Implied Undertaking Rule in Tax Court Appeals

Implied Undertaking Rule in Tax Court Appeals - Use of Documents obtained through discovery

Fio Corporation v The Queen, 2014 TCC 58

The taxpayer brought a motion directing the MNR and AG Canada to pay $100,000 as "punishment for her/their contempt of this Court" and costs on full indemnity basis for the breach of the implied undertaking rule as it relates to the use of information obtained in the course of pre-trail discovery proceedings.

The TCC held that once a taxpayer provides discovery documents to the respondent in the course of discovery, there is an **implied undertaking to the Court** not to use the information for purposes other than the appeal. The court stated that "[t]he Respondent's use of the Discovery Documents without leave of the Court constitutes an abuse of process. That abuse was not inadvertent" (para 77).

The TCC noted that it has the power to vacate the reassessment as a remedy, but ordered: (i) the documents not to be used by the MNR for a purpose other than the first assessment appeal; and (ii) substantial costs of $25,000 against the MNR for breach of the implied undertaking rule.

FACTS

The taxpayer filed a Notice of Appeal to the TCC from a reassessment by the MNR, and after filing the notice (but on the same day) provided respondent counsel with a number of documents. Accompanying the documents was a letter that made it clear that the documents were provided along with the Notice of Appeal, and for the purpose of minimizing time and costs involved in resolving the appeal and with the hope of reaching a settlement.

The MNR reassessed the taxpayer on the basis of these documents for taxation years other than those under the original appeal.

ANALYSIS

The TCC referred to the Supreme Court of Canada decision in *Juman v. Doucette*, 2008 SCC 8 , where at paragraph 4 it was stated:

> [...] the rule is that both documentary and oral information obtained on discovery, including information thought by one of the parties to disclose some sort of criminal conduct, is subject to the implied undertaking. It is not to be used by the other parties except for the purpose of that litigation, unless and until the scope of the undertaking is varied by a court order or other judicial order or a situation of immediate and serious danger emerges.

The implied undertaking rule exists because of the invasive nature of pre-trial discover, and the need for complete and candid discovery. The implied undertaking rule applied to pre trial discovery under the *Tax Court of Canada Rules (General Procedure)*. The TCC stated:

- An appeal with the TCC is commenced when the Notice of Appeal is filed with the court, and not when the TCC serves the Notice of Appeal on the Respondent (Section 17.2, *Tax Court of Canada Act*);
- Documents provided pursuant to the TCC rules for discovery are not provided voluntarily, but as part of pre-trial discovery;

The respondent used the documents for a purpose “other than securing justice in the civil proceedings in which the answers were compelled" when the MNR used them to reassess the taxpayer. This second reassessment results in new litigation.

The TCC rejected the MNR's argument that the implied undertaking rule doesn't apply to the Minister in the fact situation before the court. Since the MNR has relied on the implied undertaking rule in the past, the court would not endorse more favourable treatment for one party. This argument would defeat the purpose of the implied undertaking rule, and the MNR is not able to use any information obtained during the discovery process for assessment purposes (unless it applied to the court for such use). The undertaking is to the Court.

Whether or not the MNR would have obtained the information otherwise, for example through an audit, is irrelevant to the question of whether the undertaking was breached. This fact may be relevant when the court is considering an application by the MNR to either modify or relief the MNR's implied undertaking.

The MNR, to use information covered by the implied undertaking, must apply to the Court for leave to use these documents for a valid purpose **before** using the documents for a purpose other than the appeal. The TCC will never automatically grant such leave as an undertaking will only be set aside in exceptional circumstances.

The TCC also dealt with the argument that Subsection 241(4) of the ITA allows the MNR to use any information however obtained for the listed purposes. The TCC stated that subsection 241(4) was an exception to the section 241(1) duty to keep taxpayer information confidential, and did not apply to the implied undertaking to the Court and does not override common-law rules. It was also irrelevant, for purposes of the implied undertaking rule, that the taxpayer has a low expectation of privacy with respect to tax records as privacy is not a condition of the application of the implied undertaking rule.

As for remedies, the court recognized that it has the power to vacate the second assessment and that this may be a proper remedy where that assessment is based entirely on the information obtained in breach of the implied undertaking (*Ereiser v. The Queen*, 2013 FCA 20). The TCC may vacate an appeal were the assessment is found to not be "valid" - not in compliance with the procedural provisions of the ITA - not "correct" - the amount of tax is determined using an incorrect interpretation of the ITA provisions as applied to the assessment - or when vacating the appeal is part of the jurisdiction of the court to control its own process and

ensure its proper functioning (paras 68-69) (see *R v Cunningham,* 2010 SCC 10). The TCC is both a Superior Court and a Statutory Court, and a remedy of a breach of the implied undertaking rule may be corrected by exercising the Court's inherent power to control its own process.

The TCC ordered that the documents may not be used by the MNR as part of the second assessment of the taxpayer, but gave the MNR 30 days to apply for leave to use the documents for such a purpose. Also, though contempt is a remedy available for breach of the implied undertaking, it is a drastic measure to be taken only when no other will suffice. In this case an award of substantial costs of $25,000 was seen as appropriate.

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