81 Parliament has chosen to indirectly address the issue of a Canadian taxpayer shifting profits to a non-arm's length person located in another jurisdiction by implementing the transfer pricing rules found in Part XVI.1 of the *Act*. These rules will adjust prices paid for goods purchased and sold and for services provided in transactions between a taxpayer and a non-resident person with whom that taxpayer is not dealing at arm's length, if such prices differ from the amount that would be paid in an arm's length transaction. By adjusting prices for goods and services, the profit realized by the Canadian taxpayer will be adjusted. However, the rules in paragraph 247(2)(*b*) and (*d*) of the Act are not as broad as the Crown suggests. They do not allow the Minister to simply reallocate all of the profit of a foreign subsidiary to its Canadian parent company on the basis that the Canadian corporation would not have entered any transactions with its foreign subsidiary if they had been dealing with each other at arm's length.
>
> 82 Paragraphs 247(2)(*b*) and (*d*) of the *Act* apply only where a taxpayer and non-arm's length non-resident have entered into a transaction or a series of transactions that would not have been entered into between any two (or more) persons dealing at arm's length, under any terms or conditions. In such a situation, the transaction or series of transactions that would have been entered into between arm's length persons is substituted for the transaction or series of transactions in question, with the appropriate terms and conditions. In particular, paragraphs 247(2)(*b*) and (*d*) of the *Act* cannot be used to simply reallocate all of the profits earned by CEL to *Cameco*, its Canadian parent corporation, in the circumstances of this case. Of course, in another situation where these paragraphs would apply, the substituted transactions may well result in adjustments to the income (and the profit) of a Canadian taxpayer.

(3) Transfer Pricing Adjustments Under Paragraphs 247(2)(*a*) and (*c*)

[22] The relevant provisions are set out in Appendix 2. Transfer pricing adjustments under these provisions require the Court to consider:

(i) whether the terms or conditions of the parties' transactions would have been agreed to by arm's length parties; and

(ii) if not, what terms and conditions would arm's length parties have agreed to.

[23] The terms and conditions subject to review under paragraphs (*a*) and (*c*) are not limited to those setting out a price or cost or other amount. If paragraphs (*a*) and (*c*) apply, the quantum or nature of income amounts are redetermined on the basis of the parties' transactions reflecting substituted notional arms' length terms and conditions.

[24] The difference between paragraph (*a*) and (*c*) transfer pricing adjustments and paragraph (*b*) and (*d*) transfer pricing adjustments is that income amounts are redetermined as to quantum and/or nature under paragraph (*c*) by reference to revised terms and/or conditions of the parties' transactions, whereas under paragraph (*d*) it is by reference to substituted notional transactions. That distinction is clear from the text of the provisions. The nature and/or the quantum of income amounts can be redetermined under either sets of provisions.

[25] These provisions were also most recently considered by the Federal Court of Appeal in *Cameco* which made it clear that these provisions require that adjustments be made having regard to either the terms and conditions of the parties' transactions or notional arms' length transactions, and that they do not permit simply reallocating profits to a taxpayer because that taxpayer would not have engaged its affiliate had that affiliate been arms' length.

(4) Penalties

[26] AgraCity has been assessed a subsection 247(3) transfer pricing penalty in respect of the ClearOut sales profit amount added to its income.

[27] If the Respondent is successful in its primary position of sham, the Court would still be required to carry on and decide the Respondent's alternative positions in order to determine if the subsection 247(3) transfer pricing penalty was properly assessed.

[28] AgraCity was also assessed a penalty under subsection 163(2) for knowingly understating its income. If the Appellant is not completely successful with respect to the Respondent's alternative positions, the Appellant's position requires the Court to consider whether penalties can be assessed under both subsection 247(3) and subsection 163(2) in respect of the same income adjustments.

Witnesses

[29] The Court heard from the following material/fact witnesses :

1. James Mann:

James Mann is the founder of Farmers of North America Inc. which was a predecessor to Farmers and Families of North America Inc. (“FNA”) and its FNA Group. He held a Chief Executive Officer role in the FNA Group companies. He has a Bachelor of Agriculture from the University of Saskatchewan.

2. Jason Mann:

Jason Mann is James Mann’s younger brother. He completed post-secondary studies in Agriculture and in Chemical Technology. He grew up on a working farm, became a farmer, became involved in custom seeding and harvesting in Canada and the US before moving on to construction and real estate development in British Columbia. He returned to work with his older brother James at FNA Group in the years in question. He was the President of AgraCity throughout the period. He became director and sole owner of AgraCity when James Mann transferred the shares to him in December 2006.

3. Jeff Bergen

Mr. Bergen is a certified professional accountant CPA. He holds a Bachelor of Commerce from the University of Saskatchewan. He worked at Ernst & Young Regina, KMPG Saskatoon and the University of Saskatoon’s College of Medicine and its Central Accounting Department. During the period in question he was the Controller of the FNA Group of companies responsible for general ledgers, accounting systems, preparation of financial statements and tax compliance for all corporations controlled by James or Jason Mann.

4. Spencer Vance:

Mr. Vance was the President of Albaugh North America (“Albaugh”) for about 20 years including the years in question.

He was responsible for all functions, commercial and otherwise, across the United States and Canada. Albaugh had worldwide revenues of about US $1,000,000,000 in the period in question and North America generated close to half of that. He holds a Bachelor of Science in Animal Science and Agriculture from the University of Nebraska. Albaugh was the principal supplier/source for ClearOut sold by NewAgco Barbados in the years in question.

5. Lyle Forden:

Mr. Forden is a farmer and business owner. He holds a degree in Agricultural Science and Crop Farming from the University of Saskatchewan. He owns and operates a family farm engaged in mixed farming of Simmental cattle and crops. He also worked at FNA as a Member Service Representative ("MSR") and as National Member Service Manager in the years in question.

6. Scott Kilbride:

Mr. Kilbride is a fourth generation family farmer with a Crop Science degree from the University of Guelph. In the years in question he operated his family farm through Kildare Acres in Wallaceburg, Ontario. He was a FNA member and a purchaser of ClearOut from NewAgco Barbados.

7. Ashley Skinner:

Mr. Skinner did contract work at FNA and AgraCity before and during the period in question, doing general consulting work on member and membership issues including the FNA newsletter. He was not involved in business decision-making or in the management of any FNA Group companies.[8]

8. Angela Spence:

[8] Transcript January 31, 2019, page 1155 lines 1-19.

Ms. Spence is currently an engineering technologist with the City of Courtenay, British Columbia. She worked for the FNA Group in the years in question as a MSR and did related work for AgraCity.

9. Dr. Karen Dodds:

In the years in question Dr. Dodds was the Executive Director of the Pest Management Regulatory Agency ("PMRA") at Health Canada responsible for the regulation of pesticides throughout the country. She holds a B.Sc., an M.Sc. and a Ph.D. in Biology, Chemistry and Micro-Biology from the University of Waterloo and the University of Guelph. Following her time at Health Canada, she went on to be the Assistant Deputy Minister of the Science and Technology Branch at Environment Canada.

10. Karen McCullagh:

Ms. McCullagh was the Director General of Compliance and Laboratory Services at the PMRA in the years in question, responsible for compliance across headquarters, regions and labs, chemistry evaluations, and enforcement.

11. Bob Friesen:

Mr. Friesen was the President of the Canadian Federation of Agriculture ("CFA") in the years in question; he had previously been its vice-president. CFA is a federation of provincial agricultural organisations and commodity organisations which operates as a Canadian agricultural umbrella quasi-lobbying group that works with the Canadian government. He was a member of the PMRA's Own Use Import OUI Task Force in the years in question. He handles government relations for the FNA.

[30] All of the material/fact witnesses were intelligent, educated and clear spoken. They gave credible evidence. They gave overall reliable evidence, usually making it clear where their understanding, perception or knowledge of particular aspects or details was limited given their role in the organizations or the transactions. While there was a history of contentious litigation and allegations

between the Mann brothers' business and Ashley Skinner involving appropriation of business opportunities relating to FNA promoted products including ClearOut, it is not relevant to what I have to decide.

[31] In addition the Court heard from the following expert witnesses:

1. Sir Trevor Carmichael:

Sir Carmichael is an Attorney-at-Law in Barbados and is an expert in Barbados corporate law.

2. Brad Rolph:

Mr. Rolph is a partner at Grant Thornton where he is an economist specialising in transfer pricing.

3. Dr. Muris Dujsic:

Dr. Dujsic is a transfer pricing economist specialist who testified as an expert economist in transfer pricing. He is a partner and Chief Economist at Deloitte. He holds a Bachelor in Economics, a Masters in Finance and Accounting and a Doctorate in Economic Sciences from the University of Novi Sad in Serbia.

4. Oliver Rogerson:

Mr. Rogerson was called by the Respondent as an expert in the economic analysis of transfer pricing. Mr. Rogerson holds a Masters degree in Economics from Wilfrid Laurier University and a Bachelors level degree in economics from Royal Military College. Mr. Rogerson has 18 years of experience as a transfer pricing economist at CRA where for 13 years he was the Chief Economist in the International Tax Division and for five years was an Economist in that division. He was a member of the CRA's Transfer Pricing Review Committee.[9] While he was at the CRA, Mr. Rogerson was the Canadian delegate to the OECD

[9] The transactions in question went to the Transfer Pricing Review Committee however Mr. Rogerson did not participate in meetings or any other aspect.

> Working Party Six responsible for updating and maintaining the transfer pricing guidelines which are the extended commentary to Article 9 of the OECD model tax treaty dealing with transfer pricing. Since 2016 he has been at the Department of Finance as the Director of the International Tax Division in its Business Income Tax Directorate ("BIT"). In 2017 he became the Director of the Resource and Environmental Taxation Group in BIT. At Finance, he continued to be a delegate to the OECD Working Party Six. He was qualified as an expert in the field of economic analysis of transfer pricing in *Marzen Artistic Aluminium Ltd. v. The Queen*, 2014 TCC 194 in our Court in 2014 (Affirmed: 2016 FCA 34). In *Marzen* his Expert Report was ruled inadmissible but Justice Sheridan went on to rely on his Rebuttal Report.

FNA Group of Companies

[32] FNA is described by its founder James Mann as a business alliance of farmers from across Canada and parts of the United States designed to change how markets function in order to increase farmer profitability. In his words, it was to counter the observation that farmers are the only business people who buy retail and sell wholesale. FNA's strategy is to achieve its objectives on behalf of its membership by:

i) creating competition and enhancing negotiation,

ii) creating efficiencies in the marketplace in favour of farmers,

iii) moving up and down the value chain to capture those margins, and

iv) reducing technological risk, for example through the development and implementation of information systems.

[33] FNA is a member and membership services-based organization. Virtually all of its revenues come from selling memberships to its members. Where the FNA Group provides products, commodities or services to members, those are promoted by FNA but are provided through separate FNA Group companies. There are a significant number of different FNA Group companies as they work in different markets with different suppliers and with different co-investors unique to the product, service, or business being developed.

Regulation of Glyphosate-Based Herbicides:

[34] In Canada glyphosate-based herbicides, such as ClearOut, are subject to the federal *Pest Management Control Act* ("PMCA") which is administered by the PMRA.

[35] The sale, distribution and use of regulated products such as glyphosate-based herbicides, including ClearOut, in Canada requires that the particular product itself be registered. Registration in Canada is a lengthy, detailed and complicated process, as one would expect, requiring chemical evaluations of the glyphosate sourced by the applicant as well as the overall product formula for which it is an active ingredient. The process of registering a regulated product in Canada can be somewhat shortened if the product has already been registered in the United States by the Food and Drug Administration ("FDA").

[36] In the period in question, ClearOut was not available or offered for sale in Canada as a Canadian registered product. The initial US manufacturer of the ClearOut had applied for and obtained registration in Canada in 2006, but this was not known to the FNA Group or the Mann brothers at that time. The PMRA did register ClearOut in May 2006 but it was not made available in Canada in accordance with the registration and under the conditions of registration until sometime in 2008 after Albaugh had become the owner, manufacturer and supplier of the product. This resulted in Canadian farmers thereafter being able to buy ClearOut directly from Canadian suppliers which promptly ended FNA's role as sponsor of ClearOut under the Canadian OUI program, and NewAgco Barbado's business of selling ClearOut to FNA members under the OUI program.

[37] In the years in question, it was the US FDA registration of ClearOut that permitted FNA to apply as sponsor to the PMRA for ClearOut's acceptance under the OUI program to be eligible for Canadian farmers to be able to purchase it in the US, from any source whether or not affiliated with FNA Group in any manner, and to import it into Canada for themselves for their own use.

[38] The PMCA also regulates who may use the registered product, as well as the location, timing and purpose of any use.

The OUI Program

[39] The OUI program was established to allow Canadian users to import designated pesticides themselves for their own use. It was aimed at ensuring Canadian agricultural producers would have access to competitively priced pesticides by giving them potential access to lower priced foreign pesticides that are chemically equivalent to Canadian pesticides, thereby giving them access to a larger range of regulated products than the Canadian market provides at any time in the agricultural sector. Only products that could be shown to be equivalent to products already registered in Canada could be approved. The OUI program has since been replaced with the Grower Request Own Use program ("GROU").

[40] The OUI program was a two-step process. In the first step, individuals, or a user/commodity group or sponsor for such persons, applied to have a foreign product accepted in the OUI program. At this stage the applicant had to provide detailed technical chemical analyses of both the foreign and Canadian registered products sufficient to establish their chemical equivalency, both as to the active ingredient and the formula. The applicant was required to submit a copy of a "label" for the foreign registered product and the draft "label" for the equivalent Canadian registered product. The word "label" is a misnomer. These are extensive booklets or brochures approved by the FDA or PMRA that are capable of being affixed to each product container in adhesive sleeves. The Canadian labels had to comply with Canadian labelling requirements under all applicable federal legislation.

[41] In the second step each farmer was required to obtain approval for each import from the PMRA. Actual users or groups of users applied for individual import permits to bring a specified volume of the product into Canada for a specified use at a specified time on specified property. Such a permit allowed them to bring it into Canada through customs. Individual users were required to obtain an import permit for each importation and the product to be imported had to be separately packaged, identified and labelled as belonging to the particular user and fully comply with the specific detailed terms of the permit.

[42] The PMRA inspectors audited OUI importers to verify invoices, permits, storage and use, including time of use, to ensure strict compliance with the import permits. The PMRA officials also reviewed FNA's publications to ensure FNA as a Canadian corporation was only viewed by PMRA as promoting the availability of ClearOut for import under the OUI program, and not promoting the sale of ClearOut.

[43] While it appears that the OUI program may have initially anticipated individual farmers each using their own vehicles to personally purchase and collect their product in the US and to drive it through customs and into Canada themselves, the PMRA in the case of ClearOut permitted the use of independent trucking companies using third party customs brokers to collect all of the individual purchases by FNA members each season, by picking up and importing on behalf of each farmer their individually segregated and labelled containers of ClearOut and delivering those to them at their farm, all as arranged by FNA as the purchaser's agent, with the US suppliers, the trucking companies and customs brokers etc.

[44] Prior to ClearOut being accepted into the OUI program by the PMRA in February/March of 2005, there had only been a few products accepted at the first step of the process. None of these products ever got to the second stage of actual importation. This is because Canadian markets promptly recognized the price discipline mechanics imposed by acceptance into the OUI program. That is, Canadian prices of the Canadian registered equivalent products dropped to more closely align with the price of the US registered equivalent product in the US market which could then begin entering Canada under the OUI program. That was not to be the case for ClearOut. The PMRA received thousands of import permit applications (in quintuplicate) from Canadian farmers, virtually all being FNA members using FNA as their agent. Over 4,500 applications were received in 2005 and 2006. In 2005, over 3,000 permits were issued for almost six million litres of ClearOut. The PMRA Executive Director described receiving boxes of chemical equivalency application materials and of import applications by the semi trailer truck load full at both stages of the process. In 2005, the FNA Group grew from a one million dollar enterprise to a twenty seven million dollar enterprise. The US ClearOut FNA made available to its members allowed FNA to grow its membership base accordingly.

The Transactions in Question

2005:

[45] Following the acceptance of ClearOut into the OUI program, FNA Group put in place a business operations structure by which FNA would be able to promote the availability of ClearOut under the OUI program to its members and to facilitate their purchases and importations.

[46] Following their extensive consultations and numerous meetings with the PMRA, the Manns and FNA understood that ClearOut and the OUI program could be promoted by FNA to its members but, that it remained forbidden for anyone to offer ClearOut for sale in Canada or to sell it in Canada. Further, they understood from their PMRA consultations, materials and meetings that this meant that their members would have to purchase the ClearOut from a non-Canadian supplier outside Canada. The regulator described the difference between offering for sale and promoting availability as a fine line to draw or walk. I find on the evidence that this was a perfectly reasonable understanding of PMRA's position, and in any event would have been the prudent business decision to make to avoid any adverse interpretation of the provisions of the PMCA by the PMRA or any challenge by Canadian glysophate-based herbicide suppliers who would be significantly affected by dropping prices or sales as a result of ClearOut being available under the OUI program.[10]

[47] To this end, in 2005 James Mann caused a new US corporation, NewAgco Inc. ("NewAgco US"), to be established in the state of Delaware to be used to purchase ClearOut in the US markets, to warehouse it in its rented warehouse facilities in North Dakota, and to sell it to FNA members.

[48] In that year NewAgco US sourced its ClearOut in the US from a large number of suppliers with ClearOut available at a fraction of the price that glysophate-based herbicides were selling for in Canada. Their suppliers included Chemical Products Technology ("CPT") who was then the manufacturer of ClearOut (and who later sold its rights to ClearOut to Albaugh), as well as a number of other agricultural supply distributors across the US who had available ClearOut product. NewAgco US' demand for ClearOut from FNA members in Canada was very significant and greatly reduced the available supply in the US such that NewAgco US worked very hard and went to considerable lengths to locate and acquire all the ClearOut they could from available sources.

[49] NewAgco US sold ClearOut to individual FNA members FOB their individual farms in Canada. NewAgco US typically purchased ClearOut from its US suppliers in large quantities, paid for them upon purchase, and arranged for it to be delivered by transport truck to their US warehouse facilities. From there individual containers (being either totes of 1,000 litres or drums of 200 litres)

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[10] See, for example, McCullagh Transcript January 30, 2019 page 1104 lines 18 to 20, and page 1113 line 20 to page 1120, line 3.

would be specifically identified as having been purchased by specific Canadian purchasers and each purchaser's Canadian labels would be affixed, along with the purchaser's individual OUI permit and necessary customs forms, all in multiple copies and while maintaining the integrity of the US FDA labeling. This would include the purchaser's Import/Export Account Number from CRA which was typically newly obtained by FNA as agent for a farmer upon their first purchase unless they had previously imported goods into Canada commercially. NewAgco US would arrange and pay for third party truck transport to the Canadian buyers. After a short period of time, NewAgco US engaged third party customs brokers to clear customs on behalf of each individual purchaser and that purchaser's ClearOut containers. These were dedicated transport trucks filled only with ClearOut that Canadian farmers had purchased from NewAgco US. The number of truck loads measured in the hundreds.

[50] NewAgco US used AgraCity to attend to the logistical and related activities of its sales and deliveries to its Canadian buyers. This was set out in a written Services Agreement between these two corporations. Under its terms, AgraCity was paid an amount per litre of ClearOut sold to perform these services. That amount was revised and adjusted upwards twice between 2005 and 2007 to ensure it was and remained profitable for AgraCity in practice.

[51] AgraCity and its staff would coordinate with FNA MSRs and other FNA staff once an order for ClearOut was placed with FNA by a member to attend to all of the purchase, import and customs paperwork, labeling and arranging payment and delivery. FNA would promote the availability of ClearOut at a price per litre fixed by NewAgco US and communicated to FNA. FNA was responsible for all of its member service activities up to placing the order and fixing its terms for payment delivery and importation. FNA worked with each member to facilitate and administrate the OUI process as well as to organise and direct delivery to the member's farm. Members would appoint FNA their agents in writing for attending to customs and duties upon importation. AgraCity was thereafter responsible, as a sub-contractor of NewAgco US, for all of the logistics required to complete the sale, import and delivery to the purchaser.

[52] FNA and AgraCity shared office space in Saskatoon with most space designated for one or the other. They each had their own staff and payroll for their separate and distinct businesses. It was on occasion the practice for one to borrow available staff from the other as needed and to make intercompany charges at year end based on shared staff time and costs estimates. The sudden surge of activity

from the successful high demand ClearOut service offered by FNA to its members required such staff lending between AgraCity and FNA, and it was not uncommon for FNA MSRs after taking and placing the order to help attend to AgraCity's logistics services, including such things as preparing and completing customs importation paperwork and preparing, signing and affixing each individual copy of each label for each purchaser. These were tracked and accounted for.

[53] FNA consulted extensively with PMRA to ensure it was in compliance with the OUI program and permit requirements. Its initial member communication announcing ClearOut availability through the OUI program was reviewed by PMRA staff before it went out. One of the PMRA's key concerns was that FNA only be promoting ClearOut's availability under the OUI program and offering its services to members in connection with that, and that FNA not be offering ClearOut for sale in Canada.

[54] In 2005 FNA recorded and reported in Canada its membership fee revenues and AgraCity recorded and reported in Canada its revenues under the Services Agreement with NewAgco US. They each accounted for the shared employee payments. There is no evidence that could lead me to conclude that NewAgco US did not record and report its ClearOut sales profits in the US. CRA did not reassess anyone in respect of the 2005 ClearOut sales and related transactions. It can be noted that the US is perceived as a high corporate tax jurisdiction and that it has a full tax treaty with Canada.

[55] In December 2005 CPT sold the ClearOut rights and inventory etc to Albaugh which already had its own glyphosate-based product. This was the first the Mann brothers had heard of Albaugh. Jason Mann promptly set about persuading Spencer Vance at Albaugh to sell ClearOut to NewAgco Barbados. In negotiations between Spencer Vance and Jason Mann in late 2005 NewAgco Barbados got an exclusive supply agreement from Albaugh. The two corporations also signed a confidentiality agreement relating to their arrangements in the first half of 2007.

2006 and 2007

[56] The structure put in place and used in 2005 continued largely unchanged except that:

i) NewAgco Barbados was incorporated in March 2006 to take on the role NewAgco US had until then carried on;

ii) NewAgco US' orders from the FNA members in the Fall of 2005 for Spring 2006, and its ClearOut inventory and rights, were transferred to NewAgco Barbados; and

iii) Albaugh became the virtually sole supplier to NewAgco Barbados of ClearOut under its exclusive supply agreement following Albaugh's acquisition from CPT of the ClearOut rights and inventory.

[57] After the end of the 2005 agricultural season and before the 2006 agricultural season began, the Mann brothers decided to transfer NewAgco US' Canadian ClearOut sales business to a new corporation to be incorporated in Barbados. This was done primarily to minimise the US tax payable on the sales profits. An asset sale was completed in which money, accounts and ClearOut inventory changed hands. The newly incorporated NewAgco Barbados purchased the ClearOut related business assets from NewAgco US and took over its US warehouse space.

[58] Jason Mann was given express though unwritten authority to set the price by NewAgco Barbados from James Mann as director of NewAgco Barbados. This was formally minuted in 2007.

[59] FNA was receiving orders from two to three thousand farmers each year during this period and multiple orders each year per farmer. Orders for member purchases from NewAgco Barbados amounted to five to seven million litres each year.

[60] Jason Mann continued to buy all available ClearOut for NewAgco Barbados, as he had before for NewAgco US. The price of ClearOut to Canadian farmers continued to be determined by Jason Mann for NewAgco Barbados as its cost from Albaugh from time to time plus a reasonable margin for expenses and profit.

[61] NewAgco Barbados was having virtually all of its Albaugh ClearOut purchases transported to the North Dakota warehouse for sale and delivery to Canadian farmers.

[62] The payments from farmers were received in Canadian dollars prior to delivery. AgraCity collected the funds and then periodically transferred them to NewAgco Barbados.

[63] For the first few months NewAgco US paid for the inventory purchased by NewAgco Barbados but that cost was reimbursed and borne by NewAgco Barbados. After the first few months in 2006 NewAgco Barbados paid Albaugh directly.

[64] The ClearOut purchases and sales were properly recorded on the financial statements of NewAgco Barbados.

[65] The freight invoices from the third party trucking companies were also borne by NewAgco Barbados. Some were payable in Canadian dollars and some were payable in US dollars.

[66] The warehousing costs of the North Dakota warehouse were also borne by NewAgco Barbados.

[67] The drum and tote recycling costs for the shipping containers in which the farmers purchases were delivered were also borne by NewAgco Barbados.

[68] In 2006 NewAgco paid management fees of $50,000 a month in respect of the shared employee services to FNA relating to ClearOut activities. After Mr. Bergen became Controller in December 2006, he put in place the cost reimbursement program in respect of shared employee services in its place. He understood that the management fee amount was itself based on estimated costs.

2008

[69] CPT's Canadian registration of ClearOut was not transferred by the PMRA to Albaugh until very late 2007.

[70] In 2008 Albaugh made the registered Canadian ClearOut product available for sale in Canada in accordance with its Canadian registration requirements. A seller in Canada of a Canadian registered product is subject to greater reporting requirements to the PMRA under the PMCA than is required under the OUI program. This was done by Albaugh when Albaugh decided it was the appropriate time for it to enter the Canadian market for ClearOut in this fashion. The OUI

program was no longer attractive, even while US registered ClearOut remained eligible for it, and was not promoted or serviced by FNA.

[71] Albaugh does not sell its products to end users. After December 2007 Albaugh ClearOut was sold to FNA members via AgraCity Crop and Nutrition, an affiliate member in the FNA Group, that sold other products to FNA members. The order-taking arrangements and the transfer arrangements remained virtually identical.

Analysis

Sham

[72] Paragraph 19 of the Amended Reply reads:

> 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 risk, and accordingly the profit from the series in the amounts of $2,413,520 and $3,670,478 are properly included in [AgraCity's] income for its taxation years 2007 and 2008, respectively, pursuant to s.3 and 9 of the *Act*;[11]

[73] In its written argument the Respondent's position is that the Services Agreement is a sham to camouflage the operations of AgraCity as those of NewAgco Barbados, that gave the illusion that NewAgco Barbados was selling ClearOut to Canadian farmers "when the evidence shows that the activities were those of AgraCity." The reasons put forward by the Respondent in support of this are:

- NewAgco Barbados was an empty shell.
- The Services Agreement purports to be a logistics service agreement when in fact AgraCity performed all of the functions relating to the sale.
- The Services Agreement was disregarded by the parties because the services went beyond the enumerated activities and included all aspects of carrying

[11] Paragraph 15c) of the Amended Reply reads identically except it ends by referring to s.247(2)(*b*) and (*d*) in place of s. 3 and 9.

on the ClearOut business which included selling the ClearOut and sourcing the ClearOut, and negotiating with suppliers.

- The Services Agreement specifies it is not an agency agreement but the ClearOut invoices sent to farmers indicated at times AgraCity "acting on behalf of NewAgco Inc." or "as agent on behalf of NewAgco."

- The specified services fee was set out in the Agreement at ten cents per litre but that amount was increased at year ends and only ratified by NewAgco's Board of Directors later in 2008.

- The Services Agreement was entered into to deceive the Minister into believing the profits were earned in a low tax jurisdiction.

- The confused books and records of AgraCity and NewAgco Barbados were intended to deceive tax authorities in the event of an audit. Even the uses of FNA and Farmers of North America was to create the illusion that Farmers of North America Inc. was still in business after its operations were transferred to Farmers and Families of North America.

- Albaugh mailed its invoices to NewAgco Barbados at a United States address.

- Some invoices prepared by Albaugh still referred to NewAgco US.

- Other third parties addressed their invoices to such non-existent entities as "NewAgco Farmers of North America," "Farmers of North America AgraCity Ltd." and "NEW AG CO."

- Invoices addressed to NewAgco Barbados did not have an address in Barbados but either the warehouse address in North Dakota or the address of AgraCity and FNA in Saskatoon.

- The MSRs were not aware of the corporate structure of the FNA Group or its operations.

- The Board of Directors of NewAgco Barbados was put in place to give the appearance that something was happening in Barbados, though it only rubber stamped decisions previously made in Canada.

[74] In addition, the Respondent in its Amended Reply made several assumptions that would support its characterisation of the Services Agreement as a sham. These would include in particular;

> q) NewAgco-Barbados was created for the purposes of sheltering profits of the Farmers of North America corporate group from the Canadian fisc and more specifically to shelter the profits of AgraCity from the Canadian fisc;
>
> …
>
> t) On March 29, 2006, AgraCity entered into a service agreement with NewAgco-Barbados to carry on the activities of selling ClearOut to FFNA members;
>
> …
>
> w) The business of selling ClearOut to FFNA members was transferred to NewAgco-Barbados at no cost;
>
> …
>
> bb) The fair market value of the services rendered by AgraCity to NewAgco-Barbados was [the amounts of net profits from ClearOut sales recorded by NewAgco Barbados].
>
> cc) In respect of the sale of ClearOut to FFNA members:
>
> i) NewAgco-Barbados held no assets and performed no economic activities;
>
> ii) NewAgco-Barbados performed no functions and held no risk;
>
> iii) NewAgco-Barbados provided no value-added functions;
>
> iv) AgraCity undertook all of the functions and assumed all the risks;
>
> dd) NewAgco-Barbados had no employees;
>
> …

> kk) NewAgco-Barbados was not a party to the sale of ClearOut to FFNA members and they were not aware of its existence;
>
> ll) The suppliers of ClearOut made no sales of ClearOut to NewAgco-Barbados. The sales of ClearOut were rather made to AgraCity and other members of the Farmers of North America corporate group;
>
> …
>
> nn) NewAgco-Barbados did not negotiate with suppliers of ClearOut;
>
> oo) The decision making process for NewAgco-Barbados was made in Canada by James Mann and Jason Mann;
>
> pp) The board of directors of NewAgco-Barbados acted by approving decisions already made in Canada by James Mann and Jason Mann;
>
> qq) Since it was first established in 1998, FFNA negotiated with program suppliers on behalf of FFNA members. Jason Mann negotiated the price of ClearOut with suppliers;

[75] In addition to the assumptions, the Respondent stated the following additional facts in the Amended Reply:

> a) The service agreement entered into between [sic] and NewAgco-Barbados did not reflect the true agreement between the parties;
>
> b) AgraCity and NewAgco-Barbados acted in concert to give the false appearance that NewAgco was carrying on the business of selling ClearOut.
>
> c) AgraCity knew that the profits reported by NewAgco-Barbados from selling ClearOut were the profits of AgraCity;

[76] The Amended Reply of the Respondent also states that the series of transactions that amounted to a sham started with the incorporation of NewAgco Barbados, and included the conclusion of the Services Agreement between AgraCity and NewAgco Barbados, the services provided under the Agreement, the acquisition of ClearOut and its sale to FFNA members.

[77] Having heard and considered all of the evidence, from the witnesses and their documents, I must conclude that it falls far short of establishing either:

i) that the parties to the transactions sought to present to anyone that the legal rights and obligations of the parties were different than what they knew or understood them to be, or

ii) that any of those parties sought to deceive anyone about their purpose or intention or reasons for entering into any of the transactions.

[78] That is, the evidence presented does not establish the existence of any sham transactions, nor any deceptive window dressing. The key reasons for this are as follows:

i) The reassessed 2006 and 2007 transactions (involving NewAgco Barbados in its 2007 and 2008 fiscal years) are otherwise identical to the calendar 2005 year transactions which used NewAgco US, a related company that was not in a low tax jurisdiction. The initial structure put in place in 2005 involving NewAgco US corroborates that the basic structure involving a non-Canadian company to source and sell the ClearOut was done for *bona fide* non-tax reasons with no reason to, or intention to, to deceive anyone. Further, the initially chosen structure was clearly not adopted to reduce taxes. It also corroborates that James and Jason Mann and other key FNA Group officers and their advisors generally understood from the PMRA that a Canadian company would not be permitted to be responsible for selling or distributing ClearOut under the OUI program and would not be allowed to be the seller.

ii) The structure adopted in 2005 involved a new non-Canadian corporation with a name, NewAgco Inc., quite distinct from other corporations in the FNA Group. There was no attempt to mislead or deceive others about the adopted structure, the participants involved or its purpose and objectives. The Respondent made much of the fact that the new corporation incorporated in Delaware in early 2005 and the new corporation incorporated in Barbados in early 2006 were both named NewAgco Inc. This can hardly be seen as indicative of a sham perpetrated on the Canadian tax or health authorities, nor of an attempt to window dress the facts for such Canadian authorities. Involving a non-Canadian company would hardly concern the Canadian health authorities at the time given their evidence to this Court. The new name could not even be confused with, an existing

Canadian company in the FNA Group. It is not as though they named their new US company AgraCity Ltd., and then went on to give that same name to their Barbados corporation.

iii) The evidence relating to the PMRA policies and practices, its interpretation of the PMCA, and how the OUI program fit into the statutory and regulatory regime was provided to the Court by the PMRA's then Executive Director and its then Director General of Compliance. Their testimony could not have been more clear. It was consistent with the understanding of James Mann and FNA that a Canadian entity could not be the seller of the US ClearOut to the Canadian farmers under the OUI program. Even if PMRA's view is incorrect and a Canadian could have been the seller, it would have remained an entirely reasonable risk management based strategic decision to have a non-Canadian company be the seller of the US ClearOut from the US given PMRA's stated concerns, evidenced by both this same testimony and by its concerns that the scope of FNA's activities be limited to making members or potential members aware of ClearOut's eligibility under the OUI program and FNA's ability to assist its members make their purchases. This understanding of the Manns and FNA Group is corroborated by the fact they used a US corporation at the start for the first year.

iv) It was clearly NewAgco Barbados that purchased the ClearOut by Albaugh. The President of Albaugh was aware that NewAgco Barbados was the purchaser and was aware that Jason Mann was acting on behalf of NewAgco Barbdos in negotiating the purchases and the exclusive supply agreement. Similarly, NewAgco Barbados and the Mann brothers intended for NewAgo Barbados to be the purchaser. Those in the FNA Group, such as the comptroller, officers and board, knew that NewAgco Barbados was purchasing the ClearOut from Albaugh and selling it to FNA members under the OUI program. In its initial announcement to members[12] they were clearly told that FNA was only the sponsor and that they could remit payments to FNA who would then transfer those funds to the US supplier. Some of the farmers who testified knew they were buying it from NewAgco Barbados and even some of FNA's MSRs had some

[12] Exhibit A-92 – which was provided to PMRA for review prior to release.

knowledge of NewAgco Barbados within the FNA Group. The purchases and sales were recorded in the books of NewAgco Barbados. The money came from and went into the bank accounts of NewAgco Barbados.

v) NewAgco Barbados received orders from Canadian farmers at a price set in Canadian dollars by Jason Mann, duly authorized by NewAgco Barbados to do so on its behalf. These orders were placed through FNA who promoted ClearOut availability under the OUI program to its members. NewAgco Barbados purchased its ClearOut from Albaugh at a US dollar price negotiated from purchase to purchase by Mr. Vance on behalf of Albaugh and by Jason Mann duly authorized to do so by NewAgco Barbados. NewAgco Barbados had the ClearOut shipped to its warehouses in the US that it paid for. NewAgco Barbados arranged for and paid for the ClearOut to be delivered to the Canadian farmers/FNA member/purchasers. The amounts paid by these purchasers were collected by AgraCity and remitted to and recorded by NewAgco Barbados.

vi) NewAgco Barbados bore material risk in these transactions. It had foreign exchange risk as it sold in Canadian dollars but purchased in US dollars, paid for its warehouse rent in US dollars and paid commercial transport in US dollars. During the period it operated in this manner, NewAgco Barbados realized and recorded a foreign exchange gain or loss duly recorded in its financial statements. NewAgco Barbados owned inventory[13] and thus bore some of the market risks of Canadian demand dropping, or of Canadian prices dropping or of US prices increasing, such that the commercial opportunity declined or disappeared. NewAgco Barbados owned, sold and transported internationally a chemical herbicide product applied to food products. This would have had potential product liability risk for which the US would appear to be the relevant jurisdiction in which any such claim would be pursued. However remote, this too is real commercial risk. That the parties to these transactions took steps to minimize their risks is consistent with sound commercial and business practices.

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[13] NewAgco Barbados even bought NewAgco US' inventory on hand when NewAgco Barbados started up in 2006.

vii) NewAgco Barbados had acquired a very valuable asset for itself which was key to the transactions and the business opportunity it was profitably pursuing: the exclusive supply agreement NewAgco Barbados had with Albaugh for US ClearOut product – the only manufacturer of the only glyphosate-based herbicide product approved under OUI program.

viii) Sir Trevor Carmichael gave unrefuted expert evidence that all was done properly by NewAgco Barbados and in accordance with applicable Barbados corporate and commercial law. This included the validity of:

1) the appointment of Jason Mann by its director James Mann to attend NewAgco Barbados board meetings in his place;

2) the 2008 ratification of the sales by NewAgco Barbados of ClearOut in 2006 and 2007.

3) the 2008 ratification of the 2006 and 2007 increases in the service fees by NewAgco Barbados to AgraCity under the Services Agreement.

ix) There was no serious suggestion based upon the evidence that any of the agreements, transactions or activities did not comply with US or Canadian law as appropriate. I am completely unable to seriously consider the Respondent's Hail Mary argument that the sale of ClearOut was somehow a breach of Canada's *Agriculture and Agri-Food Administrative Monetary Penalties Act* and the *Agriculture and Agri-Food Administrative Monetary Penalties Regulations Respecting the PMCA*. These were not referred to in the Amended Reply. The Respondent did not ask any questions of either Dr. Dodds who was the Executive Director of the PMRA established under the PMCA, nor of its own witness Ms. McCullagh, who was a Director General at the PMRA, about how import purchasers under the OUI program complied with this other federal legislation, even though from the name of the related regulations it appears to be respecting the PMCA. Dr. Dodds in particular in her testimony described the challenges of giving effect to the OUI program mandated under the PMCA regulations given the broad language of the PMCA itself. It is wise to

give deference to regulators interpret their own statutes – especially where, as here, their interpretation was not challenged in the pleadings or in the course of their evidence. The failure of the Respondent to do this with respect to this other federal statute and regulations, or to request prior to argument leave to recall either of these witnesses to address this issue, would make it both unfair and inappropriate for me to consider this. It was not raised in the pleadings and the Court was given no evidentiary basis within which to consider this.

x) The fact that third-party suppliers sent invoices to a misdescribed, non-existent or related party, or addressed to an FNA Group Washington D.C. address or to the North Dakota warehouse, is of little concern given that NewAgco Barbados and the FNA Group would have little control of how suppliers maintain or update their internal accounts. Most importantly, there is no evidence to even suggest that any such wrong information was used, or continued to be used, at the Manns' or at the FNA Group's request. The evidence is the suppliers got paid and that payment was borne by the correct and intended party. The evidence is also that the invoices tended to get paid against the emailed, not the mailed accounts. The purchase orders themselves were consistent with NewAgco Barbados being the purchaser.

xi) Similarly, the fact that a legal agreement specifies it is not an agency agreement (in the same provision that also negates a partnership or joint venture) but the parties, persons related to them, or their employees described themselves acting as an agent of, or acting on behalf of, a party does not of itself indicate the agreement was intended to disguise the real facts and deceive third parties. It is perhaps simply reflective of the difference between the use of words in a legal contract and in other forms of communication.

xii) The Services Agreement between AgraCity and NewAgco Barbados appears to be a valid contractual agreement setting out in very large measure what AgraCity was responsible for doing and what it in fact did, as well as how AgraCity was to be paid for performing those services. There is no requirement that such a contract or agreement be in writing. Nor is there a requirement that such an agreement be specifically crafted for accuracy by highly paid retained professionals

even if its involves millions of dollars. That two businessmen in Saskatoon operating their owner-managed businesses would take a precedent from the internet for an inter-company services agreement should hardly surprise anyone – much less concern them very much. This agreement specifies the services to be provided as those that were in fact provided: promotion and the provision of administrative services related to the sale of ClearOut in Canada, being specifically detailed as promotion, invoicing, collection of receivables, payment of supplier invoices, bookkeeping services, logistics, boarder services, reporting and any other services agreed to from time to time.

xiii) The service fee in the Services Agreement was specified as ten cents per litre "and may be reviewed from time to time and adjusted as mutually agreed by the parties." That two related parties would sit down at year end and ensure the service fee generated a reasonable profit above the service provider's costs should not be surprising or of much concern. They did this twice, increasing it first to fifteen cents for the first year and thereafter to twenty cents. These increases were subsequently duly ratified by NewAgco Barbados' Board of Directors. It is easy for non-arm's length related parties to readily agree to prices and fees without open market forces constraining them. That is precisely why the *Act* requires such amounts to be reasonable and to reflect fair market value and, in cross-border circumstances, the very reason for the *Act*'s transfer pricing rules which were relied on by the Respondent in reassessing and as an alternative in this Court, and which are addressed separately below. The non-arm's length setting and adjusting of prices is not, at least in this case, able to be construed as evidence of a sham if the legal definition of sham is properly understood and applied. Nor can it, at least in this case, be construed as window dressing, if the legal definition of window dressing is properly understood and considered.

xiv) Many Canadian businesses have what the Respondent may describe as confused books and records. The *Act* specifies that adequate books and records must be kept but too many appeals to this Court regularly prove that Canadians often fall short. Confusing, incomplete or inadequate records create challenges for CRA at the verification stage, and challenges for taxpayers and judges when the dispute reaches the Court. They are not, on their own, evidence of a sham unless their

> inaccuracies, inconsistencies and/or omissions can be shown to favor a particular, but clearly inaccurate, recording of the party's rights, obligations, revenues etc. In this case they do not.

Transfer Pricing Recharacterisation - Paragraphs 247(2)(*b*) and (*d*)

[79] One of the express requirements for recharacterisation is that non-arm's length parties must be participants in a transaction or series of transactions that would not have been entered into between arm's length persons. That is, the issue of concern to the fisc is not simply the price or other terms agreed to by the parties, it is that the very transactions agreed to and completed by the parties "would not have been entered into between persons dealing with arm's length". The requirement that this prerequisite to recharacterisation be proved was most recently considered by the Federal Court of Appeal in *Cameco*. As set out above Justice Webb correctly rejected the Crown's argument that this could be more broadly interpreted or applied than is written.

[80] Since the reassessments were made as transfer pricing adjustments under paragraph 247(2)(*a*) and (*c*), it is not surprising that there are no factual assumptions in the Amended Reply to support the Respondent's position that arm's length parties would not have entered into these transactions (at least not that are separate from the assumptions made in support of the sham or transfer pricing quantum adjustment positions of the Respondent.) The Amended Reply does raise the additional fact that "NewAgco Barbados did not perform any function in the series of transactions for which an arm's length party would pay."

[81] The Respondent's expert report of Mr. Rogerson does not address this either. His two surrebuttal reports do not clearly do so either in a way that includes any factual data, evidence, assumptions or conclusions. His reports still focus on the absence of any function for NewAgco Barbados in the transactions even though it is the buyer of the ClearOut from Albaugh and the seller of the ClearOut to Canadian farmers. His report is structured entirely as a functional analysis to support his opinion that transfer pricing adjustments under paragraphs 247(2)(*a*) and (*c*) are warranted.

[82] The Respondent's position on paragraph 247(2)(*b*) and (*d*) recharacterisation is effectively that it is obvious that arm's length commercial parties would never agree to let NewAgco Barbados have any of the profits if it served no function in the transactions given that it had no assets, employees, resources, or other role or

value to contribute to the profit making enterprise or to bring thereto. Respondent's counsel acknowledged that its position on recharacterisation was dependent upon the same interpretation or understanding of the facts and evidence, and somewhat similar argument, as their primary position on sham.[14]

[83] This absence of evidence provided to the Court to support the Respondent's position that arm's length parties would not enter into the transactions is alone sufficient to dismiss this first alternate argument given the findings above that NewAgco Barbados had assets and resources involved in the transactions and took on real risks in respect of the transactions.

[84] However Mr. Rogerson, after identifying that the Services Agreement between NewAgco Barbados and AgraCity was the transaction under review in his report, agreed in his testimony that the Services Agreement, subject to proper pricing, was a contract to which arm's length parties would agree[15]

[85] He continued by explaining that proper arm's length pricing would only see NewAgco Barbados reimbursed for its out-of-pocket arm's length expenses of costs of product, warehouse and transport fees, accounting and legal fees, incorporation fees, costs of meetings of its board of directors etc., with no profit component whatsoever – effectively allocating all of the net profits from the ClearOut sales to AgraCity. The reason he gave in testimony was as set out in his report – NewAgco Barbados performed no function of any value, describing it as "the holder of the buy-sell contract", that NewAgco Barbados "is an entity that adds value by its existence only".[16] This expert opinion testimony of Mr. Rogerson is a further reason for dismissing the Respondent's first alternate transfer pricing argument, especially given the findings on the involvement of NewAgco Barbados and its assets, resources and exposure in the ClearOut sales transactions and in creating the ClearOut sales profits in question.

[86] There was nothing in any of the Appellant's expert reports or testimony that could provide material support for the Respondent's position that the transactions in question were not transactions that arm's length parties would have entered into.

Transfer Pricing Adjustment Amounts - Paragraphs 247(2)(*a*) and (*c*)

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14 See for example transcript of September 20, 2019 at page 54, lines 3 to 13.

15 Transcript of July 17, 2019 at pages 233-234.

16 Paragraph 16 of Rogerson's Dujsic Surrebutal Report.

a) The Rogerson Economic Transfer Pricing Report

[87] Mr. Rogerson's economic transfer pricing report sets out his expert opinion that the value created by the parties to the transactions did not align with what was credited to AgraCity and NewAgco Barbados. This opinion was based upon the facts he was asked to assume by the Respondent. His expert opinion was that 100% of the net sales profits realized from the ClearOut sales by NewAgco Barbados to FNA members should have been AgraCity's and none of those profits would have been NewAgco's had they been dealing at arm's length.

[88] Mr. Rogerson was provided with the following assumptions, among others, from the Respondent for purposes of arriving at his opinion:

1) Jason Mann negotiated the price of ClearOut with suppliers. (Rogerson Economic Transfer Pricing Report ("Main Report") at paragraph 43). Mr. Rogerson expressly relies on this in his functional analysis at paragraph 54(2).

2) FNA staff were establishing pricing for ClearOut (Main Report at paragraph 44(c)). Mr. Rogerson expressly relies on this in his financial analysis at paragraph 44(1).

3) NewAgco Barbados purchased ClearOut from Albaugh and also from other foreign suppliers (Main Report at paragraph 49).

4) NewAgco Barbados sold ClearOut to FNA members throughout the period in question (Main Report at paragraph 29).

5) NewAgco Barbados was the entity:

    a) contractually selling ClearOut to Canadian farmers (Main Report at paragraph 58(a))

    b) contractually acquiring ClearOut (Main Report at paragraph 58(b))

    c) making the payments for ClearOut and for the transportation of ClearOut (Main Report at paragraph 58(c))

6) The decision-making process for NewAgco Barbados was made in Canada by James Mann and Jason Mann (Main Report at paragraph 59).

7) Jason Mann had sole signing authority in respect of NewAgco Barbados's bank account and was approving all payments to be made by NewAgco Barbados (Main Report at paragraph 54).

8) In 2006 AgraCity entered into the Services Agreement with NewAgco Barbados to carry on the activities of selling ClearOut to FNA members (assumption 27 at paragraph 10 of Main Report) Mr. Rogerson expressly relied on this when he wrote in his functional analysis in his Main Report at paragraph 53: "NewAgco Barbados entered into a Services Agreement with AgraCity under which AgraCity would carry out the activities of selling ClearOut to FNA members"

9) Mr. Rogerson went on to state as part of his understanding of the commercial and financial relations and his functional analysis:

   - "However, NewAgco Barbados had no employees, and therefore no ability to perform any functions" (Main Report at paragraph 74)

   - "NewAgco Barbados on the other hand did not bring a potential market (the farmers), a potential product (ClearOut), or suppliers that were not already known, and did not relieve AgraCity from performing any functions by performing them in its place. … therefore, there was no opportunity for NewAgco Barbados to add value in the transaction or extract value from AgraCity." (Main Report at paragraph 77)

   - "NewAgco Barbados performed no functions, and was therefore not able to either generate or retain any value for itself in the context of a arm's length pricing analysis" (Main Report at paragraph 78)

   - "The functional analysis describes what each party to the transaction actually does. The functions performed, taking account of assets used and risks assumed in the performance of those functions, provides important information…" (Main Report at paragraph 88)

   - "While NewAgco Barbados is contractually involved in the transactions, the functions required to carry out the ClearOut

transactions are all performed by other parties, related and unrelated. The transactions to be priced comprised the interactions between NewAgco Barbados and AgraCity and between these two entities, the least complex entity is NewAgco Barbados as it performs no functions, uses no assets and takes no risk." (Main Report at paragraph 96)

- "While NewAgco Barbados is contractually involved in the transactions, the functions required to carry out the ClearOut transactions are all performed by other entities, both related and unrelated" (Main Report at paragraph 96)

- "In this case, NewAgco Barbados was contractually buying and selling ClearOut between arm's length parties. However, all of the functions required to actually buy and sell the ClearOut were performed outside of NewAgco Barbados – by AgraCity and FFNA, and by NewAgco-US. Since NewAgco Barbados performed no functions we must look at two components of pricing of functions they are contractually responsible for: 1) First, the value added by the parties actually performing the functions; and 2) Second, whether NewAgco Barbados has any ability to add or retain value from having the functions flow through it" (Main Report at paragraph 99)

- "In this situation, NewAgco Barbados does not negotiate prices to either buy or sell ClearOut" (Main Report at paragraph 108)

- "The second issue is the arm's length ability of NewAgco Barbados to generate or extract value from participants to the transactions… NewAgco Barbados performs no functions and is not able to either generate or retain any value for itself in the context of an arm's length transfer pricing analysis. This would drive the transfer pricing to zero with the exception that some arm's length parties are paid through NewAgco Barbados" (Main Report at paragraph 109)

[89] In his testimony before the Court, Mr. Rogerson opined that an OECD functional analysis does not involve a narrow definition of a function and that it would include the use of assets and the assumption of risks.[17]

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[17] Transcript July 17, 2019 pages 222 to 226.

[90] Mr. Rogerson testified that in forming his opinion he did understand that ClearOut had to be sold to Canadians by a non-Canadian.[18]

[91] Mr. Rogerson could not explain to the Court his description in his report of NewAgco Barbados as "the holder of the buy-sell contract". He answered that NewAgco Barbados was "the entity that actually has the contract. So their name is on it." He would not answer whether he views NewAgco Barbados to be something less than the buyer of the US ClearOut and the seller of the ClearOut who owns the product in between.[19]

[92] Mr. Rogerson confirmed that the transactions under review for purposes of considering adjustments to the quantum of the amounts charged are those provided for in the Services Agreement.[20]

[93] Mr. Rogerson testified that he would not allocate any value in an OECD transfer pricing functional analysis to any actual foreign exchange, product liability or other risk actually borne by NewAcgo Barbados as buyer, owner, then seller of the ClearOut in the transactions in question even if arm's length parties in the same circumstances would expect to pay and receive a fee for assuming these risks for the other. His reason was that he did not think a functional analysis allowed him to allocate anything to a person he did not believe performed a function. He acknowledged that he understood why the Court should have trouble thinking a notional arm's length party to these transactions would actually agree to be paid nothing when legally assuming real risks. His explanation was that "if there's risks that's disassociated from anything that is being done, then that's very difficult to price. That's the problem there." Of the difference between his functional analysis limited binary choices of 100% and zero versus what notional real world arm's length parties would expect, he said to the Court that "it's your problem to deal with, and I am sorry I can't help you with it more."[21]

[94] Mr. Rogerson testified that in his functional analysis he tested NewAgco Barbados and not AgraCity – i.e. he looked at the value of the functions performed

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18 Transcript July 17, 2019 page 229. This is not in his assumptions, but he was presumably told this by the Respondent who now takes the position that this is not the case.

19 Transcript July 17, 2019 pages 230 to 234.

20 Transcript July 17, 2019 pages 232 to 234. I agree with this approach and find that the Services Agreement is the transaction under review. It is the Services Agreement that is the cross-border agreement between a Canadian resident and a non-resident.

21 Transcript July 17, 2019 pages 245 to 257.

by, and the contributions of, NewAgco Barbados. His reason was that it was because "AgraCity performs much more in the way of functions" than NewAgCo Barbados "and then finding comparables for everything that [AgraCity] does would be much more difficult than it was to find comparables for what NewAgco Barbados does." He went on to say that had he instead tested AgraCity's functions for comparables, he would still expect that AgraCity would be allocated "substantially all of the profits from the transaction"[22] (emphasis added).

[95] In his examination in chief, Mr. Rogerson testified about his Main Report:

- He looked at the transactions between AgraCity and NewAgco Barbados and the function performed by each.

- He understood the functions were all performed in AgraCity not in NewAgco Barbados.

- His opinion was that NewAgco Barbados was not entitled to a return for any functions performed because it did not perform any.

- He understood NewAgco Barbados had the contract to buy ClearOut from arm's length providers and the contract to sell ClearOut to FNA members.

- He stated that the Services Agreement made AgraCity "responsible to basically provide all the functions that it required to actually make the transaction happen, to get the product from the arm's length suppliers to the arm's length and users".

- When he looked at NewAgco Barbados "they don't actually have any employees, they don't perform any functions directly" "so obviously to the extent that they are having things performed for them that are required for the transaction, we will have to take that into account in pricing the transaction between NewAgco Barbados and AgraCity."

- He stated that in the Services Agreement "NewAgco Barbados doesn't perform any functions, and AgraCity is responsible for essentially all of

[22] Transcript July 17, 2019 pages 259 and 264.

the functions that are required to get the product sold into Canada to Canadian farmers"

- His opinion was that a good understanding of how to allocate the value between parties requires one to "look at the functions that are performed, take into account the assets that are needed and risks that are associated with using those assets and those functions."

- He believed NewAgco Barbados had no inventory risk "because nobody is buying inventory on spec, they always have an order"[23]

- He believed NewAgco Barbados had no pricing risk because FNA Group knows its costs of ClearOut before it set its price to Canadian farmers.[24]

[96] In his cross-examination, Appellant's counsel put to Mr. Rogerson three propositions:

1) Neither AgraCity nor FNA, nor any other Canadian entity could lawfully sell ClearOut to FNA's Canadian members, even through a US branch;

2) NewAgco Barbados actually sourced and negotiated with the arm's length ClearOut supplier Albaugh; and

3) NewAgco Barbados effectively had a monopoly on US ClearOut having negotiated with Albaugh a supply agreement for 95% of Albaugh's production, and was actively buying out other available ClearOut in the US.

[97] Mr. Rogerson agreed that if those facts were correct they do create value in NewAgco Barbados and that would have to be looked at in a functional analysis transfer pricing report.[25]

[98] In re-examination Mr. Rogerson went on to explain that:

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23 This is inconsistent with NewAgco Barbados having purchased NewAgco US' inventory. Further NewAgco Barbados' purchases were neither conditional on, nor contemporaneous with, their sales.

24 This does not address other costs, such as transport, recycling, customs brokers etc. or the associated foreign exchange risk.

25 Transcript July 15, 2019 pages 51 to 53.

- "So what's important is that it is now actively sourcing and negotiating with suppliers, and that they have somehow locked up the supply of the market. So if that's the only product that can be brought in through OUI, and they've got the suppliers of the product, and they are doing the work to negotiate it, then that's what would add the value. …So the fact that they're doing something, and that they have a monopoly, that would give them the ability to add value in the transaction"[26]

[99] There was nothing in any of the Appellant's expert reports or testimony that could provide material support for the Respondent's position that if NewAgco Barbados and AgraCity were arm's length parties, they would have entered into a Services Agreement on terms and conditions that gave 100% of the ClearOut sales profits to AgraCity and no share whatsoever of those profits to NewAgco Barbados - nor did they provide any data, information or support that would help establish that the service fees payable to AgraCity were different than, or outside the range of, what arm's length parties would be expected to provide for.

Burden of Proof

[100] In *House v. The Queen*, 2011 FCA 234, the Federal Court of Appeal allowed the taxpayer's appeal from its loss in our Court. In doing so, Nadon J.A.[27] wrote the following:

> [30] In determining the issue before us, it is important to keep in mind the Supreme Court of Canada's decision in Hickman Motors Ltd. v. Canada, [1997] 2 S.C.R. 336 (Hickman), where Madam Justice L'Heureux-Dubé enunciated, at paragraphs 92 to 95 of her Reasons, the principles which govern the burden of proof in taxation cases:
>
> 1. The burden of proof in taxation cases is that of the balance of probabilities.
>
> 2. With regard to the assumptions on which the Minister relies for his assessment, the taxpayer has the initial onus to "demolish" the assumptions.
>
> 3. The taxpayer will have met his initial onus when he or she makes a prima facie case.

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[26] Transcript July 15, 2019 pages 62 to 63.

[27] As he then was -and is again.

> 4. Once the taxpayer has established a prima facie case, the burden then shifts to the Minister, who must rebut the taxpayer's prima facie case by proving, on a balance of probabilities, his assumptions (in this case, that Hunt River held at the end of taxation year 2002 a long-term investment of $305,000, which it transferred to the appellant in 2003).
>
> 5. If the Minister fails to adduce satisfactory evidence, the taxpayer will succeed.

[31] More particularly, at paragraphs 92 and 93 of her Reasons in Hickman, Madam Justice L'Heureux-Dubé explained in clear terms what onus had to be met by the taxpayer at the initial stage:

> 92. It is trite law that in taxation the standard of proof is the civil balance of probabilities: *Dobieco Ltd. v. Minister of National Revenue*, [1966] S.C.R. 95, and that within balance of probabilities, there can be varying degrees of proof required in order to discharge the onus, depending on the subject matter: *Continental Insurance Co. v. Dalton Cartage Co*., [1982] 1 S.C.R. 164; *Pallan v. M.N.R.*, 90 D.T.C. 1102 (T.C.C.), at p. 1106. The Minister, in making assessments, proceeds on assumptions (*Bayridge Estates Ltd. v. M.N.R.*, 59 D.T.C. 1098 (Ex. Ct.), at p. 1101) and the initial onus is on the taxpayer to "demolish" the Minister's assumptions in the assessment (*Johnston v. Minister of National Revenue*, [1948] S.C.R. 486; *Kennedy v. M.N.R.*, 73 D.T.C. 5359 (F.C.A.), at p. 5361). The initial burden is only to "demolish" the exact assumptions made by the Minister but no more: *First Fund Genesis Corp. v. The Queen*, 90 D.T.C. 6337 (F.C.T.D.), at p. 6340.
>
> 93 This initial onus of "demolishing" the Minister's exact assumptions is met where the appellant makes out at least a prima facie case: *Kamin v. M.N.R.*, 93 D.T.C. 62 (T.C.C.); *Goodwin v. M.N.R.*, 82 D.T.C. 1679 (T.R.B.). In the case at bar, the appellant adduced evidence which met not only a prima facie standard, but also, in my view, even a higher one. In my view, the appellant "demolished" the following assumptions as follows: (a) the assumption of "two businesses", by adducing clear evidence of only one business; (b) the assumption of "no income", by adducing clear evidence of income. The law is settled that unchallenged and uncontradicted evidence "demolishes" the Minister's assumptions: see for example *MacIsaac v. M.N.R.*, 74 D.T.C. 6380 (F.C.A.), at p. 6381; *Zink v. M.N.R.*, 87 D.T.C. 652 (T.C.C.)...

[101] The Federal Court of Appeal's approach in *House* was not interfered with by the majority in its later decision *Sarmadi v.The Queen*, 2017 FCA 131. However, in his concurring reasons in *Sarmadi* Webb J.A. developed a new and, from my perspective as a trial judge, preferable approach and interpretation of the development of the jurisprudence governing the parties' burden of proof and onus in tax cases. The issue of onus in tax cases was recently reviewed by the Federal

Court of Appeal in *Eisbrenner v. The Queen*, 2020 FCA 93, the appeal from Justice Owen's decision in this Court in *Morrison v. The Queen* 2018 TCC 220.

[102] In *Eisbrenner* it appears that JA Webb writing the unanimous reasons adopted his dissenting approach in *Sarmadi* to the parties' onus and burden of proof in the Tax Court.

[103] In *Sarmadi*, JA Stratas, with whom JA Woods concurred on this issue, described JA Webb's approach to burden as a "thoughtful, illuminating and attractive" articulation of this fundamental issue. He went on to invite judges of the Tax Court to share their useful insights.

[104] I commend all of theses judges of the Federal Court of Appeal for their efforts to see that the law in this area be reviewed and perhaps evolve. For what it is worth, never in my experience has the *Hickman Motors* initial onus /*prima facie*/demolish assumptions/shifting burden gloss on the civil balance of probabilities standard been necessary or particularly helpful. It can almost always be expected to generate much more heat than light in the courtroom. This is not to say I did not try to rely on it when it would help my client or apply it when it could make my reasons more simple. It is the law as set out by the Supreme Court of Canada and that is binding on me. I applaud all efforts to have it reviewed and would favour an outcome that simply applies the ordinary civil burden and onus of the balance of probabilities standard in the Tax Court in the same manner as that standard applies in all other non-criminal trials in Canadian courts.

[105] That said, I am mindful that the *Hickman Motors* approach is expressly grounded in even earlier decisions of the Supreme Court of Canada, and that the Supreme Court of Canada has never clearly and expressly reviewed its *Hickman Motors* decision, much less clearly overruled it. As a trial judge I am also mindful of my position in the Fundukian/Bowmanesque judicial pecking order.[28] In *The Queen v. Craig* 2012 SCC 43 the Supreme Court unanimously makes it clear that lower courts are not entitled to disregard or purport to overrule their precedent that is up to the Supreme Court alone and it can be expected to do that clearly and expressly: See paragraphs 3, 18-23, 24-25, 26-31 and 32 of Justice Rothstein's

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[28] See *Sussex Square Apartments Ltd. v. HMQ* (1998) 97-620-ITG at footnote 2.

reasons in *Craig*. For these reasons I am following the *Hickman Motors* and *House* line of jurisprudence on the issue.[29]

Disposition of Appeals

[106] This Court has found that the ClearOut purchase, sale, and related transactions were not a sham, nor was any individual transaction in the series of transactions beginning with the incorporation of NewAgco Barbados for the ClearOut sales activity a sham. The transactions that occurred and were documented were the transactions the parties intended, agreed to, and that the parties reported to others including the CRA. Any shortcomings in any paperwork was not intended by the Appellant or anyone else in the FNA Group to deceive the CRA or anyone else.

[107] This Court has found that:

- In 2005 NewAgco US was chosen to be the purchaser and seller of the ClearOut because it was generally understood by James Mann and by others involved in the FNA Group that a non-Canadian entity was required under the OUI program as administered by the PMRA under the PMCA, and that FNA could only promote ClearOut's availability under that program to its members and potential members. Further, I find their understanding was a reasonable one in the circumstances. This understanding was unchanged when NewAgco US' business was transferred to NewAgco Barbados in early 2006.

- NewAgco Barbados was the purchaser of the ClearOut, and was the beneficial owner of the ClearOut acting on its own account upon purchasing it until it sold the ClearOut to the Canadian farmers. It was not a holder of a buy-sell contract agent, bare trustee, prête-nom or any form of nominee or nominal title-holder.

- NewAgco Barbados paid for its purchases and received the sales proceeds for its own account.

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[29] I am quite certain that AgraCity's appeal would also succeed if I had to apply Justice Webb's interpretation of the law on burden of proof in tax appeals set out in paragraphs 61 to 63 of his reasons in *Samardi* (dissenting on this point) and in *Eisbrenner*. I would however be writing these reasons somewhat differently.

- NewAgco Barbados had sourced all of the relevant US ClearOut that it had bought and sold. Jason Mann did this on behalf of NewAgco Barbados which had duly authorized him to do exactly that. NewAgco Barbados was buying all of the US ClearOut that it could locate.

- NewAgco Barbados had Jason Mann negotiate an exclusive supply agreement with Albaugh which secured NewAgco Barbados access to 95% of US ClearOut manufactured by the only person with the right to manufacture US ClearOut.

- NewAgco Barbados took real foreign exchange risk in its ClearOut sales activities because it was buying and incurring related expenses in US dollars and selling in Canadian dollars. That foreign exchange risk was able to be minimised with respect to the costs of purchasing the US ClearOut, but not with respect to some of the US transport costs for delivering the ClearOut once sold to the Canadian farmers, or US warehouse costs and other expenses associated with those activities that were performed in the US.

- NewAgco Barbados took real risk as owner of large volumes of a chemical based regulated herbicide applied to food products, and as an international transporter of that product to the Canadian farmers.

- The Services Agreement is the proper transaction whose terms, rights and obligations are to be reviewed for purposes of the transfer pricing rules in the *Act*.

[108] These findings, based on the Appellant's evidence and the Respondent's evidence in response thereto, clearly makes out a *prima facie* case that the reassessments are incorrect and demolishes the Respondent's assumptions of fact that supported the transfer pricing adjustments that allocated all of NewAgco Barbados' net sale profits of approximately six million dollars to the Appellant. This leaves the Court having to determine what amount, less than all and greater than none, of NewAgco Barbados′ net sales profits would have been payable by NewAgco Barbados to the Appellant for the services provided by AgraCity under the Services Agreement had they been dealing at arm's length.

[109] The Appellant had reported approximately two million dollars of service fees (calculated at the agreed 15 and 20 cent per litre rates) earned by it under the Services Agreement in the period in question. It is that amount that the

reassessments impugn as far too low for the value of the services provided and as an amount far less than arm's length parties would have agreed to.

[110] The services provided by AgraCity pursuant to the Services Agreement were largely, though not exclusively, logistical in nature. They were also largely subcontracted by AgraCity to arm's length third parties at arm's length rates, eg transportation, warehouse, customs brokers, container recycling and disposal etc.

[111] The Respondent has chosen not to provide the Court with any evidence in support of how to determine any such amount, nor what to base it upon or test it against. The Respondent instead maintains it must be all of the net sales profits that would have been payable by an arm's length party to AgraCity. The Respondent's expert could not offer any help to the Court even after he acknowledged that if NewAgco Barbados was the party actually sourcing the US ClearOut and had secured a quasi-monopoly on supply, those facts would mean that NewAgco Barbados did bring value to the transactions.

[112] The Appellant's expert Brad Rolph provided expert opinion evidence in support of the service fee in the Services Agreement generating revenues for AgraCity for its services under the Services Agreement within the arm's length range. He set this out in his Rebuttal Report to the Respondent's Rogerson Economic Transfer Pricing report and he explained it in his testimony. In essence, Mr. Rolph's report looked at available data on returns, margins or mark-ups on costs earned by North American corporations that are known to provide broadly similar logistics services. He looked in particular at large public corporations, many in the US, and at large Canadian freight forwarding, brokerage and agency companies. Based on these available numbers, such companies would earn in the range of 5 to 15% returns over their costs. The cost plus method is also recognized in the OECD transfer pricing guidelines and should be considered in the absence of comparable uncontrolled arm's length prices (CUPs).[30]

[113] In his Rebuttal Report, Mr. Rolph calculated AgraCity's return on costs on a comparable basis as approximately 30%. In his testimony, he acknowledged that it

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30 Apparently some transfer pricing experts would refer to this approach as the transactional net margin method or TNMM and not CUP, even though the available data is not, in Mr. Rolph's opinion, transactional.

would be fair to regard it as more appropriately being about 12% because in his report he had calculated return on costs after backing out from AgraCity's costs amounts paid by it to FNA as would be done under the OECD guidelines, whereas the available arm's length data would have been calculated on total costs including those incurred to non-arm's length parties.[31]

[114] Based on this, Mr. Rolph's opinion was that AgraCity's returns were at the higher end of the range of comparable cost plus returns from the available data he could obtain, and that AgraCity's service fee under the Services Agreement was a reasonable rate of return for its primarily logistics services.

[115] This evidence is clearly not without its limitations. Mr. Rolph himself described it as "just a crude benchmarking analysis". It is however the only evidence the Court has been given by either party that addresses the ultimate question to be decided under paragraphs 247(2) (*a*) and (*c*) of whether the amount received by AgraCity from NewAgco Barbados for its services relating to the ClearOut sales was an amount that would have been payable between arm's length persons for those services.

[116] The only evidence the Court has on the point indicates that the amount paid to AgraCity generated a return on its costs that was in the range of what somewhat comparable arm's length parties earn. Being the only evidence of what notional arm's length parties would have agreed to for the services provided by AgraCity, it is also by definition the best evidence the Court has, notwithstanding its limitations.

[117] I conclude that the Appellant has met its initial onus to "demolish" the Respondent's assumptions as set out by the Supreme Court of Canada in *Hickman Motors* and again by the Federal Court of Appeal in *House*. The Appellant has gone far beyond making out a *prima facie* case. The Respondent has failed to produce satisfactory evidence from its own witnesses or those of the Appellant to prove on a balance of probabilities that its relevant assumptions, or its further allegations and positions, were correct. Therefore the taxpayer succeeds in this appeal.

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[31] Transcript July 16, 2019 pages 177 to 179, 186, 191 to 193, 203, 205 to 206 and 208 to 209.

[118] I can add that, even if Justice Webb's arguably more attractive, fair and equitable approach to burden of proof and onus with respect to tax appeals in *Sarmadi* and *Eisbrenner* were the approach required or chosen to be applied, I would also find for the Appellant. The taxpayer has provided credible, unchallenged, uncontested and unrefuted expert evidence based on available data that confirms the amount reported by AgraCity as its profit over the costs of its services to NewAgco Barbados was well within the somewhat rough, but in my view acceptable, range of what an arm's length service provider might have enjoyed in circumstances similar to what I have found to be the transactions between NewAgco Barbados and AgraCity.

Penalties

[119] Neither of the penalties assessed can be supported.

Costs

[120] Costs are awarded to both Appellants. The parties shall have 30 days from the date hereof to reach an agreement on costs, failing which the parties shall have a further 30 days to file written submissions on costs. Each party will have a further 15 days thereafter to file any responding submissions. Any such submissions shall not exceed 15 pages in length initially, and 10 pages for responding submissions. If the parties do not advise the Court that they have reached an agreement and no submissions are received from the Appellants, costs shall be awarded in the amount set out in the Tariff to the *Rules*.

Signed at Montreal, Quebec, this 27th day of August 2020.

"Patrick Boyle"

Boyle J.

Appendix 1 Transfer Pricing Recharacterisation

247(2) Transfer pricing adjustment- Where a taxpayer …and a non-resident person with whom the taxpayer does not deal at arm's length…are participants in a transaction or a series of transaction and

…

(b) the transaction or series

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

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

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 … 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,

(d) where paragraph (b) applies, the transaction or series entered into between the participants had been the transaction or series that would have been entered into between persons dealing at arm's length, under terms and conditions that would have been made between persons dealing at arm's

247(2) Redressement – Lorsqu'un contribuable… et une personne non-résidente avec laquelle le contribuable, … a un lien de dépendance, … prennent part à une opération ou à une série d'opérations et que, selon le cas:

…

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

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

(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,

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 … 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 :

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 les modalités qui auraient été conclues entre de

length.

telles personnes.

Appendix 2 Transfer Pricing Adjustments

247(2) Transfer pricing adjustment – Where a taxpayer and a non-resident person with whom the taxpayer … does not deal at arm's length … are participants in a transaction or a series of transactions and

> (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

any amounts that, but for this section and section 245, would be determined for the purposes of this Act in respect of the taxpayer … 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,

> (c) Where only paragraph (a) applies, the terms and conditions made or imposed, in respect of the transaction or series, between the participants in the transaction or series had been those that would have been made between persons dealing at arm's length …

247(2) Redressement – Lorsqu'un contribuable … et une personne non-résidente avec laquelle le contribuable … 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) les modalité 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,

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 … 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) dans le cas où l'alinéa a) s'applique les modalités conclues ou imposées, relativement à l'opération ou à la série, entre les participants avaient été celles qui auraient été conclues entre personnes

sans lien de dépendance ;

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REASONS FOR JUDGMENT BY:	The Honourable Justice Patrick Boyle
DATE OF JUDGMENT:	August 27, 2020

APPEARANCES:

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Counsel for the Respondent:	Pascal Tétrault Vincent Bourgeois John Krowina

COUNSEL OF RECORD:

For the Appellant:

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