Federal Court  Cour fédérale

Date: 20111101

Citation: 2011 FC 1249

Ottawa, Ontario, November 1, 2011

PRESENT: The Honourable Madam Justice Tremblay-Lamer

Docket: T-1619-09

BETWEEN:

THE MINISTER OF NATIONAL REVENUE

Applicant

and

RBC LIFE INSURANCE COMPANY

Respondent

Docket: T-484-10

AND BETWEEN:

THE MINISTER OF NATIONAL REVENUE

Applicant

and

INDUSTRIAL ALLIANCE PACIFIC INSURANCE AND FINANCIAL SERVICES INC.

Respondent

Docket: T-485-10

AND BETWEEN:

LE MINISTRE DU REVENUE NATIONAL

Applicant

and

INDUSTRIELLE ALLIANCE ASSURANCE ET SERVICES FINANCIERS INC.

Respondent

Docket: T-879-10

AND BETWEEN:

THE MINISTER OF NATIONAL REVENUE

Applicant

and

BMO LIFE ASSURANCE COMPANY

Respondent

REASONS FOR JUDGMENT AND JUDGMENT

[1] These are four motions, brought by the respondents RBC Life Insurance Company, Industrial Alliance Pacific Insurance and Financial Services Inc., Industrielle Alliance Assurance et Services Financiers Inc. and BMO Life Assurance Company [collectively the Insurers], to cancel *ex parte* orders of this Court dated October 6, 2009, April 12, 2010 and June 7, 2010. The orders were issued pursuant to section 231.2(3) of the *Income Tax Act*, RSC 1985, c 1 (5th Supp) [the Act], and

authorize the Minister of National Revenue to impose on the Insurers requirements to produce certain information and documents.

[2] For the reasons that follow, the motions will be granted.

Part I – Background Facts

[3] On October 6, 2009, Justice Yvon Pinard granted the Minister of National Revenue [the Minister] *ex parte* authorization to issue the requirement to RBC Life Insurance Company [RBCI]. The requirement, which was served on November 5, 2009, seeks "all information and documents relating to RBC Life Insurance Company's 10-8 plan holders," including names and social insurance numbers, business numbers, or trust numbers. The requirement was issued following claims by the Minister that this information was required in order to verify that these persons are in compliance with the Act. On November 19, 2009, RBCI moved to challenge Justice Pinard's order.

[4] On April 12, 2010, I granted two *ex parte* applications brought by the Minister for authorization to issue similar requirements to Industrial Alliance Pacific Insurance and Financial Services Inc. and Industrielle Alliance Assurance et Services Financiers Inc. [collectively IA]. The first of these requirements seeks "A listing of all loans outstanding […] contracted by individuals, corporations and/or trusts" relating to IA's 10-8 plan in a specified period, including: names; policy numbers; social insurance numbers, business numbers or trust numbers; amounts owing on any loans; the cash surrender value of their policies; and the interest on the loans for each 10-8 plan holder. The second requirement seeks "Une liste de tous les prêts […] souscrit par toute personne

physique, fiducie et/ou compagnie, faisant l'objet de la Stratégie 10-8" in a specified period. On April 30, 2010, IA moved to challenge both of my orders.

[5] Justice Richard Mosley issued an order authorizing a requirement to BMO Life Assurance Company [BMO] on June 7, 2010. The requirement seeks "all information and documents" in a specified period pertaining to BMO's 10-8 plan holders. On July 14, 2010, BMO moved to challenge Justice Mosley's order.

[6] At the same time that BMO was served with the requirement authorized by Justice Mosley's order, it was also served with a requirement issued without judicial authorization which sought "all information and documents […] relating to BMO Life Assurance Company's (formerly AIG Life Insurance Company of Canada) 10-8 Investment Plans" during a specified period. This requirement was challenged by way of an application for judicial review which BMO commenced on July 12, 2010. Although the parties' joint submissions address this application together with the four motions described above, the application will be dealt with in separate reasons.

[7] All of the requirements concern insurance leveraging strategies for high net worth individuals referred to as "10-8 plans." A 10-8 plan involves two essential elements: a life insurance policy that includes an investment account, and a loan which is secured by the life insurance policy in an amount equal to the balance of the investment account. The term "10-8 plan" refers to the interest rates applicable to these elements, as the policy-holder pays 10% interest on the loan and receives an 8% return on the investment in the life insurance policy. The 10-8 plan creates a tax

benefit because the 8% interest paid to the client is tax-exempt as part of a life insurance policy, and the 10% interest payable on the loan may be tax-deductible if it is used to produce income.

[8] Each of the Insurers provided the Minister with information and documents relating to their 10-8 plans, although BMO did not provide this information until after it was served with the two requirements. Each of the Insurers also refused to provide the Minister with names or other identifying information relating to its 10-8 plan holders. The Minister therefore initiated the *ex parte* applications described above to seek authorization to issue the various requirements in an effort to obtain information relating to the identities of 10-8 plan holders. I note, however, that each of the requirements is considerably more broad than merely seeking the identifies of the Insurers' 10-8 plan holders in a given period.

[9] On February 24, 2010, Prothonotary Martha Milczynski issued an order pursuant to Rule 54 of the *Federal Courts Rules* requiring the Minister to produce all relevant documents related to Justice Pinard's order. Prior to Prothonotary Milczynski's order, the Minister had refused to produce anything other than certain documents that RBCI had created and provided to the Minister, as well as a news article and a publicly available presentation about 10-8 plans. The Minister refused to disclose any other documents on the basis that they were privileged or irrelevant, failing even to produce the documents to her counsel for review. Prothonotary Milczynski disagreed, finding that "The Court, [sic] and RBCI need to know all the facts that were within the Minister's knowledge at the time of the hearing. […] The information sought is relevant to the issue of whether the Minister made full and frank disclosure at the time the *ex parte* application was made." Prothonotary

Milczynski therefore ordered the Minister to produce her file to RBCI and awarded RBCI its costs of the motion.

[10] Following Prothonotary Milczynski's order, the Minister made further disclosure to RBCI. However, the Minister continued to refuse to produce certain documents – namely, documents surrounding an Advanced Income Tax Ruling Request [ATR] made by another insurer regarding its 10-8 plan and internal discussions relating to the consideration of the ATR by the General Anti-Avoidance Rule Committee [GAAR Committee], as well as the questionnaire which the Minister had developed to send to 10-8 plan holders. The Minister refused to produce these documents, again claiming privilege and that they were not relevant to the motion.

[11] An ATR is a publicly available document issued by CRA. Generally, the purpose of an ATR is to seek guidance from CRA as to how it will apply the provisions of the Act in a specific context. This ATR, which was submitted by a third party insurer in 2007, provided detailed information about the submitter's proposed 10-8 plan and sought to determine whether the proposed plan complied with the Act. In contrast to a technical interpretation in which CRA addresses a hypothetical scenario, an ATR provides a specific and concrete scenario for the CRA to consider.

[12] This particular ATR was considered by the GAAR Committee, a specialized committee within CRA Rulings. The GAAR Committee assesses the potential application of the GAAR, an exceptional provision that allows CRA and the Minister to address abusive tax avoidance behaviour. GAAR can only be used as a last resort where no other provisions of the Act apply. After examining

the ATR, the GAAR Committee concluded that the proposed 10-8 plan was likely in compliance with the Act and did not believe that the GAAR could be successfully applied.

[13] In light of the Minister's continued refusal to produce documents relating to the GAAR Committee's consideration of the ATR, the Insurers brought a second disclosure motion. On January 13, 2011, Prothonotary Roza Aronovitch ordered the Minister to produce the above described documents, finding that "The Minister may wish to argue at the hearing on the merits that the documents sought to be produced by way of the direction to attend are not relevant, however, it is not open for argument at this juncture, as that determination has already been made."

[14] Following Prothonotary Aronovitch's order, the Minister produced the documents in question and from these documents a different picture emerges. For the reasons set out below, these documents establish that the Court was not in a position to appreciate the full context in which the Minister brought the *ex parte* applications and the orders must therefore be cancelled.

[15] The four motions were consolidated along with BMO's application on January 13, 2011. The hearing was based on a joint record and joint written submissions from both parties. These reasons will address the four motions brought by the Insurers.

Part II – The Evidence

[16] The evidence in each of the *ex parte* applications consisted of the following:

- In the RBCI application, an affidavit of Randy Jacobs, CRA officer, stating that "CRA is seeking to verify the compliance with the obligations and duties under the *Income Tax Act* of certain taxpayers who are clients of [RBCI] and who participate in […] the '10-8 plan'" and that "The CRA is not aware of the identity of the RBC

Insurance policyholders who have participated in the [10-8 plan]. The Minister seeks to determine whether the RBC Insurance policyholders who have participated in the [10-8 plan] have complied with their duties and obligations under the *Income Tax* [sic];"

- In the IA applications, two nearly identical affidavits of Michel Lévesque, CRA officer, both stating that "Depuis 2008, l'ARC a entrepris de vérifier si les contribuables qui ont souscrit comme clients aux produits généralement connus sous le nom de « programmes 10/8 » auprès de compagnies d'assurance ont respecté quelque devoir ou obligation prévu par la *Loi de l'impôt sur le revenu*" and that "les informations recherchées et décrites au paragraphe 11 de ma dénonciation serviront à vérifier si chacune des personnes physiques, fiducies ou compagnies ayant participé à la Stratégie 10/8 décrite aux sous-paragraphes 9I, 9II, 9III A. à J. inclusivement ont respecté quelque devoir ou obligations prévu par la LIR;"
- And, in the BMO application, an affidavit of Linda Szeto, CRA officer, stating that "I am seeking to verify the compliance with the obligations and duties under the *Income Tax Act* of certain taxpayers who are clients of BMO Life who participate in the 10-8 program," that "The CRA is currently examining the 10-8 program offered by certain insurance companies, including BMO Life, to their policyholders," and that "In order to verify if the unknown policyholders […] who have participated in the 10-8 program have complied with their duties and obligations under the *Income Tax Act*, the Minister requires BMO Life to provide [the information listed in the requirement]."

[17] However, a significant amount of additional evidence was disclosed following the orders of Prothonotary Milczynski and Prothonotary Aronovitch.

[18] The following evidence was disclosed in response to Prothonotary Milczynski's order:

- A ruling dated December 6, 2004 in response to an inquiry regarding the deductibility of the interest paid on the loan, which concluded that "Apart from the issue of reasonableness [of the interest rate], as it would seem that this type of arrangement is not in accord with the purpose and spirit of the provisions in the Act related to exempt insurance policies we have referred this matter to the Department of Finance for their consideration;"
- E-mail correspondence between various individuals at the Canada Revenue Agency, including the following statements:
    - While discussing the strategy of using targeted audits to alert the insurance industry to its concerns regarding 10-8 plans, "We should make sure we have some technical basis supporting our concerns before we embark on this project, otherwise we could look pretty bad. […] we better back up our concerns with real effective and timely

action" and that "Finance has been aware that there are a number of issues with the policyholder legislation. About 8-9 years ago they started to look into revamping policyholder tax policy (we attended the meetings) but it didn't get off the ground (too big a project) […] it looks like policyholder reform in [sic] now being reconsidered." [my emphasis]

- Upon learning that insurance governance bodies were receiving inquiries from insurers seeking clarification as to the Canada Revenue Agency's interest in and concerns with 10-8 plans, "This is all good. In fact, I'm delighted. Policyholder taxation is an area long overdue for attention;"

- In instructions to front-line auditors at the launch of the 10-8 plan audit program, "You should put together all the facts. You must be able to answer the following questions. You will notice that this does not require knowing the names of the participants;" and

- In an update on the progress of the 10-8 plan audit project, "[redacted] did provide the names of the participants and we chose 20 files and started a test audit."

[19] The following additional evidence was disclosed following Prothonotary Aronovitch's order on the second disclosure motion:

- A memorandum from F. Lee Workman, manager of the Charitable and Financial Institution Sectors, to the GAAR Committee which states the following:

    - "any loans under the [collateral loan facility] will not be 'policy loans' as defined in subsection 148(9), the assignment of the policy as security for the loans under the [collateral loan facility] will not be a disposition of an interest in the policy by virtue of paragraph (f) of the definition of 'disposition' in subsection 148(9), and provided the loans to be advanced by the insurer to the policyholder under the [collateral loan facility] will be borrowed money for the purposes of paragraph 20(1)(c) the interest paid on the [loan] advances will be deductible by the policyholder;"

    - "the only manner in which the tax benefits to be realized the [sic] proposed transactions might be challenged is by denying a portion of the interest the policyholder claims under paragraph 20(1)(c) on the basis that the interest rate of 10% is not reasonable;"

    - "the exempt policy can reasonably be said to have been purchased primarily for insurance purposes (and investment purposes to the extent permitted by the 'exempt policy' rules);"

- "The entering into of the [collateral loan facility], in order to obtain a loan from the insurer, can reasonably be said to have been undertaken by the policyholder, primarily to obtain financing;"

- "It is the fact that the borrowing is at an annual rate of 10% that might be said to have not been undertaken for a bona fide non-tax purpose as the rate is probably higher than the policyholder would likely be willing to pay on a borrowing [sic] from a bank where a policy has been assigned as collateral. The reasonability of the 10% rate is not a GAAR issue however;"

- "the collateral assignment of the policy to the insurer as security for the loan is an ordinary commercial transaction;"

- "given that whether a transaction or a series of transactions were arranged primarily for a non-tax purpose is a question of fact, it may be difficult to convince a court that the series of transactions is an avoidance transaction;"

- "the Department of Finance Explanatory Notes that were released with section 245, state that 'Subsection 245(3) does not permit the "re-characterization" of a transaction for the purposes of determining whether or not it is an avoidance transaction. In other words, it does not permit a transaction to be considered an avoidance transaction because some alternative transaction that might have achieved an equivalent result would have resulted in higher taxes.'"

- "the fact that the 8% rate of return being earned on the [collateral loan account] balance will be tax deferred is consistent with the words, object, spirit and purpose of section 12.2 and section 306 of the Regulations;"

- "the proposed series of transactions is not a misuse of the definition of 'policy loan' nor an abuse of the scheme of the Act with respect to policy loans;"

- "If the loan in question is not a 'policy loan' at law, then it would be difficult to argue that the proposed transactions are an abuse of the provisions of the Act dealing with policy loans;" and

- "we do not believe that the GAAR can be successfully applied to redetermine the implications of these transactions but it is our view that <u>there are policy concerns that should be considered with a view to proposing amendments</u>." [My emphasis]

- A memo from Margaret McCreary, Insurance Specialist, to the Manager of the GAAR & Technical Support Section stating that "Insurance policy tax legislation is out of date and has not kept up with the innovations in insurance products. […] For years, insurance companies took a conservative approach and tailored their products to fit the intent, if not the exact wording, of the legislation. […] the largest insurers are starting to lose a bit of their market share and they are concerned that the designs of the new products being offered by their competitors are no longer within the spirit of the legislation," and concluding that "a limited number of targeted audits will be extremely effective in putting the industry on notice that CRA is concerned about the direction they are headed;" and

- Additional email correspondence between individuals at the Canada Revenue Agency which contains the following statements:

    - Following a GAAR Committee meeting at which 10-8 plans were discussed, "The discussion was interesting and the decision was that CRA would not provide a ruling. It would send a message to the insurance industry that we are troubled with the arrangement. Finance certainly was concerned by the 10/8 arrangement from a policy perspective …" and "That response [to the ATR] is that we will not provide a ruling, that both the CRA and Finance believe this product to be contrary to tax policy with regard to exempt policies, it is not clear that the 10% interest meets the reasonable test in paragraph 20(1)(c) and we are leaving the door open to the possible application of GAAR until we have audited a specific case;"

    - In an update regarding the audit strategy for dealing with 10-8 plans, "I said we would be starting an audit blitz early next year on a number of insurers know [sic] to be offering the product with the objective of obtaining sample contracts to review the 20(1)(c) interest deductions and to consider the application of GAAR;" [My emphasis]

Part III – Relevant Statutory Provisions

[20] These motions concern section 231.2 of the Act:

231.2 (3) On ex parte application by the Minister, a judge may, subject to such conditions as the judge considers appropriate, authorize the Minister to impose on a third party a requirement under subsection 231.2(1) relating to an unnamed person or more than one unnamed person (in this section referred to as the "group") where the judge is satisfied by information on oath that	231.2 (3) Sur requête ex parte du ministre, un juge peut, aux conditions qu'il estime indiquées, autoriser le ministre à exiger d'un tiers la fourniture de renseignements ou production de documents prévue au paragraphe (1) concernant une personne non désignée nommément ou plus d'une personne non désignée nommément — appelée « groupe » au présent article —, s'il est convaincu, sur dénonciation sous serment, de ce qui suit :
(*a*) the person or group is ascertainable; and	*a*) cette personne ou ce groupe est identifiable;
(*b*) the requirement is made to verify compliance by the	*b*) la fourniture ou la production est exigée pour

person or persons in the group with any duty or obligation under this Act.	vérifier si cette personne ou les personnes de ce groupe ont respecté quelque devoir ou obligation prévu par la présente loi;
[…]	**[…]**
(5) Where an authorization is granted under subsection 231.2(3), a third party on whom a notice is served under subsection 231.2(1) may, within 15 days after the service of the notice, apply to the judge who granted the authorization or, where the judge is unable to act, to another judge of the same court for a review of the authorization.	(5) Le tiers à qui un avis est signifié ou envoyé conformément au paragraphe (1) peut, dans les 15 jours suivant la date de signification ou d'envoi, demander au juge qui a accordé l'autorisation prévue au paragraphe (3) ou, en cas d'incapacité de ce juge, à un autre juge du même tribunal de réviser l'autorisation.
(6) On hearing an application under subsection 231.2(5), a judge may cancel the authorization previously granted if the judge is not then satisfied that the conditions in paragraphs 231.2(3)(*a*) and 231.2(3)(*b*) have been met and the judge may confirm or vary the authorization if the judge is satisfied that those conditions have been met.	(6) À l'audition de la requête prévue au paragraphe (5), le juge peut annuler l'autorisation accordée antérieurement s'il n'est pas convaincu de l'existence des conditions prévues aux alinéas (3)*a*) et *b*). Il peut la confirmer ou la modifier s'il est convaincu de leur existence.

Part IV – Issues

[21] There are three issues before the Court on these motions:

1. Did the Minister fail to make full and frank disclosure in the *ex parte* applications?
2. Were the requirements obtained for the purpose of verifying compliance with the Act?

3. Does section 231.2(3) of the Act unjustifiably infringe section 8 of the *Charter of Rights and Freedoms*?

Part V – Discussion

1. *Full and Frank Disclosure*

i. The law

[22] Given the *ex parte* nature of the applications, the Applicant had a duty to make full and frank disclosure to the Court. It is well established that this burden requires the party in an *ex parte* hearing to present all material facts, even if those facts are adverse to its case.

[23] This Court was faced with a similar statutory provision in *Canada (Commissioner of Competition) v Labatt Brewing Co et al*, 2008 FC 59, 323 FTR 115. In that context, Justice Anne Mactavish noted that, in *ex parte* proceedings, the "normal checks and balances of the adversary system" are absent, and that the Court is therefore "at the mercy" of the party seeking *ex parte* relief (at paras 23 to 24). She also noted that "There is no situation more fraught with potential injustice and abuse of the Court's powers than an application for an *ex parte* injunction" (*Watson v Slavik*, in *Labatt*, above, at para 24). This potential injustice is the reason why the party seeking *ex parte* relief "must inform the Court of any points of fact or law known to it which favour the other side" (*Friedland* in *Labatt*, above, at para 25).

[24] As Justice Mactavish noted in *Labatt*, above, this duty of full and frank disclosure is crucial to the proper exercise of judicial discretion:

> Section 11 of the *Competition Act* provides for independent judicial oversight with respect to the extensive investigative powers granted

> to the Commissioner under the *Competition Ac*t. To this end, section 11 does not mandate that the Court act as a mere "rubber stamp" […]
>
> I agree that the Court must indeed be satisfied that the two statutory conditions precedent to the granting of a production order have been met […] However, in order to properly exercise the discretion conferred on the Court by section 11 of the *Competition Act*, and for the Court to be able to control its own processes, and to guard against the abuse of those processes, the Court must also be fully apprised of the relevant circumstances surrounding the request. [At paras 50-51]

[25] My colleague Justice Luc Martineau also considered a jeopardy order issued pursuant to the Act in *Canada (National Revenue) v Robarts*, 2010 FC 875, 374 FTR 87. In that decision, Justice Martineau noted that:

> In all *ex parte* matters the applicant is obliged to draw to the attention of the Court all facts in issue, even those which it considers unhelpful or inconvenient, and all relevant caselaw. […] Indeed, full and frank disclosure requires that the Minister disclose "what might reasonably be regarded as [known] weaknesses". […]
>
> While the omission [in the Minister's disclosure] was apparently made with no malicious intent, it severely undermines the *ex parte* application that was made by the Minister. [At paras 35 and 41]

[26] The Federal Court of Appeal considered the disclosure obligation in section 231.2 proceedings in *R v Derakhshani*, 2009 FCA 190, 2010 DTC 5043. In that decision, the unanimous Court noted the importance of full and frank disclosure to the judicial discretion captured in subsection 231.2(3):

> It is useful to recall that the existence of judicial discretion is <u>essential</u> to the constitutional validity of this type of provision, which is comparable to a seizure even when used in a regulatory (or even non-criminal) context […] It is this discretion, conferred upon an independent judge, which protects individuals from the damaging use of this kind of power and brings it in line with the requirements of section 8 of the *Canadian Charter of Rights and Freedoms* […]

> The fact that it may be possible to obtain the information using other means does not exclude the possibility that a requirement might be authorized, but that is information that must be provided to the judge. A judge must not be left in the dark on such an important point. [At paras 19 and 29, my emphasis]

[27] It seems to me that the most basic element of the duty to make full and frank disclosure is the disclosure to the Court of any information that has already been provided (see *Labatt*, above, at paras 93 and 94).

[28] Pursuant to Rule 399 of the *Federal Courts Rules*, the Court can quash an *ex parte* order where it was issued based on "misleading, incomplete, or incorrect" facts (see *Canada (Commissioner of Competition) v Air Canada*, [2001] 1 FC 219, 186 FTR 48 at para 14). Although the *ex parte* applications were brought under section 231.2(3) of the Act, Rule 399 nonetheless applies (see *Air Canada*, above, at para 5).

[29] However, an order will not automatically be cancelled because of any breach of this duty. An *ex parte* order will only be disturbed where non-disclosure is material and must be such that, had the information been disclosed, it would have affected the exercise of the *ex parte* judge's discretion (see *Labatt*, above, at paras 31 and 98).

[30] The Court retains the discretion to continue an *ex parte* order despite flawed disclosure:

> [I]t is important to keep in mind that the reason for the disclosure requirement is firstly to deprive the person who has not observed the rule of an advantage improperly obtained and secondly to act as a deterrent to ensure that persons who make *ex parte* applications realize that they have a duty of disclosure and that they appreciate the consequences if they fail in that duty.

> […] In exercising its discretion, the court should consider the extent of the culpability with regard to the non-disclosure, and the importance and significance of the matters that were not disclosed to the court to the outcome. [*Sherwood Dash Inc v Woodview Products Inc*, [2005] OTC 1061, 2005 at paras 39-40]

ii. Parties' Submissions

[31] The Insurers submit that the Minister failed to make full and frank disclosure in the *ex parte* applications. She was required to present a balanced view to the Court and to disclose any facts which could operate against her, citing several decisions including *Robarts*, above, at para 35 and *Labatt*, above, at paras 25-26.

[32] Further, the Minister cannot justify the lack of disclosure on the basis that the information is immaterial,

> The duty extends to placing before the court all matters which are relevant to the court's assessment of the application, and it is no answer to a complaint of non-disclosure that if the relevant matters had been placed before the court, the decision would have been the same. The test as to materiality is an objective one, and it is not for the applicant or his advisers to decide the question; hence it is no excuse for the applicant subsequently to say that he was genuinely unaware, or did not believe, that the facts were relevant or important. [Steven Gee, *Mareva Injunctions and Anton Piller Relief*, 3rd ed. (London: FT Law & Tax, 1995) at p 98, in *Labatt*, above, at para 31]

[33] The Insurers also note that it is no excuse for a party to say that it did not intend to mislead the Court with its flawed disclosure, citing *R v Morelli*, 2010 SCC 8, [2010] 1 SCR 253 at para 59.

[34] The Insurers compare the orders under review to the power of the Commissioner of Competition to compel disclosure with judicial authorization, noting that this Court has held that,

> [T]he Court must indeed be satisfied that the two statutory conditions precedent to the granting of a production order have been met – namely that there is a section 10 inquiry under way, and that the respondent has information that is relevant to the inquiry – prior to granting a production order under the Act. However, in order to properly exercise the discretion conferred on the Court by section 11 of the *Competition Act*, and for the Court to be able to control its own processes, and to guard against the abuse of those processes, the Court must also be fully apprised of the relevant circumstances surrounding the request. [*Labatt*, above, at para 51]

[35] Finally, the Insurers argue that the Court's discretion to continue the *ex parte* orders despite the flawed disclosure is exceptional and limited, and that it should not be exercised simply because the orders would probably have been granted had the disclosure been complete, citing *Sherwood Dash*, above, at paras 37-39.

[36] Thus the four *ex parte* orders must be cancelled because the Minister failed to make full and frank disclosure. In particular, the Minister had a duty to disclose the documents and emails surrounding the GAAR Committee's consideration of the ATR and the Canada Revenue Agency's plan to audit 10-8 plan holders, as well as the significant volume of information about 10-8 plans that had already been disclosed to the Minister before the *ex parte* applications.

[37] The Minister, on the other hand, claims that the *ex parte* orders were sought for the purpose of verifying whether the 10-8 plan holders are in compliance with the Act, and that the GAAR Committee documents and internal discussions are immaterial to this end.

[38] The Minister further submits that, in order for the *ex parte* orders to be set aside, the Insurers must demonstrate that the disclosure made at the hearing was "misleading, inaccurate or

incomplete," citing *Labatt*, above, at para 34. She also claims that the Insurers must show that, but for the lack of disclosure, the orders would not have been made, citing *Re Papa*, 2009 FC 49, [2009] 4 CTC 93 at paras 21-23. Therefore the Insurers have not met this high burden and that I should therefore decline to exercise my discretion to cancel the orders.

iii. Analysis

[39] In my opinion, the Minister fell short of her obligation to make full and frank disclosure in two respects. First, she did not disclose the significant volume of information that the Insurers had already provided to her before the *ex parte* applications were commenced. These documents provided a great deal of information about the Insurers' 10-8 plans, and with the exception of the identities and personal information of the Insurers' 10-8 plan holders, responded fully to the requirements for which the Minister sought *ex parte* authorization.

[40] The second, and more troubling, omission is the Minister's failure to disclose internal documents and information suggesting that the 10-8 plans comply with the letter of the Act, if not with its spirit. These documents – the bulk of which were only disclosed to the Insurers after two separate motions – are undoubtedly material and, had they been disclosed to the Court, could certainly have affected the outcome of the *ex parte* applications.

[41] More specifically, the evidence disclosed following the Prothonotaries' orders include the following material facts which were not disclosed to the Court on the *ex parte* applications:

a) The fact that the Department of Finance had refused to amend the Act to address the outdated policyholder provisions;
b) The ATR, which provided a great deal of information regarding a specific 10-8 plan for the express purpose of determining whether the plan complied with the Act;

c) The fact that the GAAR Committee had determined that the 10-8 plan likely complied with the letter of the Act, if not with its spirit; and

d) The decision to "send a message to the industry" by refusing to answer the ATR and to take measures to "chill" 10-8 plan business, in part by undertaking an "audit blitz".

[42] The fact that the Minister decided to undertake an "audit blitz" to "send a message to the insurance industry" is clearly relevant to the balancing exercise that the Court has to undertake in deciding whether or not the orders should be granted. For the Court to be able to control its own processes and to guard against any abuses, it must be fully apprised of all relevance circumstances surrounding the request (see *Labatt*, above, at paras 47 and 51 to 52).

[43] Although subsection 231.2(6) of the Act does not explicitly state that the Court can cancel an authorization previously issued based on a lack of disclosure, I find that Rule 399 of the *Federal Courts Rules* gives me the inherent power to do so (see *Air Canada*, above, at para 5). The Court must retain the authority to control its own processes and to remedy any abuse that results from an *ex parte* order granted based on incomplete or misleading disclosure.

[44] I note as well that, had the Minister disclosed these material facts on the *ex parte* applications, the orders might still have been granted. However, I would have had many questions for the Minister about the information she had already received and CRA's position on the 10-8 plans and her goal in auditing 10-8 plan holders. As was the case in *Derakhshani*, above, the evidence omitted from the *ex parte* applications does not exclude the possibility that the requirements might be authorized, but the information must be before the judge. Otherwise the *ex parte* applications become a rubber stamp exercise and the Court cannot effectively exercise its discretion.

[45] I am satisfied that this information was material and that, because of its omission from the *ex parte* applications, the Court was not in a position to make an informed decision. As a result, the orders must be cancelled.

2. *Purpose of the Requirements*

i. The law

[46] Section 231.2(3)(*b*) requires that the Minister's purpose in seeking to issue a requirement concerning unnamed persons be to "verify compliance by the person or persons in the group with any duty or obligation under this Act." This purpose requirement is one of two conditions of which the presiding judge must be satisfied in order for the authorization to be granted, the other condition being that the group must be ascertainable.

[47] The purpose requirement in subsection 231.2(3)(*b*) of the Act has not been the subject of much adjudication. It appears that this dearth of judicial consideration results from the Minister's broad audit powers under the Act:

> Accordingly, the Minister of National Revenue must be given broad powers in supervising this regulatory scheme to audit taxpayers' returns and inspect all records which may be relevant to the preparation of these returns. The Minister must be capable of exercising these powers whether or not he has reasonable grounds for believing that a particular taxpayer has breached the Act. Often it will be impossible to determine from the face of the return whether any impropriety has occurred in its preparation. A spot check or a system of random monitoring may be the only way in which the integrity of the tax system can be maintained. [*McKinlay*, above, at para 36]

[48] The most direct ruling on the purpose requirement in subsection 231.2(3)(*b*) comes from Justice Johanne Gauthier in *Minister of National Revenue v Greater Montréal Real Estate Board*, 2006 FC 1069, 303 FTR 29: "The language of the Act is clear. The information and documents requested must be for the purpose of verifying whether the persons being investigated have complied with some duties or obligations set out in the Act. The courts have held that the information must be "relevant" to the inquiry" (at para 61).

[49] In *Nadler Estate v Canada (Attorney General)*, 2005 FC 935, [2005] 4 CTC 7, Justice Johanne Gauthier noted that "The Act does not require that the third party from whom the information is sought be given any details as to the purpose of the Requirement" (at para 9) and was satisfied that the Requirement at issue was valid because "The Requirement properly indicates the name of the taxpayer concerned, refers to the appropriate enabling provision and gives a description of the information required which is sufficient to enable Canada-Israel Securities Ltd. to prepare its response" (at para 9).

[50] Similarly, I held in *Ministre du Revenu national v Banque Toronto Dominion*, 2004 FC 169, 253 FTR 90 that:

> It is not the function of a financial institution to which the requirement is sent to decide on the relevance of the information sought under that requirement. It noted [sic] that the procedure created under subsections 231.2(2) and (3) of the I.T.A. has the twofold function of requiring the Canada Customs and Revenue Agency to justify the obtaining of the information required when the requirement relates to unnamed persons and allowing the financial institution to which the requirement is sent to comply with its obligations to its clients. [At para 15]

[51] However, the Minister may have more than one purpose in issuing requirements. Where a secondary purpose such as the audit of a named taxpayer is sufficiently connected to the enforcement purpose relating to the unnamed persons, subsection 231.2(3)(b) is still satisfied (see *Whitewater Golf Club Inc v Minister of National Revenue*, 2009 FC 739, [2009] 6 CTC 51 at paras 15 to 16).

ii. Parties' Submissions

[52] The Insurers submit that the requirements were issued for an improper purpose: namely, a fishing expedition intended to chill their 10-8 plan business. They claim that the Minister failed to establish in the *ex parte* applications that the requirements were necessary to verify compliance with the Act and note that the Minister has not alleged any specific breach of the Act.

[53] The Insurers argue that the Minister was required to act in good faith in exercising her powers under section 231.2 of the Act, citing *Greater Montréal Real Estate Board*, above, at para 48.

[54] Further, section 231.2(3) requires the Minister to show that the requirements are necessary to ensure compliance, again citing *Greater Montréal Real Estate Board*, above. They claim that the requirements were not actually necessary to verify that the 10-8 plans were in compliance with the Act, and that they had already provided enough information to allow the Minister to determine that their 10-8 plans comply with the Act without conducting any audits.

[55] The Minister submits that nothing in the record contradicts the evidence in the *ex parte* applications that the requirements are needed to conduct targeted audits of 10-8 plan holders and ensure their compliance with the Act. She is not required to justify her decision to audit, and that an audit program that targets 10-8 plan holders is not evidence of bad faith.

iii. Analysis

[56] As stated above, I am satisfied that the orders must be quashed solely because of the incomplete disclosure. However, I will make the following comments about the question of the Minister's true purpose in issuing the requirements since the issue was fully argued before me.

[57] There is no merit to the Insurers' claim that the Minister was required to identify a specific section of the Act that she believed had been breached. The Supreme Court held in *McKinlay*, above, that "The Minister must be capable of exercising these [audit] powers whether or not he has reasonable grounds for believing that a particular taxpayer has breached the Act. Often it will be impossible to determine from the face of the return whether any impropriety has occurred in its preparation" (at para 36). The Minister was not, therefore, required to give more detail as to the purpose of the Requirements as long as the information is "relevant" to the verification of compliance with a duty of obligation under the Act. Subsection 231.2(3) does not require the Minister to show that there are reasonable grounds to believe that there is failure to comply with a provision of the Act.

[58] At the hearing, the Insurer's conceded that the Minister had a valid audit purpose in issuing the requirements, but argued that this valid purpose was extraneous to her primary goal, which was to chill their 10-8 plan business. I agree.

[59] I do not believe that the Minister's central purpose in issuing the requirements is sufficiently tied to her valid audit purpose. Contrary to the Minister's pretension, I did find evidence that the targeted audit of specific 10-8 plan holders was not only done to test the reasonableness of the 10% payable interest rate or the possible application of the GAAR but to send a message to the industry. I am not satisfied that the Minister's attempt to "send a message" is a valid enforcement purpose such that subsection 231.2(3)(*b*) of the Act is satisfied or that this goal is sufficiently connected to the Minister's valid audit purpose.

[60] Moreover, I am not satisfied that the requirements are actually necessary for the Minister to verify compliance with the Act. The only evidence in the *ex parte* applications to the effect that the requirements were necessary consisted of bald assertions by the Minister's affiants, who apparently were not apprised of the context in which the applications were brought. Not only have the Insurers provided the Minister with a substantial amount of information, but RBCI has also provided her with the identities of certain of its 10-8 plan holders. Of course, it is not the role of the Court to question the Minister's decision to audit someone (see *Greater Montréal Real Estate Board*, above, at para 28). However the Minister cannot pretend that she is unable to audit any of the Insurers' 10-8 plan holders or to otherwise determine whether the 10-8 plans comply with the Act because that is simply not the case. Further, the ATR, although made by another insurer, provided sufficient

concrete information to allow the Minister to make a determination – and, in fact, she determined that the 10-8 plan likely complies with the Act.

[61] The Minister therefore was already in a position to assess the 10-8 plans and their compliance with the Act. Again, this begs the question of her true purpose in bringing the *ex parte* applications.

[62] If, as the Minister's delegates claimed in the internal emails, "Policyholder taxation is an area long overdue for attention," then the manner in which it should receive this attention is through legislative amendment. It is a misuse of the Minsiter's powers – powers which the Courts have repeatedly called "intrusive" – to use section 231.2 to pursue policy objectives rather than to enforce tax obligations. It was not open to the Minister to seek *ex parte* authorization under the pretence of verifying compliance with the Act when her true purpose was to achieve through audits what the Department of Finance refused to do through legislative amendment.

3. *Constitutionality of Section 231.2(3) of the Act*

[63] The Charter issue is raised in the specific context of these motions and is intertwined with the first two issues. In light of my above conclusion that ex parte orders must be cancelled, it is unnecessary for me to address this issue.

Part VI – Conclusion

[64] As a result of the incomplete disclosure in the *ex parte* motions, these motions are allowed and the *ex parte* orders are cancelled with costs.

JUDGMENT

THIS COURT ORDERS that the motions are allowed and the *ex parte* orders are cancelled with costs.

"Danièle Tremblay-Lamer"
Judge

FEDERAL COURT

SOLICITORS OF RECORD

DOCKET:	T-1619-09, T-484-10, T-485-10 and T-879-10
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DATED:	01 NOVEMBER 2011

APPEARANCES:

Margaret Nott Samantha Hurst Ian Demers Pierre Lamothe Christopher Bartlett	FOR THE APPLICANT
Mahmud Jamal Pooja Samtani David Mollica Hermant Tilak	FOR THE RESPONDENT

SOLICITORS OF RECORD:

Myles J. Kirvan Deputy Attorney General of Canada Department of Justice Tax Law Services Section Ontario Regional Office Toronto, Ontario	FOR THE APPLICANT
Osler, Hoskin & Harcourt LLP Box 50, 1 First Canadian Place Toronto, Ontario	FOR THE RESPONDENT