CANADIAN INTERNATIONAL TRADE TRIBUNAL
TRIBUNAL CANADIEN DU COMMERCE EXTÉRIEUR

Ottawa, Monday, April 6, 1992

Appeal No. AP-89-264

IN THE MATTER OF an appeal heard on October 2 and 3 and December 2, 1991, under section 81.19 of the *Excise Tax Act*, R.S.C., 1985, c. E-15, as amended;

AND IN THE MATTER OF a decision of the Minister of National Revenue dated October 20, 1989, relating to a notice of objection served under section 81.15 of the *Excise Tax Act*.

BETWEEN

ALPHA FUELS LIMITED **Appellant**

AND

THE MINISTER OF NATIONAL REVENUE **Respondent**

DECISION OF THE TRIBUNAL

The appeal is allowed. The Tribunal declares that the appellant paid federal sales and excise taxes pursuant to the *Excise Tax Act* by virtue of having paid its supplier on a "tax-paid" basis pursuant to the Alternative Tax Accounting Method for Combined Retailer - Wholesalers.

Charles A. Gracey
Charles A. Gracey
Presiding Member

Sidney A. Fraleigh
Sidney A. Fraleigh
Member

W. Roy Hines
W. Roy Hines
Member

Robert J. Martin
Robert J. Martin
Secretary

365 Laurier Avenue West
Ottawa, Ontario K1A 0G7
(613) 990-2452 Fax (613) 990-2439

365, avenue Laurier ouest
Ottawa (Ontario) K1A 0G7
(613) 990-2452 Téléc. (613) 990-2439

CANADIAN INTERNATIONAL TRADE TRIBUNAL | TRIBUNAL CANADIEN DU COMMERCE EXTÉRIEUR

UNOFFICIAL SUMMARY

Appeal No. AP-89-264

ALPHA FUELS LIMITED **Appellant**

and

THE MINISTER OF NATIONAL REVENUE **Respondent**

Whether the appellant purchased fuel from its supplier on a tax-paid basis pursuant to the Alternative Tax Accounting Method for Combined Retailer - Wholesalers. Whether such payment discharges the appellant's tax liability. Whether the appellant is a deemed manufacturer of diesel fuel.

HELD: *The appeal is allowed. The appellant purchased fuel from its supplier on a tax-paid basis and, in so doing, discharged its tax liability.*

Place of Hearing:	*Ottawa, Ontario*
Dates of Hearing:	*October 2 and 3, and December 2, 1991*
Date of Decision:	*April 6, 1992*
Tribunal Members:	*Charles A. Gracey, Presiding Member* *Sidney A. Fraleigh, Member* *W. Roy Hines, Member*
Counsel for the Tribunal:	*Clifford Sosnow*
Clerk of the Tribunal:	*Janet Rumball*
Appearances:	*Patricia Conway, for the appellant* *Michael Ciavaglia, for the respondent*

365 Laurier Avenue West
Ottawa, Ontario K1A 0G7
(613) 990-2452 Fax (613) 990-2439

365, avenue Laurier ouest
Ottawa (Ontario) K1A 0G7
(613) 990-2452 Téléc. (613) 990-2439

CANADIAN INTERNATIONAL TRADE TRIBUNAL | TRIBUNAL CANADIEN DU COMMERCE EXTÉRIEUR

Appeal No. AP-89-264

ALPHA FUELS LIMITED **Appellant**

and

THE MINISTER OF NATIONAL REVENUE **Respondent**

TRIBUNAL: CHARLES A. GRACEY, Presiding Member
SIDNEY A. FRALEIGH, Member
W. ROY HINES, Member

REASONS FOR DECISION

This is an appeal under section 81.19 of the *Excise Tax Act*[1] (the Act) from a decision of the Minister of National Revenue (the Minister) issued on October 20, 1989, with respect to sales and excise taxes on gasoline and diesel fuel sold by the appellant to its customers during the period February 1, 1983, to July 31, 1986.

During that period, the appellant was deemed to be a manufacturer of gasoline and diesel fuel pursuant to paragraph 2(1)(*e*) of the Act and was issued two manufacturer and sales tax licences as a retailer-wholesaler of gasoline and of diesel fuel. As a deemed manufacturer, the appellant was entitled to purchase gasoline and diesel fuel exempt from sales or excise tax by virtue of paragraph 21(3)(*d*) and subsection 27(2) of the Act as it then was.

The appellant, however, elected to operate under the Alternative Tax Accounting Method for Combined Retailer - Wholesalers (Alternative Tax Accounting Method) and claims to have purchased its gasoline and diesel fuel on a sales and excise tax-paid basis. Pursuant to this provision, the appellant would only be required to account for taxes on its markup to retailers. The appellant had made this election prior to 1983 and had been audited once while operating under that method.

Prior to January 1984, the appellant had been purchasing its fuel supplies from Petro-Canada Ventures (Petro-Canada) on a tax-paid basis. In January 1984, the appellant commenced a transition from Petro-Canada to Can-Am Liquids Corp. Ltd. (Can-Am) and, for several weeks, purchased its fuel supplies from both suppliers.

On November 12, 1986, following an audit, the appellant received a notice of assessment for unpaid federal sales and excise taxes on the sale and/or purchase of gasoline and diesel fuel covering the period February 1, 1983, to July 31, 1986. On December 23, 1986, the appellant was assessed in the same manner for the period August 1, 1986, to October 31, 1986.

Notices of objection to these two assessments were served by the appellant on February 2, 1987, and March 17, 1987, respectively. On October 20, 1989, notices of decision concerning the assessments were issued, allowing the objection in part, but confirming the balance as a

1. R.S.C., 1985, c. E-15, as amended.

365 Laurier Avenue West
Ottawa, Ontario K1A 0G7
(613) 990-2452 Fax (613) 990-2439

365, avenue Laurier ouest
Ottawa (Ontario) K1A 0G7
(613) 990-2452 Téléc. (613) 990-2439

tax liability. The appellant now appeals those reassessments to this Tribunal.

The appellant contends that it purchased its fuel supplies from Can-Am under the Alternative Tax Accounting Method, and, having done so, fulfilled its obligation to pay tax. Further, the appellant contends that, in respect to its purchases of diesel fuel, it was not a deemed manufacturer and was therefore not responsible for collecting and remitting federal sales or excise tax on its diesel fuel.

The issues arising out of this appeal are as follows:

1. Did the appellant purchase its diesel fuel and gasoline from Can-Am on a tax-paid basis pursuant to the Alternative Tax Accounting Method?

2. If the answer to question No. 1 is yes, has the appellant thereby discharged its sales tax liability pursuant to the Act?

3. If the answer to question No. 2 is no, is the appellant a deemed manufacturer of diesel fuel and thus not responsible for sales tax in respect of sales of diesel fuel?

The first witness for the appellant was its president, Mr. Michael A. Krula. He testified that he had been in the business of distributing gasoline and diesel fuel to users and retailers since 1974. The preponderance of the sales of diesel fuel were to users, and most of the sales to retailers were of gasoline. The witness testified that his firm elected to use the Alternative Tax Accounting Method and purchased its fuel supplies from Petro-Canada on that basis. In early 1984, the appellant firm became dissatisfied with the payment terms imposed by Petro-Canada and sought an alternate supplier. Mr. Krula testified that he entered into discussions and price negotiations with Mr. Reginald H. Carr who had been sales representative for Alpha Fuels Limited (Alpha) at Petro-Canada, but who had become a sales representative for Can-Am. Alpha took delivery of fuel from Can-Am as early as January 20, 1984, several weeks before Alpha signed a purchase agreement with that firm.

The appellant argued, and the respondent contested, that Alpha purchased its fuel supplies from Can-Am on a tax-paid basis in accordance with the Alternative Tax Accounting Method just as it had been doing with Petro-Canada. The evidence is clear from invoices from both suppliers that during the period when Alpha was switching suppliers, the prices charged by the two suppliers were very similar. Counsel for the appellant submitted that since the amount of the federal sales tax was then 9 percent, a decrease of approximately that magnitude should have been apparent on the diesel purchases and a greater decrease, inclusive of the excise tax, should have been apparent on the price of gasoline if these fuels had been sold tax exempt.

In reality, decreases were observed, but were much less than might have been expected when one switched from buying on a tax-paid to a tax-exempt basis. The evidence of the appellant was that it switched suppliers in order to arrange more favourable payment terms and not for reasons of price. Counsel argued that it was inconceivable that the appellant would knowingly have negotiated an arrangement that meant it would be paying prices which, with the addition of the federal sales and excise tax, would result in final costs that averaged 2.31¢ to 2.80¢ per litre higher than it was simultaneously paying its other supplier. In point of fact, counsel argued that the slightly lower prices negotiated with Can-Am were consistent with that firm's eagerness to get into the market in that region.

Mr. Krula testified that all of his discussions with Mr. Carr, the agent for Can-Am, were on a tax-paid basis and, when called to testify, Mr. Carr agreed unequivocally. Mr. Carr also testified that he had authority to negotiate prices with Alpha on a "tax-in" or a "tax-out" basis and acknowledged that prices would have to be discussed on a "tax-in" basis in order to make meaningful price comparisons.

Mr. Carr was shown the sales agreement between Can-Am and Alpha dated March 16, 1984. This agreement included several price quotations, and Mr. Carr agreed that the prices were tax-paid prices.

Mr. Krula testified that neither he nor his associate, Mr. Frank Dundas (now deceased), ever supplied their manufacturer's licence to Mr. Carr. The licence was necessary to assure Can-Am that Alpha was licensed to receive tax-exempt (tax-out) inventory. Mr. Carr was unable to state where he got the licence, but it was established that it was possible to get a copy of it from Revenue Canada. However, Mr. Krula's denial that anyone at Alpha had supplied the licence to Can-Am was not rebutted.

A witness for the appellant, Mr. Bruce Thompson, the Executive Vice-President of Sipco Oil Limited, yet another supplier of fuels to the appellant, was called to testify as to industry practices. He testified that, where a sale is tax exempt, it is industry practice to so indicate by recording the licence number on the sales invoice. This is necessary, he testified, in order to avoid the liability for tax that would fall back on the seller if, in fact, the sale was not tax exempt. This is because the vendor has the responsibility, pursuant to the Alternative Tax Accounting Method, to ensure that the taxes are remitted. Mr. Thompson further testified that, if the sale was inclusive of tax, the general industry practice is to include the federal tax in the base price on the invoice and to enter the provincial road tax as a separate item. Despite this industry practice, evidence was adduced that none of the invoices sent to Alpha by Can-Am included the licence number or any other indication to establish that the sale was tax exempt. Mr. Thompson was shown a representative invoice from Can-Am to Alpha and expressed the opinion that, since there was no indication on the invoice that it was a tax-exempt sale, the price cited would include the federal sales and excise taxes.

Counsel for the respondent referred to the wording of the two contracts that Alpha had with Petro-Canada and with Can-Am, respectively, to illustrate that the latter could be distinguished from the former and, thereby, to confirm that the contract with Can-Am was on a tax-exempt basis. The relevant clauses are:

Petro-Canada

> 14. Any tax, duty, charge or fee, now or hereafter levied on the products sold hereunder or required to be paid or collected by the PARTNERSHIP shall be paid by PURCHASER in addition to the prices specified herein, and all such taxes, duties, charges or fees are excluded from the prices specified herein unless expressly included.

Can-Am

> 4. **Taxes** - If any tax, assessment or charge is imposed upon the products sold hereunder by governmental authority after the date of this contract, such charge shall be for the account of Buyer, it being understood that the prices stated herein are exclusive of all such taxes, assessments and charges.

Mr. Kewal Gupta, a senior excise auditor with Revenue Canada, Excise, performed an audit of the appellant firm in 1986. He testified that, during his first visit, he confirmed that Alpha was a manufacturer of fuel.

In the course of his investigation, Mr. Gupta met with Mr. Carr to verify that Alpha was buying from Can-Am on a tax-paid basis. He testified that Mr. Carr provided "three or four documents which proved that those things were on a tax-excluded basis." The first of these documents was a sales

agreement dated March 16, 1984. The face of the agreement cited several prices, but Mr. Gupta agreed that there was no indication whether the prices were tax included or not.

The second document he received from Mr. Carr was a sales agreement dated February 19, 1985, and this document did cite a price and did specify "plus applicable taxes." The document had the phrase "We hereby confirm sales to" overwritten with the word "INTERNAL." No evidence was provided that such a document was ever sent to Alpha, although the clear reading of this document was that Alpha was to remit the taxes to Can-Am.

The third document was a memorandum dated January 6, 1984, from Mr. Carr to Mrs. Gloria Williams in the Calgary office, instructing her to set up an account for Alpha and stating that sales of diesel fuel and gasoline were federal sales tax exempt as per enclosed copies of the "G" and "E" licences provided to him by Alpha. Despite stating that his discussions with Mr. Krula had always been on a tax-paid basis, Mr. Carr agreed that he had sent the above-noted memorandum, but offered no explanation for the evident inconsistency between his price negotiations with Mr. Krula and the instructions he gave to Mrs. Williams. The evidence before the Tribunal indicates that Mr. Carr did not send a copy of this memorandum to Alpha.

Further, the Tribunal does not ascribe probative value to this document. First, it is merely an internal document authorizing the setting up of an account and does not purport to be an agreement with or represent a sale to the appellant. Second, it is dated January 6, 1984, some two months prior to the actual agreement signed on March 16, 1984, between Can-Am and Alpha. Third, and most importantly, the first and second page of the memorandum of January 6, 1984, related to different time periods (i.e. post-January 6, 1984, and pre-December 1983) and different goods (i.e. diesel fuel and gasoline as opposed to propane). Mr. Carr did not clarify these discrepancies.

The evidence relating to the wording of paragraph 4 in the Can-Am "Terms and Conditions" document must, however, be further considered. It is the position of the respondent that the clause in question confirms that the agreement specifies the sales were to be made on a tax-exempt basis. The Tribunal is not so persuaded. While paragraph 4 is not conclusive, it certainly permits the acceptance of the meaning that the buyer is responsible for any <u>new</u> taxes, charges or assessments <u>after</u> the contract date.

Under cross-examination, it was established that Mr. Gupta had reviewed the notes relating to previous audits of the appellant firm and was aware that Alpha had been using the Alternative Tax Accounting Method. He agreed that he had seen no indication that Alpha had discontinued that method and agreed that the appellant would have to notify Revenue Canada before doing so. Mr. Gupta stated that he had seen no such notation in the appellant's file. Mr. Gupta agreed that when he reviewed the invoices from Can-Am, he did not find a single one that stated that the sale was tax exempt. Questioned about normal industry practice, he stated that he did not know because he had never done any other audit of a company in the petroleum industry.

Mr. Gupta agreed, under cross-examination, that he had reviewed the books of Can-Am to determine whether or not it had paid the taxes. Asked if he looked at the purchase price that Can-Am had paid for the product and the sale price to Alpha, Mr. Gupta replied that he had not.

Financial records were presented by counsel for the appellant to confirm that the appellant acted in a manner consistent with a belief that it was obtaining its supplies on a tax-paid basis. In the Tribunal's view, there was no evidence in the records of any significant decrease in selling prices that one would expect if the appellant was aware that its fuel purchases were on a tax-exempt basis and that it would have to charge the tax directly to its customers. Further, the financial records reveal an overhead cost of about 6¢ per litre, and the spread between the buying price and the selling price was

not large enough to include both this overhead and the taxes allegedly outstanding. Finally, evidence was presented to confirm that, throughout the period under review, the appellant calculated and remitted tax on the markup between its purchase cost and its selling price.

For all of the reasons that flow from the evidence adduced, the Tribunal is satisfied that Alpha did purchase its supplies from Can-Am throughout the audit period on a tax-included basis.

Given that Alpha purchased product on a tax-paid basis, the question the Tribunal must consider is whether the appellant, in so doing, discharged its tax liability. The respondent argues that even if Alpha did purchase product on a tax-paid basis, nevertheless, this was done pursuant to the Alternative Tax Accounting Method and, therefore, was not paid pursuant to the Act. The Tribunal disagrees with the respondent's position and concludes that Alpha has discharged its tax liability.

The Tribunal considers that the central point to consider is whether the total tax liability required to be paid by Alpha pursuant to the Act has changed as a function of the Alternative Tax Accounting Method. In the Tribunal's view, it has not. Indeed, the Minister is not arguing that Alpha is required to pay an amount different than that imposed pursuant to the Act. He is not saying: "Alpha, you got a tax break by using the Alternative Tax Accounting Method. You owe us more money." Thus, quantum is not in issue. The Minister is simply saying that he has not received a portion of the total tax liability imposed on Alpha. In this case, the amount at issue is the amount paid by Alpha to Can-Am.

According to the Act, Can-Am, a licensed manufacturer, is not required to pay tax when it sells product to Alpha, another licensed manufacturer. When Alpha sells product, it is required to pay tax on the sale price it charges to its customers. Alpha is required to pay that money directly to Revenue Canada. According to the Alternative Tax Accounting Method, Alpha's sales tax liability is split into two components: a taxable amount determined as a function of Can-Am's sale price to Alpha and a taxable amount determined as a function of Alpha's markup on the sale price it charges to its customers.

In other words, all that the Alternative Tax Accounting Method does is change the flow of the direction of tax monies. The Alternative Tax Accounting Method does not place a tax burden on Can-Am in the sense of requiring it to pay a tax that the Act otherwise does not impose. What the Alternative Tax Accounting Method does is establish Can-Am as a tax collector. Thus, the Alternative Tax Accounting Method establishes routes for the payment of sales tax liability that are consistent with the Act. If the Minister chooses, as a matter of policy, the routes through which sales tax monies are to be directed to Revenue Canada, it is not for the Tribunal to comment on the policy and state otherwise.

In view of the Tribunal's conclusion that the appellant has satisfied its tax liability pursuant to the Act, the Tribunal does not consider it necessary to determine whether the appellant is a deemed manufacturer of diesel fuel.

For all the foregoing reasons, the appeal is allowed.

The Tribunal wishes to make further comment on the position of the Minister that the Alternative Tax Accounting Method should be completely disregarded. The Tribunal considers that this position raises serious issues of fairness. While it is clear the Alternative Tax Accounting Method does not have the force of law, the testimony and the documentary evidence before the Tribunal make it clear that taxpayers like the appellant have been encouraged to use the Alternative Tax Accounting Method.

The Alternative Tax Accounting Method was widely promulgated throughout the industry and was designed for use by exactly the type of operation run by the appellant. Indeed, there never was any

question, throughout the hearing, of the appellant's entitlement to use the Alternative Tax Accounting Method. Finally, it is in the nature of the Alternative Tax Accounting Method that, when a party makes use of it, the taxpayer will have no means of assuring itself that the tax it paid has been remitted to Revenue Canada. As stated earlier, the effect of the Alternative Tax Accounting Method is to make the vendor the tax collector when agreement is reached with the purchaser that sales of fuel will be on a "tax-in" basis.

That being the case, the Tribunal considers it to be quite unreasonable to hold a taxpayer like the appellant responsible for the tax when it has paid the tax pursuant to an accepted tax accounting method and has no practical means of ensuring that the person to whom the monies have been paid has, in fact, remitted these amounts to Revenue Canada.

Charles A. Gracey
Charles A. Gracey
Presiding Member

Sidney A. Fraleigh
Sidney A. Fraleigh
Member

W. Roy Hines
W. Roy Hines
Member