Federal Court of Appeal  Cour d'appel fédérale

Date: 20151030

Docket: A-125-14

Ottawa, Ontario, October 30, 2015

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

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

and

FIO CORPORATION

Respondent

JUDGMENT

The appeal is allowed, with costs. The Order of the Tax Court of Canada dated February 20, 2014 is set aside and the motion of Fio Corporation for an Order vacating the October 2012 reassessments is dismissed, with costs in the Tax Court of Canada.

"Johanne Gauthier"
J.A.

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Respondent

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

Judgment delivered at Ottawa, Ontario, on October 30, 2015.

REASONS FOR JUDGMENT BY: WEBB J.A.

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

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REASONS FOR JUDGMENT

WEBB J.A.

[1] The issue in this appeal is the application of the implied undertaking rule to the specific facts of this case. D'Arcy J, of the Tax Court of Canada, issued an Order dated February 20, 2014 (2014 TCC 58). This Order prohibited the Crown from using certain documents that had been submitted by Fio Corporation (when it commenced its appeal to the Tax Court of Canada) in any other proceeding. Costs in the amount of $25,000 were also awarded to Fio Corporation

and the Crown was given 30 days to file an application for leave to use the prohibited documents in another proceeding.

[2] The Crown has appealed this Order. For the reasons that follow, I would allow this appeal.

Background

[3] Fio Corporation in 2007 and 2008 was working "on the development of a portable medical diagnostic instrument … that can screen a specimen of human blood and detect the presence of one or more of a wide range of human diseases…" (Affidavit of Stephen Petes, Chief Information Officer for Fio Corporation, dated April 17, 2013).

[4] In filing its tax returns for 2007 and 2008 under the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) (the Act), Fio Corporation claimed scientific research and experimental development tax credits (SRED Credits). In 2009, the Canada Revenue Agency (CRA) audited these claims. In particular, on October 2, 2009 Gary Kakis, a science auditor, and Amir Giga, a financial auditor, attended at the offices of Fio Corporation. Stephen Petes confirmed that a number of documents were made available to the CRA auditors.

[5] The Minister of National Revenue (the Minister) reassessed Fio Corporation in relation to its SRED Credits that were claimed in 2007 and 2008 by notices of reassessment dated March 2, 2011 and March 11, 2011. Fio Corporation served notices of objection to these reassessments.

On April 12, 2012, Fio Corporation filed a notice of appeal to the Tax Court of Canada without having received a response from the Minister in relation to the notices of objection. At the same time that Fio Corporation filed its notice of appeal, it also forwarded to the Department of Justice a list of documents under Rule 81 (Partial Disclosure) of the *Tax Court of Canada Rules (General Procedure)* (the Rules) and copies of the documents that were on this list. The Tax Court Judge referred to the documents that were sent to the Department of Justice on April 12, 2012 as the Discovery Documents and for ease of reference I will use the same term in referring to these documents.

[6] The Department of Justice forwarded the Discovery Documents to the Minister. Upon reviewing these documents, additional reassessments were issued for 2007 and 2008 in October 2012 to reduce the SRED Credits for 2007 and 2008. In 2013, following the issuance of these reassessments, Fio Corporation brought the motion before the Tax Court of Canada that is the subject of this appeal. This motion was for an Order vacating the reassessments issued in October 2012 on the basis that the making of these reassessments was "a violation of the implied undertaking rule and a contempt of this Court" (paragraph 7 of the Notice of Motion of Fio Corporation).

Decision of the Tax Court

[7] At paragraph 15 of his reasons, the Tax Court Judge made the following finding of fact:

> [15] Counsel for the Respondent admitted that the Minister based the Second Reassessments, at least in part, on documents that she *obtained for the first time* in the course of pre-trial discovery, specifically, documents that were included in the

> Appellant's List of Documents and provided to counsel for the Respondent on April 12, 2012 (the Discovery Documents).
>
> (emphasis added; citation omitted)

[8] The Tax Court Judge then referred to certain passages from the decision of the Supreme Court of Canada in *Juman v. Doucette*, 2008 SCC 8, [2008] 1 S.C.R. 157 [*Juman*]. The Tax Court Judge determined that Fio Corporation's appeal commenced when it filed its notice of appeal and that since the Discovery Documents were obtained by counsel for the Crown "in the course of discovery" (paragraphs 40 and 50 of his reasons), the implied undertaking rule was applicable. The Tax Court Judge also concluded that the reassessments issued in October 2012 "gave rise to new litigation".

[9] However, having made these findings, the Tax Court Judge did not grant the request of Fio Corporation to vacate the October 2012 reassessments but rather he granted the following Order:

> In accordance with the attached Reasons for Order:
>
> a) The Court orders the [Crown] not to use any documents obtained by the [Crown] in the course of the discovery relating to [Fio Corporation's] appeal instituted on April 12, 2012 in any other proceeding before this Court or any other court. The Court's order does not apply to any documents that the Canada Revenue Agency obtained prior to the date [Fio Corporation] instituted its appeal.
>
> b) Costs are awarded to [Fio Corporation] in the amount of $25,000.
>
> c) The [Crown] shall have 30 days to file an application with the Court for leave to use the relevant documents in another proceeding.

Standards of review

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

Issue

[11] The issue in this appeal is whether, based on the facts of this case, the implied undertaking rule was applicable to the Discovery Documents.

Implied undertaking rule

[12] There is no implied undertaking rule in the Rules. However, there is no dispute in this appeal that the implied undertaking rule applies to litigants before the Tax Court of Canada. In order to determine whether this rule applies to the Discovery Documents in this case it is necessary to review the rule.

[13] In *Juman*, the issue was whether alleged criminal activity discovered in a civil proceeding could be disclosed to the police. Binnie J, writing on behalf of the Supreme Court of Canada, stated at paragraph 1 that:

> The principal issue raised on this appeal is the scope of the "implied undertaking rule" under which evidence compelled during pre-trial discovery from a party to civil litigation can be used by the parties only for the purpose of the litigation in which it was obtained….

[14] The implied undertaking rule applies to evidence (which would include documents) that a party to civil litigation is compelled to disclose in the course of that litigation. The requirement that the disclosure is compelled in the course of the litigation is emphasized several times by Binnie J. (see, for example, paragraphs 4, 5, 24, 25 and 27). This requirement is also consistent with the rationale for the rule as set out in paragraphs 23 to 27 of *Juman*:

> [23] Quite apart from the cases of exceptional prejudice, as in disputes about trade secrets or intellectual property, which have traditionally given rise to express confidentiality orders, there are good reasons to support the existence of an implied (or, in reality, a court-imposed) undertaking.
>
> [24] In the first place, pre-trial discovery is an invasion of a private right to be left alone with your thoughts and papers, however embarrassing, defamatory or scandalous. At least one side in every lawsuit is a reluctant participant. Yet a proper pre-trial discovery is essential to prevent surprise or "litigation by ambush", to encourage settlement once the facts are known, and to narrow issues even where settlement proves unachievable. Thus, rule 27(22) of the B.C. *Rules of Court* compels a litigant to answer all relevant questions posed on an examination for discovery. Failure to do so can result in punishment by way of imprisonment or fine pursuant to rules 56(1), 56(4) and 2(5). In some provinces, the rules of practice provide that individuals who are not even parties can be ordered to submit to examination for discovery on issues relevant to a dispute in which they may have no direct interest. It is not uncommon for plaintiff's counsel aggressively to "sue everyone in sight" not with any realistic hope of recovery but to "get discovery". Thus, for the out-of-pocket cost of issuing a statement of claim or other process, the gate is swung open to investigate the private information and perhaps highly confidential documents of the examinee in pursuit of allegations that might in the end be found to be without any merit at all.

> [25] The public interest in getting at the truth in a civil action outweighs the examinee's privacy interest, but the latter is nevertheless entitled to a measure of protection. The answers and documents are compelled by statute solely for the purpose of the civil action and the law thus requires that the invasion of privacy should generally be limited to the level of disclosure necessary to satisfy that purpose and that purpose alone. Although the present case involves the issue of self-incrimination of the appellant, that element is not a necessary requirement for protection. Indeed, the disclosed information need not even satisfy the legal requirements of confidentiality set out in *Slavutych v. Baker*, [1976] 1 S.C.R. 254. The general idea, metaphorically speaking, is that whatever is disclosed in the discovery room stays in the discovery room unless eventually revealed in the courtroom or disclosed by judicial order.
>
> [26] There is a second rationale supporting the existence of an implied undertaking. A litigant who has some assurance that the documents and answers will not be used for a purpose collateral or ulterior to the proceedings in which they are demanded will be encouraged to provide a more complete and candid discovery. This is of particular interest in an era where documentary production is of a magnitude ("litigation by avalanche") as often to preclude careful pre-screening by the individuals or corporations making production. See *Kyuquot Logging Ltd. v. British Columbia Forest Products Ltd.* (1986), 5 B.C.L.R. (2d) 1 (C.A.), per Esson J.A. dissenting, at pp. 10-11.
>
> [27] For good reason, therefore, the law imposes on the parties to civil litigation an undertaking to the court not to use the documents or answers for any purpose other than securing justice in the civil proceedings in which the answers were compelled (whether or not such documents or answers were in their origin confidential or incriminatory in nature)….

[15] The rationales for this rule are only applicable if the evidence in question is disclosed as part of the litigation and such disclosure is compulsory. If the evidence has previously been disclosed, there is no invasion of privacy in relation to such evidence as a result of the pre-trial discovery. Any invasion of privacy would have occurred earlier when the evidence was first disclosed. If the evidence has previously been disclosed, there is also no need to encourage "a more complete and candid discovery". As well, if the disclosure is made voluntarily and the person is not compelled to make that disclosure, the concerns about the invasion of privacy are reduced as the person chose to make the particular disclosure. The lack of compulsion would

also reduce the likelihood of a more complete and candid discovery as the person could choose what to disclose or keep secret.

[16] As a result, in my view, in relation to appeals before the Tax Court of Canada, the implied undertaking rule does not apply to:

(a) any evidence that was disclosed prior to the commencement of the proceedings in the Tax Court of Canada; or

(b) any evidence that a party produced in the course of such proceedings but which such party was not compelled to produce as part of such proceedings.

Analysis

[17] The first question that must be addressed is whether the Discovery Documents had previously been disclosed to the Minister. In my view, the Tax Court Judge made a palpable and overriding error in finding that the Discovery Documents were first disclosed to the Minister following the delivery of such documents to the Department of Justice on or about April 12, 2012. As noted above, the Tax Court Judge made this finding at paragraph 15 of his reasons. In the footnote for this paragraph he referred to the transcript of the hearing, pages 85 and 97, as support for this finding.

[18] However, page 85 of the transcript reveals that counsel for the Crown made the following submissions:

> Ms. Linden: … Stephen Petes, the Appellant's affiant admitted in his affidavit and on cross-examination - - this is very important. My friend made no reference to

> this fact, and in our respectful submission, this is the key fact - - that the documents at issue - - that is, actually, not only the four [*sic*] document, but the seven volumes as I take as evidence - - had already been available to the auditor in 2009.
>
> The reference for that to the evidence is the Affidavit of Mr. Petes at paragraph 31. It's in the Appellant's Motion Record at Tab C.
>
> > "All 314 documents that were disclosed on our behalf in the Tax Court appeal were available to both Mr. Kakis, the science auditor and Mr. Giga, the financial auditor, during the reviews in 2009 and 2010."
>
> I asked him about that on his cross-examination. You have the transcript. I started to discuss it at question 205, but I think a cleaner question and answer can be found at question 243 of the examination.
>
> Here's my question:
>
> > "So then I take it that it's your evidence that all of the documents that have been produced under the list of Documents for partial disclosure, the three sets - -"
>
> The three sets - - it's only the first set that was the 261 documents from which the four that are relevant to this come.
>
> > "- - including the biggest set, which went in advance of the Notice of Appeal, having been ascribed a court - -"
>
> I should have said "having not yet been ascribed a court file number."
>
> > "- - which were in those seven books, according to your affidavit were all disclosed on your behalf, were all available to Mr. Kakis, the science auditor, and Mr. Giga, the financial auditor. So all those taxpayer records were available to both sets of auditors, the science auditor and the financial auditor."
>
> And the answer is, "Plus a lot more."

[19] These submissions are not an admission that the Minister obtained the Discovery Documents for the first time following the submission of these documents by Fio Corporation on April 12, 2012. These are detailed submissions, with references to the affidavit of Steven Petes that had been filed by Fio Corporation in support of its motion and also to the transcript of his

cross examination that confirmed that the Discovery Documents had previously been made available to the CRA, who were acting on behalf of the Minister.

[20] The Tax Court Judge also referred to page 97 of the transcript of the hearing. However, the only relevant statement disclosed on this page is the confirmation by the Tax Court Judge that the reassessments issued in October 2012 were based on documents that were included as part of the Discovery Documents. There is no indication that counsel for the Crown was retracting her earlier submissions that these documents had previously been made available to the CRA auditors. Subsequent to the statements that appear at page 97 of the transcript of the hearing, counsel for the Crown, in submissions that appear at page 127 of this transcript, reiterated her position that "by the Appellant's own admission, they had already been made available to the CRA auditors in 2009, well before and quite apart from any obligation to do so under the discovery rules in a tax appeal".

[21] As a result there was no basis upon which the Tax Court Judge could have concluded that the first time that the Discovery Documents were disclosed to the Minister was after April 12, 2012 and the evidence presented at the Tax Court hearing (which Fio Corporation did not dispute in this appeal) was that all of the Discovery Documents had previously been made available to the CRA auditors in 2009 and 2010. Although the CRA auditors may not have appreciated the significance of some of the documents, and in particular the four documents upon which the October 2012 reassessments were based, this does not change the fact that these documents had been disclosed to them prior to the commencement of the appeal to the Tax Court of Canada.

[22] The error of the Tax Court Judge in finding that the documents were first disclosed in April 2012 was a palpable and overriding error. The evidence does not support this finding and this finding would have a direct impact on the result. Since, based on the evidence submitted, the documents were previously disclosed to the CRA auditors in 2009, the implied undertaking rule does not apply to the Discovery Documents.

[23] The Tax Court Judge also made additional comments with respect to section 241 of the Act that he noted were not needed in this matter. In his view, Fio Corporation was compelled to disclose the Discovery Documents under the Rules.

[24] In this case, Fio Corporation provided the Discovery Documents under Rule 81 (the partial disclosure rule). Since I have found that the Discovery Documents had previously been disclosed to the CRA, it is not necessary, in this appeal, to decide whether documents disclosed under Rule 81 would be documents that the taxpayer is compelled to disclose. It is also not necessary to decide whether the reassessments issued in October 2012 gave rise to new litigation. As a result I would defer these questions to another appeal where it would be necessary to make such determinations. Nothing herein should be construed as an endorsement of the Tax Court Judge’s conclusions on these questions.

[25] Fio Corporation had also made submissions with respect to the different roles of the Minister and the Crown in assessing tax under the Act and in tax appeals. In light of my finding that the implied undertaking rule does not apply to the Discovery Documents, it is not necessary to address these arguments. However, I would note that since the appeal before the Tax Court of

Canada is in relation to the reassessments issued by the Minister, it was appropriate, in my view, for the Department of Justice to send the Discovery Documents to the CRA, who are acting on behalf of the Minister in enforcing the Act. In doing so, the Department of Justice was simply sending documents to the CRA that had previously been made available to the CRA auditors who were reviewing the SRED Credits claimed by Fio Corporation under the Act.

Conclusion

[26] The Order of the Tax Court stated that the Order did not apply to any documents that the CRA had obtained prior to the date that Fio Corporation had instituted its appeal. Since the Discovery Documents had been made available to the CRA prior to Fio Corporation instituting its appeal, it would appear that the Order does not apply to these documents. From reading the reasons and the other parts of the Order awarding costs of $25,000 to Fio Corporation and providing that the Crown "shall have 30 days to file an application with the Court for leave to use the relevant documents in another proceeding", it is clear that the Tax Court Judge intended that the first part of his Order prohibiting the use of the documents would apply to the Discovery Documents. To remove any doubt I would set aside the Order of the Tax Court.

[27] As a result, I would allow the appeal, with costs, set aside the Order of the Tax Court of Canada, and dismiss the motion of Fio Corporation for an Order vacating the October 2012 reassessments, with costs in the Tax Court of Canada.

"Wyman W. Webb"
J.A.

“I agree.
Johanne Gauthier J.A.”

“I agree.
D.G. Near J.A.”

FEDERAL COURT OF APPEAL

NAMES OF COUNSEL AND SOLICITORS OF RECORD

AN APPEAL FROM THE ORDER OF THE HONOURABLE JUSTICE STEVEN K. D'ARCY OF THE TAX COURT OF CANADA DATED FEBRUARY 20, 2014, COURT FILE NO.: 2012-1452(IT)G

DOCKET:	A-125-14
STYLE OF CAUSE:	HER MAJESTY THE QUEEN v. FIO CORPORATION
PLACE OF HEARING:	TORONTO, ONTARIO
DATE OF HEARING:	APRIL 30, 2015
REASONS FOR JUDGMENT BY:	WEBB J.A.
CONCURRED IN BY:	GAUTHIER J.A. NEAR J.A.
DATED:	OCTOBER 30, 2015

APPEARANCES:

Wendy Linden Toronto, Ontario	FOR THE APPELLANT
A. Christina Tari Toronto, Ontario	FOR THE RESPONDENT

SOLICITORS OF RECORD:

William F. Pentney Deputy Attorney General of Canada	FOR THE APPELLANT
Richler and Tari Toronto, Ontario	FOR THE RESPONDENT